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New Jersey Consumer Fraud Act Update: New Jersey Supreme Court Clarifies the Standard for Principals' Individual Liability for Corporate Regulatory Violations

On July 7, 2011, in *Allen v. V and A Bros., Inc*. (A-30-10)(066568), the New Jersey Supreme Court affirmed, modified in part, and reversed a June 23, 2010, decision by the Appellate Division. In so doing, the court held that principals of a corporation may be found individually liable under the New Jersey Consumer Fraud Act ("the Act") for the corporation's regulatory violations. The court departed from the Appellate Division's analysis, however, regarding the standard for determining individual liability, and provided further clarification on appropriate parameters for imposing individual liability under the Act. The parameters established in *Allen* preserve the ability of the state and consumers to seek to impose liability on individual corporate actors for regulatory violations, using a somewhat less onerous standard than what has been required under the more traditional theory of "piercing the corporate veil."

Background

In *Allen*, plaintiffs brought suit against a landscaping company and three individuals for, among other things, regulatory violations related to home improvement requirements under the Act. Specifically, the plaintiffs alleged that both the company and the individual defendants violated three home improvement regulations, which constituted a violation of the Act: 1) failing to make the home improvement contract in writing, 2) failing to obtain inspection certificates and final approval before accepting final payment for the work, and 3) making substitutions of materials without plaintiffs' consent or knowledge.

The trial court dismissed the claims against the individual defendants on summary judgment before the case went to trial, at which the plaintiffs ultimately won a $490,000 verdict against the company. The Appellate Division reversed on the issue of the individual defendants' liability, holding that the individual defendants may be held personally liable under the Act for the regulatory violations of their company. The New Jersey Supreme Court agreed but clarified the standard for determining personal liability of corporate actors for a corporation's regulatory violations; it referred the matter back to the trial court to be relitigated to determine the individual defendants' personal liability.

Related practice areas:

Consumer Finance and Creditors' Rights

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Application of the Strict Liability Standard Is Not Automatic

The court in *Allen* recognized the remedial nature of the Act and reiterated that it should be construed liberally in favor of consumers. The court stated that the Act was created to protect consumers who have fallen prey to three separate categories of unlawful practices: 1) affirmative acts, 2) knowing omissions, and 3) regulatory violations. The *Allen* case concerned the third category of unlawful practices.

The court opined that the regulatory violations category is the most complicated of the three because regulatory violations, unlike affirmative acts and knowing omissions, are typically analyzed using a strict liability standard, meaning no proof of intent or even knowledge of a violation is required to impose personal liability on corporate actors. The theory behind applying the strict liability standard in the context of regulatory violations is that parties subject to regulations are assumed to be familiar with them, so that any violation of the regulations, regardless of intent or moral culpability, makes such parties liable.

Although the court upheld the part of the Appellate Division's decision finding that corporate actors could be held personally liable for a company's regulatory violations, it departed from the Appellate Division's strict liability analysis. While acknowledging that regulatory violations are typically analyzed in terms of strict liability, the court found that imposing strict liability on individuals for the regulatory violations of the corporation under the Act implicates "notions of fairness" because some types of regulatory violations will be ones over which an individual employee has no input or control. Thus, the court found there is no single, definitive answer as to whether strict liability will be applied, because "individual liability for regulatory violations ultimately must rest on the language of the particular regulation in issue and the nature of the actions undertaken by the individual defendant."

Personal Participation Analysis Must Include a Distinction Between Principals and Employees

In addition to the proof of personal participation by an individual in a particular regulatory violation that must be shown, the court held that a distinction must also be drawn between a corporation's principals and its employees when analyzing whether there can be individual liability for the corporation's regulatory violations: "The principals may be broadly liable, for they are the ones who set the policies that the employees may be merely carrying out." The court also extended the potential for liability to include nonprincipal employees where such employees unilaterally deviate from company policy or the contract at issue. The court therefore determined that these are highly fact-sensitive inquiries and "individual liability for a violation of the [Consumer Fraud Act] will necessarily depend upon an evaluation of both the specific source of the claimed violation that forms the basis for the plaintiff's complaint as well as the particular acts that the individual has undertaken."

What the *Allen* Decision Means for Businesses and Individual Corporate Actors

The lesson learned from the *Allen* case is that businesses must be vigilant about updating company policies and aligning them with the laws and regulations that govern them. The Act permits the imposition of personal liability on corporate actors, whether they are principals or employees, even when individuals' acts that result in regulatory violations of the Act are effectuated through the corporate entity. Courts will assume individual corporate officers and company employees are familiar with the regulations and may hold individuals personally liable for company violations. Determining individual liability will require a very fact-specific analysis, and will depend largely on whether the individual has played some sort of role in violating the rules and whether he or she had control over the act that resulted in the regulatory violation.

Should you have any questions or concerns about the Consumer Fraud Act or how this decision may affect your company, please contact one of the authors of this alert.

Bar Admissions: New Jersey [NJ]

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