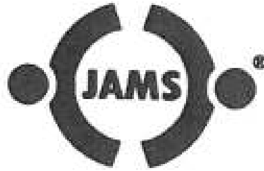

IN THE MATTER OF:	)	
MICRO SALES, INC.,	)	
Claimant	)	
vs.	)	**CASE NO. 1340010898**
ADVANTECH CORPORATION,	)	
Respondent.	)	

ORDER ON CHOICE OF LAW

Pursuant to Scheduling Order No. 2, the parties have filed briefs addressing the issue of which law should apply in this arbitration. Claimant, Micro Sales, Inc. ("Micro Sales") contends that the law of Illinois should apply, while Respondent Advantech Corporation ("Advantech") contends that the law of California should apply. For the reasons stated below, I find that the law of Illinois shall govern this arbitration.

BACKGROUND

Claimant Micro Sales is an independent manufacturer's representative who specializes in designing, marketing, and selling electronic components for computers and other electronic products for the northern Illinois and southern Wisconsin markets. Micro Sales is an Illinois corporation with offices located at 1001 West Hawthorne Drive,

Itasca, Illinois. Micro Sales does not solicit sales orders in the State of California, and Micro Sales has no sales territory in California.

Respondent Advantech designs and manufactures imbedded computing systems and imbedded computing products, such as computer modules, signal board computers, motherboards, and computing platforms. Advantech relies on independent representation to sell its products by contracting with independent manufacturers' representatives, like Micro Sales, or by using direct sales employees. Advantech is a corporation incorporated under the laws of California and maintains its United States headquarters at 380 Fairview Way, Milipitas, California.

On April 10, 2012, Micro Sales and Advantech entered into a Manufacturer Representative Agreement (the "Agreement"), which provides that Micro Sales would act as the non-exclusive selling agent of Advantech products for the Northern Illinois and Wisconsin regions. The Complaint alleges that Advantech breached the Agreement on five occasions from February 2012 through November 2013, and Micro Sales seeks recovery of $135,021.97 in unpaid commissions pursuant to the terms of the parties' Agreement. Micro Sales also contends that it is owed commissions for Advantech products sold and shipped between November 19, 2013 and April 10, 2014 and that Advantech has refused to provide an accounting for products sold in that time frame. The Complaint alleges that Advantech's actions violate the Illinois Sales Representative Act, 820 ILCS 120/1 *et seq.* (the "Illinois Act"), which provides that a foreign manufacturer is legally obligated to provide a full accounting of all commissions owed under the parties' contract and to pay commissions due and owing under certain statutory prescribed deadlines. Advantech has filed a counterclaim against Micro Sales alleging that during

the time period January 2013 through April 2014, Advantech overpaid commissions to Micro Sales in the amount of $ 15,804.42. Advantech alleges that Micro Sales has been unjustly enriched as a result of this alleged overpayment of commissions.

Micro Sales originally brought this action in the United States District Court for the Northern District of Illinois to compel arbitration under the Federal Arbitration Act, 9 U.S.C. 4, 5. On April 10, 2014, Judge Sarah Ellis granted the parties' agreed motion for the appointment of an arbitrator, appointed the undersigned arbitrator, and ordered "such arbitration to take place in Chicago, Illinois."

DISCUSSION

At issue in this case is whether the law of Illinois or the law of California should govern this arbitration. Advantech contends that the law of California should apply because the Agreement between the parties contains the following language:

> The validity, performance, construction and effect of this Agreement shall be governed by the laws of the State of California (where Advantech has its principal places of business) without giving effect to principles of conflicts of law.

Advantech Manufacturer Representative Agreement at ¶ 20. Advantech argues that this arbitrator must apply the substantive law of California to determine the merits of Micro Sales' claims in accordance with this provision of the Agreement.

Micro Sales contends that the law of Illinois should apply because it is an Illinois independent sales representative of Advantech's products. As such, Micro Sales should be protected by the Illinois Sales Representative Act, which provides that "[a]ny provision in any contract between a sales representative and principal purporting to waive any of the provisions of this Act shall be void." 820 ILCS 120/2. Micro Sales essentially argues that

the California choice of law provision in the Agreement is void because it is contrary to the public policy of the State of Illinois, and Micro Sales will not receive the protections guaranteed to it by the Illinois Act if California law were to apply.

It is well settled that an arbitrator should apply the law of the forum state in which she sits, including that state's conflict of laws rules.[1] This action was filed in the United States District Court for the Northern District of Illinois,[2] and Illinois has adopted the Restatement (Second) of Conflict of Laws to resolve conflict of laws issues.[3] *See Newell Co. v. Petersen,* 758 N.E.2d 903, 922 (Ill. App. Ct. 2001). Section 187(2) of the Restatement (Second), which governs situations in which parties have included an express choice of law provision in their contract, provides that the parties' choice of law should govern unless either "(a) the chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties' choice, or (b) application of the law of the chosen state would be contrary to a fundamental policy of a state which has a materially greater interest than the chosen state in the determination of the particular issue and which, under the rule of §188, would be the state of the applicable law in the absence of an effective choice of law by the parties." Restatement (Second) of Conflict of Laws § 187(2) (1971) (hereinafter "Restatement").

Looking first at subsection (a) of Restatement § 187(2), I find that California does have some substantial relationship to one of the parties and to the transaction. "When the

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[1] I am aware that the Agreement in this case indicates that California law shall apply "without giving effect to principles of conflicts of law." Nevertheless, a conflict of laws analysis cannot be waived merely by inserting such language in the Agreement.

[2] Micro Sales and Advantech entered into an agreed motion for the appointment of an arbitrator in Chicago, Illinois to conduct the arbitration in Chicago. The parties thus consented to this arbitration proceeding in the State of Illinois.

[3] California also follows the Restatement (Second) of Conflict of Laws to resolve disputes regarding conflict of laws. *See, e.g., Nedloyd Lines B.V. v. Superior Court*, 3 Cal. 4th 459, 464-65, 11 Cal. Rptr. 2d 330. (1992).

state of the chosen law has some substantial relationship to the parties or the contract, the parties will be held to have had a reasonable basis for their choice. This will be the case, for example, when this state is that where performance by one of the parties is to take place or where one of the parties is domiciled or has his principal place of business." Restatement (Second) of Conflict of Laws, § 187, Comment f. In this case, California need not have the "most substantial" relationship to the parties or the transaction under §187(2) (a); it need only have "some substantial" relationship for the parties' choice of law to be enforced under subsection (a). *See Potomac Leasing Co. v. Chuck's Pub, Inc.*, 509 N.E.2d 751, 754-55 (Ill. App. Ct. 1987). Since California is the state of incorporation of Advantech and it has its principal place of business there, that is contact sufficient to constitute a "substantial relationship" and thus, under subsection (a) of Restatement § 187(2), California law seems a reasonable basis for the parties' choice of law.

The next prong of the test, subsection (b) of Restatement § 187(2), examines whether the chosen state's law is "contrary to a fundamental policy of a state which has a materially greater interest than the chosen state in the determination of the particular issue and which . . . would be the state of the applicable law" in the absence of the choice of law provision. Restatement (Second) of Conflict of Laws, § 187(2)(b). In this case, since California is the law of the chosen state, I must determine whether the law of California is contrary to a fundamental policy of Illinois and whether Illinois has a materially greater interest in this case than California.

I. <u>Is Application of California Law Contrary to a Fundamental Policy of Illinois?</u>

Illinois law is clear that a fundamental policy of the state is to protect its sales representatives from unfair practices on the part of foreign manufacturers. *See Maher and Associates, Inc. v. Quality Cabinets*, 640 N.E.2d 1000, 1005 (Ill. App. Ct. 1994), *petition for leave to appeal denied*, 647 N.E.2d 1011 (1995). In order to promote and enforce its fundamental policy of protecting Illinois independent sales representatives, the Illinois legislature enacted a progressive statute that protects Illinois independent sales representatives from breach of contract, denial of earned sales commissions, and other unfavorable practices on the part of foreign manufacturers. Illinois Sales Representative Act, 820 ILCS 120/1 *et seq.* Failure to comply with the requirements of the statute can result in civil liability for the commissions owed, punitive damages not to exceed three times the amount of those commissions, and liability for attorneys fees and court costs. 820 ILCS 120/3. In addition, and most important to the choice of law analysis in this arbitration, the Illinois Act provides that "[a]ny provision in any contract between a sales representative and principal purporting to waive any of the provisions of this Act shall be void." 820 ILCS 120/2.

Micro Sales contends that Illinois has declared the protection of its sales representatives to be a fundamental policy, and a choice of law provision contained in a manufacturer representative agreement providing that another state's law governs the contract is void, unenforceable, and contrary to Illinois public policy.

In *Midwest Enterprises v. Generac Corporation*, plaintiff Midwest Enterprises was an Illinois based independent sales representative who brought an action for unpaid sales commissions against a Wisconsin manufacturer, Generac Corporation, arising out of an independent manufacturer sales representative agreement. *Midwest Enterprises v.*

Generac Corp., No. 91 C 2229, 1991 WL 169059 (N.D. Ill. August 27, 1991). The parties' contract contained a Wisconsin choice of law provision. When Generac sought to enforce the Wisconsin choice of law provision, Midwest Enterprises contended that the Illinois legislature, through the Illinois Sales Representative Act, declared the protection of sales representatives operating in the state to be a fundamental pubic policy of Illinois.

The court held that the Wisconsin choice of law provision was void as a matter of public policy. *Id.* at *4. The court noted that § 187(2)(b) of the Restatement (Second) of Conflict of Laws supported the ruling because if Wisconsin law governed, a fundamental policy of Illinois (namely the protection of its independent sales representatives) would be ignored. The court also held that Illinois had a materially greater interest than Wisconsin in the issue of commissions owed. Wisconsin's only connection to the litigation was Generac's state of incorporation. Midwest Enterprises, an Illinois corporation, worked as Generac's sales representative to solicit orders in Illinois, and all products and commissions owed, arose from sales made in Illinois. Therefore, Restatement § 187(2) voided the parties' choice of law provision in their contract. Numerous other courts have reached similar results since this seminal ruling in *Midwest Enterprises*. *See, e.g., Maher*, 640 N.E.2d at 1006 (Texas forum selection clause and Texas choice of law provision in parties' contract void and unenforceable as against fundamental Illinois public policy); *Reinherz v. Sun Microstamping, Inc.*, No. 00 C 4407, 2000 WL 1774098 (N.D. Ill. December 1, 2000) (enforcement of parties' choice of Florida law would be contrary to a fundamental policy of the state of Illinois).

Advantech attempts to distinguish these cases by contending there is no conflict with Illinois policy in the application of California law because the governing rules regarding

independent sales representatives and the recovery of commissions are essentially the same in both states. Advantech argues that the California Independent Wholesale Sales Representative Contractual Relations Act of 1990, Cal. Civ. Code, § 1738.10 *et seq.* ("the California Act"), protects Micro Sales' right to recovery of commissions in this case.

The California Act applies to and protects independent sales representatives in California. It provides, in part:

> (a) Whenever a manufacturer, jobber, or distributor is engaged in business within this state and uses the services of a wholesale sales representative . . . **to solicit wholesale orders at least partially within this state**, and the contemplated method of payment involves commissions, the manufacturer, jobber, or distributor shall enter into a written contract with the sales representative.

Cal. Civ. Code §1738.13 (emphasis added).

Although there is not much California law on the subject, at least one California court has made clear that the California Act is intended to protect California wholesale sales representatives, not out of state sales representatives. *See Reilly v. Inquest Technology, Inc.*, 218 Cal. App. 4th 536 (2013). The *Reilly* court pointed to §1738.13(a), which provides statutory protection for wholesale orders made within the State of California. When examining the scope of the California Act and determining which entities the Act applies to, the court noted:

> Moreover, we note the Legislature enacted a very broadly worded definition to include any manufacturer in the business of "producing, assembling, mining, weaving, importing, or ... any other method of fabrication." (§ 1738.12, subd. (a).) The kinds of businesses included in the Act appear limitless, and largely include "product[s] tangible or intangible." (*Ibid.*) There is nothing to suggest the Legislature intended to narrow the scope of possible products to exclude parts or components. **The only stated**

> **limitation is that the manufacturer must solicit wholesale orders in California and *intend* for its goods to be later resold or used by a California consumer, promoting California's economy.**

Id. at 551 (emphasis added).

The *Reilly* court held that the California Act is limited to cover manufacturers hiring sales persons who solicit wholesale orders within California. "These provisions, like the definition of manufacturer, limit the Act's scope to cover manufacturers hiring sales persons to solicit wholesale orders within California, having territories 'at least partially' within our state." Id. at 549-50. Therefore, the California Act does not apply to sales persons outside California who solicit wholesale orders in states outside of California, such as Illinois.

For these reasons, the California Act does not support application of the California choice of law provision in the parties' Agreement because application of California law in this case would not protect Micro Sales, an Illinois independent sales representative, as would the application of Illinois law. Although California has a similar law protecting its resident independent salesmen, the California Act does not protect Micro Sales because it protects California resident independent salesman, not Illinois independent salesmen. Illinois fundamental policy, as expressed in the Illinois Sales Representative Act, governs the relationship between the parties and voids the California choice of law provision as a matter of law. Therefore, the California statute simply does not protect Micro Sales in this case, and Restatement § 187(2)(b) requires that I void the Agreement's choice of California law in this case.

Policy reasons support this determination as well. When foreign manufacturers do business in Illinois with Illinois sales representatives, those manufacturers are put on notice that they could be subject to litigation in Illinois. *Midwest Enterprises v. Generac Corp.*, 1991 WL 169059. In this case, Advantech developed its market in Illinois under the protection of Illinois law through the use of Micro Sales as an independent sales representative. By doing so, Advantech cannot escape the Illinois fundamental policy of protecting its independent sales representatives by incorporating a choice of law provision in its standard form contract that attempts to avoid application of the Illinois Act.

Does Illinois Have a Materially Greater Interest in This Case Than California?

Examining the remaining requirement of Restatement §187(2)(b), I find that Illinois does have a materially greater interest in this case than California. This case originally was filed in the U.S. District Court for the Northern District of Illinois. Illinois is the home state of Micro Sales, a sales representative operating in Illinois, and thus this action was initiated by an Illinois sales representative in its home state. Furthermore, most, if not all, of the transactions giving rise to Micro Sales' claims for unpaid commissions in this case occurred in Illinois. The main relationship California has to the transactions at issue is that Advantech is incorporated there and has its principal place of business there. For these reasons, I find that Illinois has a materially greater interest in this case than California.[4]

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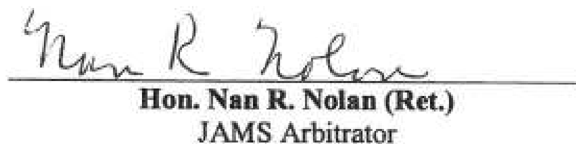
[4] Although the parties in this case have not engaged in discovery, Advantech insisted that this choice of law issue be addressed prior to discovery. Pursuant to Scheduling Order No. 4 dated February 6, 2015, the parties filed supplemental briefs addressing certain factual questions raised and unanswered in the parties' original round of briefing. Through this supplemental briefing, the parties submitted affidavits and were given an opportunity to clarify certain factual issues impacting the choice of law issue. Despite being given

CONCLUSION

For the foregoing reasons, I find that the California choice of law provision contained in Paragraph 20 of the Advantech Manufacturer Representative Agreement is void and unenforceable. Illinois law will apply to the issues in this arbitration. This case is set for a telephone status conference on May 20, 2015 at 10:00 a.m. CDT to address the issues of a discovery schedule and Micro Sales' Answer to Advantech's counterclaims.

DATED: **May 8, 2015**



Hon. Nan R. Nolan (Ret.)
JAMS Arbitrator

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this opportunity, Advantech did not provide the clear answers to the questions raised in Scheduling Order No. 4 necessary to justify a ruling in its favor on the choice of law issue.