



COMMENTARY



Decision Lowers Standard for Enforceability of Arb Clauses in Commercial Contracts



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arbitration provisions in the commercial context.



By Charles Dennen and Christopher Terlingo | April 10, 2023 at 01:00 PM

The New Jersey Appellate Division, in a recent decision, lowered the standard for enforceability of contractual arbitration provisions in the commercial setting, continuing a trend in New Jersey law of relaxing scrutiny of such provisions in the non-consumer or employment context. In *County of Passaic v. Horizon Healthcare Services*, (N.J. Super. Ct. App. Div. Feb. 8, 2023), the court held that a contractual arbitration provision that does not include an express waiver of the parties' right to seek relief in a court of law is nevertheless enforceable as between two sophisticated commercial parties of relatively equal bargaining power. This decision appears to be a departure from the contractual language that was previously deemed by the New Jersey Supreme Court necessary to enforce an arbitration provision in a commercial contract. Moreover, although prior unpublished decisions have reached similar conclusions, the *County of Passaic* case resulted in the first published Appellate Division decision containing a rule pronouncement regarding the enforceability of arbitration provisions in the commercial context.

While the decision, at first glance, appears to provide a bright-line rule regarding the enforceability of arbitration provisions in business-to-business contractual settings, a closer analysis reveals important interpretive and practical questions that remain unanswered. For instance, what qualifies a business as "sophisticated" in this context, and when do commercial parties have "relatively equal bargaining power"? More practically, how will this decision altering the existing standard impact ongoing commercial litigation arising out of a contract containing an arbitration provision? Finally, what impact might this have on transactional practice? This article addresses these important questions.

Prior to *County of Passaic*, the New Jersey Supreme Court in *Atalese v. U.S. Legal Services Group*, 219 N.J. 430, 446-47 (2014), held that, to be enforceable, contractual arbitration provisions must "at least in some general and sufficiently broad way," explain that the signatory is giving up the right to seek relief in court or have a jury resolve the dispute. The *Atalese* court explained that this requirement was necessary because the right to seek relief in court is guaranteed under the New Jersey Constitution and the waiver of constitutional rights must be reflected by a clear and unambiguous agreement to such terms. An explicit waiver of this constitutional right is evidence of a clear and unambiguous waiver, and without it the existence of mutual assent, as required for any contractual provision to be enforceable, is questionable.

The facts in *County of Passaic* were simple: Passaic County contracted with Horizon Healthcare Services to manage its employee self-funded health benefit plan beginning in 2002, with the relationship lasting until December 2019. In 2021, Passaic County sued Horizon, alleging breach of contract related to an issue involving modified reimbursement rates, following which Horizon successfully moved to compel arbitration pursuant to a provision in the parties' 2009 agreement. The provision stated that "in the event of any dispute between the parties to this Agreement arising under its terms, the

parties shall submit the dispute to binding arbitration under the commercial rules of the American Arbitration Association.” Passaic County appealed the decision enforcing the arbitration provision, arguing that the arbitration provision’s lack of an express waiver of the constitutional right to seek relief in court—as required under *Atalese*—rendered the provision unenforceable. The Appellate Division rejected the county’s argument, holding that an express waiver of the right to seek relief in court is not required to enforce an arbitration provision as between sophisticated commercial parties of relatively equal bargaining power.

In so holding, the Appellate Division acknowledged that the New Jersey Supreme Court in *Atalese* had not limited its holding in this way, but noted “the clues are there” that the case law was already moving in this direction. Generally, these “clues” revolved around the fact that, as noted by the Third Circuit in *In re Remicade Antitrust Litigation*, 938 F.3d 515, 525 (3d Cir. 2019), the state high court had to date only applied the stricter *Atalese* approach in consumer and employment contract situations, evidencing that the *Atalese* requirement of an express waiver of the right to seek relief in court was animated by a desire to protect those “not versed in the law” or aware that a constitutional right was implicated by the arbitration provision. This background was sufficient to satisfy the Appellate Division that, despite the lack of a published state Supreme Court or Appellate Division decision (the intermediate court had, on a few prior occasions, reached similar conclusions in unpublished, non-precedential opinions) reflecting the holding, it was adequately supported by the case law.

All of this begs the question, what makes commercial parties “sophisticated” and of “relatively equal bargaining power” such that an arbitration provision may now be enforced against one of them despite such provision not containing an express waiver of the right to seek relief in court? While the *County of Passaic* court did not directly answer this question, its opinion did leave “clues” as to what courts may look for. Most particularly, the opinion on more than one occasion discusses the role of legal representation. Indeed, the involvement of counsel in the relevant contractual negotiations and formation is mentioned both in the court’s identification of the policy concerns underlying the *Atalese* rule and in the facts of this case. Specifically, in the Appellate Division’s telling, *Atalese* and its progeny are all about protecting those who are not “necessarily versed in the meaning of law-imbued terminology about procedures tucked into form contracts.” Such policy concerns “vanish when considering individually-negotiated contracts between sophisticated parties—often represented by counsel at the formation stage.”

Moreover, in this case, both parties were represented by counsel “at all relevant stages of their negotiations,” during the formation of the contract, and throughout the 17-year relationship between the parties. As such, the court was convinced that these parties “understood the difference between the right to seek relief in a court of law and being relegated to arbitration.” Therefore, while the involvement of counsel at the negotiation and formation stages is likely the surest way to determine whether commercial parties are “sophisticated” and of “equal bargaining power” for this purpose, at its core the question likely comes down to whether the party against whom enforcement is sought can be said to have understood the difference between its constitutional right to seek relief in court, and instead being locked into arbitration. Businesses advised by counsel may be presumed to understand this difference, but even those that are not may potentially be so presumed if they are large entities or repeat players in their market that frequently enter into contracts or are otherwise familiar with litigation and arbitration processes.

Moving forward, and assuming the New Jersey Supreme Court does not take up this holding and reverse, it may be the case that in the commercial contract setting, if a party wishes to avoid enforcement of an arbitration provision that lacks an express waiver, such party may find itself in the potentially uncomfortable position of having to demonstrate that it is not sophisticated or otherwise lacks relatively equal bargaining power. For example, such a context could conceivably arise in contracts between large, national businesses and small, “mom and pop” shops that have considerably less experience with contractual negotiation and the relative advantages and disadvantages of the litigation and arbitration processes.

Another practical implication of the *County of Passaic* decision is its potential effect on existing commercial litigation. More specifically, of the thousands of existing litigations between businesses in New Jersey in which a contract is at issue, there are potentially many that contain arbitration provisions that do not include explicit *Ata/ese* waivers and in which, as a result, enforceability of such provisions was not previously at issue. As a result of this decision, however, those provisions are now enforceable so long as the commercial parties involved are sophisticated and possess relatively equal bargaining power. Accordingly, parties to ongoing litigation may now seek to enforce such provisions on the basis of *County of Passaic* by moving to dismiss the litigation and take the dispute to an arbitration forum, with the result being the potential frustration of ongoing litigation and an attendant waste of judicial resources, depending upon how far a given case has progressed. Commercial litigators should be aware of these potential implications for ongoing contract litigation, both those desiring to compel arbitration and those desiring to avoid it.

Finally, transactional attorneys should also be cognizant of this development, as their mere involvement in contractual negotiation and formation may now contribute to their client being viewed as sophisticated such that it may be held to an arbitration provision not containing an *Ata/ese* waiver. Moreover, transactional attorneys should advise business clients that, with respect to arbitration, businesses are now being held to a different enforceability standard than consumers and employees. Of course, they should also be aware that simply including the *Ata/ese* waiver advising the signatories that they are giving up their right to seek relief in court will circumvent the *County of Passaic* holding and any need to wonder whether their business client is “sophisticated” enough to be forced to arbitrate even in the absence of such waiver.

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