As Fallout from NorVergence Continues, New York Courts Revisit Forum Selection Clauses

By Howard M. Jaslow and Scott K. Levine

Multi-faceted and complex litigation has arisen focused on the equipment leasing industry as a result of the demise of NorVergence, Inc., a New Jersey-based reseller and provider of discount local, long-distance and cellular telecommunication services to businesses throughout the United States. As anyone involved in the equipment leasing industry is by now aware, in addition to providing ongoing telephone service to its customers, NorVergence also entered into equipment rental agreements for certain equipment known as "Matrix Boxes." These rental agreements contained the customary "Hell or High Water" provision, forum selection clauses and provisions disclosing the likelihood of the assignment of the rental agreements to third parties, among others.

It was customary for NorVergence to assign the executed rental agreements to various prominent leasing companies throughout the United States. The rental agreements specifically provided in pertinent part that:

"This agreement shall be governed by, construed and enforced in accordance with the laws of the State in which Rentor's principal offices are located or, if the Lease is assigned by Rentor, the State in which the assignee's principal offices are located, without regard to such State's choice of law considerations and all legal actions relating to this Lease shall be venued exclusively in a state or federal court located within that State, such court to be chosen at Rentor or Rentor's assignee's sole option."

In June, 2004 an involuntary petition under Chapter 11 of the Bankruptcy Code was filed against NorVergence. In July 2004, the United States Bankruptcy Court, District of New Jersey converted the NorVergence case from an involuntary Chapter 11 to a case under Chapter 7 and a Trustee was appointed. NorVergence ceased operations and shortly thereafter, the major telecommunication companies servicing NorVergence customers (Qwest, T-Mobile and Sprint) were authorized by the Bankruptcy Court to discontinue service. Numerous NorVergence customers alleged that NorVergence defrauded them and that under various legal theories, they were relieved of their contractual obligations under the rental agreements as a result of such fraud. Multiple individual suits and a number of class actions were subsequently filed on behalf of the NorVergence customers in a variety of jurisdictions. Thereafter, various Attorneys General commenced investigations of the allegations of fraud by NorVergence in response to complaints by NorVergence customers. The Attorneys General also intervened to stay the enforcement of the rental agreements by the leasing company assignees.

The demise of NorVergence has now caused courts throughout the United States to revisit the validity of time-tested "boiler-plate" provisions set forth within equipment leasing agreements, and in particular, the forum selection provisions. Prior to the NorVergence situation, the New York State courts did not take a definitive position concerning what is commonly known as "floating jurisdiction" provisions (i.e., provisions whereby the agreed mandatory venue of any action relating to the agreement could, subsequent to the execution the document, change to the principal office of an assignee by virtue of the assignment of the agreement to a third party leasing company). However, the United States District Court for the Southern District of New York had previously upheld forum selection clauses providing for jurisdiction and venue in the state of the "assignee's" place of business without determining beforehand the location of such place of business.[1] Contractual forum selection clauses have been determined to be constitutional.[2] Indeed, courts have held that such clauses have been favored and should be enforced[3] and that such clauses are prima facie valid and will be enforced except in instances of fraud or overreaching, or if enforcement would be so unreasonable or unjust such that the challenging party will effectively be denied his day in court.[4] Significantly, the standard of fraud or unreasonableness referred to in Fidelity and Deposit Co., of Maryland (1994), is not met by allegations with respect to the underlying object of the contract itself, but rather requires a showing of fraud or unreasonableness arising directly from the incorporation of the forum selection clause in the document.

Failing to substantiate any specific unreasonableness or fraud directly arising from the inclusion of the forum selection clause in the rental agreements, numerous NorVergence customers within the State of New York have asserted defenses which have been adopted in a small number of recent unpersuasive, unreported and/or non-controlling decisions. These decisions hold that — contrary to established law — the NorVergence forum selection clause at issue is not valid or enforceable because the designated forum was not fixed at the time of contract. These non-reported decisions from the New York Civil Court have relied upon dicta of the New York Court of Appeals[5] as their sole support; we believe such dicta of the Court in Brooke Group Ltd. has been misinterpreted and misapplied by these courts.

These non-reported New York Civil Court decisions conclude, without what we believe to be proper analysis, that because "certainty" of personal jurisdiction is one of the principles underlying the favored status of forum selection clauses, it follows that where the state of the forum may change over time, the clause must be viewed as too uncertain to enforce. We believe that the error these courts have made relates to their misunderstanding of the context of the word "certainty." Essentially, the importance of "certainty" arises at the time of suit and not — as suggested by these Courts — at the time of contract.

In *Brooke Group, Ltd.*, the issue before the Court of Appeals was whether a particular clause was a "service of suit clause" or a mandatory forum selection clause. If the former, it is permissive and therefore subject to a dismissal on forum non-conveniens grounds; if the latter, it is mandatory and subject to a dismissal on such grounds. In discussing the reasons for the favored enforcement of forum selection clauses, the Court of Appeals stated in part, "[forum selection clauses] provide certainty and predictability in the resolution of disputes..." Id 87 N.Y. 2d at 534. Notably, the Court of Appeals refers to certainty "in the resolution of disputes," not in execution or performance of the contract. The "certainty" the Court of Appeals was referring to is important at the time of the dispute (i.e., litigation). See also *National Union Fire Insurance Company of Pittsburgh vs. Williams*, (1996) supra 223 A.D. 2d at 397, 637 N.Y. S. 2d at 38 ("It is axiomatic that the very point of a selection of forum clause is to avoid litigation over personal jurisdiction....").

The clause set forth within a NorVergence rental agreement provides exactly the kind of certainty referred to by the New York Court of Appeals and the First Department. At the time of suit there can only be one forum state in which the action may be brought. If the rental agreement was not assigned, it must be brought in the State of New Jersey, NorVergence's principal place of business. If the rental agreement was assigned, then the appropriate forum is in the state of the assignee's place of business. That such a clause provides certainty for the parties regarding personal jurisdiction at the time of the dispute/lawsuit can be readily seen if the rental agreement is hypothetically viewed as having no enforceable forum selection clause. At the time of suit there would truly be uncertainty as to a proper forum. A potential plaintiff could institute suit in a defendant's state; the defendant could sue a plaintiff (for declaratory relief and the like) in the plaintiff's state. A plaintiff could try to sue a defendant in New Jersey where a defendant may have "transacted" business in executing the rental agreement with NorVergence. Indeed, a defendant could have relocated its principal place of business during the pendency of the rental agreement, such that a plaintiff could sue a defendant in the new state of its principal place of business or even in the former state since a defendant clearly transacted business in such former state in connection with the rental agreement. The foregoing does not even include the fact that a defendant would be amenable to personal jurisdiction in any state in which a defendant does business on a regular basis.

The forum selection clause removes the guesswork and uncertainty by providing the availability of one — and only one — forum state for the resolution of a dispute at the time of suit. No motions or evidentiary hearings are needed to determine if a defendant has sufficient contacts with the chosen forum. Thus, the parties to a NorVergence rental agreement have consented in advance to a single forum state for resolving their disputes.

That such "certainty" speaks as of the time of suit is self-evident. Numerous Courts have upheld forum selection clauses providing for jurisdiction in the State of a party's "principal place of business" despite it being patently obvious that such place of business can change during the length of the contract.[6] Likewise, the NorVergence forum selection clause provides for a specific forum (i.e. the state of the lessor's principal place of business) which could later change by assignment of the rental agreement, but which would be certain at the time of any lawsuit. Such a provision undoubtedly adds certainty to a subsequent suit between the parties than would an identical contract lacking such a clause.

While this article has focused primarily on relevant New York law, we believe that the principles set forth herein, particularly with respect to the concept of certainty at the time of any lawsuit rather than at the time of contract, should be instructive in any jurisdiction. ■

Howard M. Jaslow *and* **Scott K. Levine** *are partners in the New York City law firm of Platzer, Swergold, Karlin, Levine, Goldberg & Jaslow, LLP. Together with their partner, Stan L. Goldberg, they maintain an active equipment leasing practice and represent numerous lessors on collection and enforcement, asset recovery, bankruptcy and documentation issues.*

REFERENCES

1 A.I. Credit Corporation vs. Andrew Djiounas and Mary Djiounas, 1992 WL 131783 (S.D.N.Y.); A.I. Credit Corporation vs. Steven Liebman, 791 F. Supp. 427 (1992).

2 Bremen vs. Zapata Off-Shore Co., 407 U.S. 1, 92 S. Ct. 1907, 32 L. Ed. 2d 513 (1972).

3 National Union Fire Insurance Co., of Pittsburgh vs. Williams, 223 A.D. 2d 395, 637 N.Y.S. 2d 36 (Appellate Division, 1st Dept., 1996).

4 Fidelity and Deposit Co., of Maryland vs. Altman, 209 A.D. 2d 195, 618 N.Y. S. 2d 286 (Appellate Division, 1st Dept., 1994).

5 Brooke Group Ltd. vs. GCH Syndicate, 488, 87 N.Y. 2d 530, 663 N.E. 2d 635, 640 N.Y. S. 2d 479 (1996).

6 Commerce Commercial Leasing, LLC vs. Jay's Fabric Center, 2004 WL 2457737 (E.D., Pa., 2004); Lyon Financial Services, supra; Great American Leasing Corp. vs. Telufar Corp., 1999 WL 33656867 (N.D. Iowa, 1998).