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Staying On Track In A Non-Compete Case

As More Workers Race Off To Competitors, Lawyers Sprint To The Courthouse

Illustration by Mark Armstrong

By Jason M. Scally

With intellectual-property theft and battles over client goodwill of increasing importance to companies, more Massachusetts businesses are looking to non-compete agreements to protect themselves. And employment lawyers are seeing a renewed surge of litigation over non-competes.

Two recent decisions (with different results) illustrate why this is such a fertile ground for future court face-offs and why lawyers must gear up for a fact-based battle every time they handle a non-compete case.

In a case before U.S. District Court Judge Douglas P. Woodlock (*Oxford Global Resources, Inc. v. Guerriero, et al.*, Lawyers Weekly No. 02-199-03), a personnel-staffing company sought to enforce a non-compete agreement against former employees who had allegedly taken client lists and gone to work for a competing company. The non-compete was upheld — at least for the purposes of a preliminary injunction.

Meanwhile, in a case handled by Superior Court Judge Nonnie S. Burnes (*Cypress Group, Inc., et al. v. Stride & Associates, Inc.*, Lawyers Weekly No. 12-031-04), client lists and enforcement of a non-compete agreement were was also at issue after former employees of an IT personnel-staffing company left to join a competitor. But this time the judge ruled in *favor* of the ex-employees, granting a declaratory judgment action seeking a ruling that the non-compete agreement was unenforceable.

Lawyers interpret the differing rulings as a message that the equitable nature of non-compete cases often breed fact-specific analyses by judges, which is why results from case to case may vary, even in suits that appear similar on their face.

So what can an attorney handling a non-compete case do to get an edge?

For one, non-competes should be narrowly tailored with regard to both the duration and scope of the agreement, experts say, and employers should realize that not all employees should be — or *can* be — covered by one company-wide form.

Non-compete agreements, as contracts, also require consideration, but there may be times when "the job itself" will not be sufficient consideration to require an employee to sign a non-compete.

Parties seeking to enforce a non-compete should also be careful of their own actions, as a company with "unclean hands" may hurt its own chances to enforce a normally valid agreement.

Conversely, parties trying to invalidate the agreement can point to those same elements in support of their position if they can find violations.

Common Trap

The law of non-competes varies from state to state, but in Massachusetts it is pretty well settled. For a non-compete to be valid in the commonwealth, it must protect a "legitimate business interest," which is typically a confidential trade secret or "goodwill."

However, in this area of employment practice, just having the law "on your side" may not be enough to win the case.

"It's a common trap to fall in love with your legal argument when your facts are really bad," says Jay Shepherd, a Boston employment lawyer who says almost 70 percent of his business is now non-compete-related. "Lawyers need to remember that these cases are almost always decided at the preliminary injunction stage ... and that's equitable relief, so the judge is going to make the ruling based on equity rather than on the legal argument."

The apparently inconsistent results in the *Oxford* and *Cypress Group* signal that judges will heavily rely on the facts of each case. (On the surface, the only difference in the cases was that *Cypress Group* — where the employees prevailed — was brought in the Superior Court's Business Litigation Session and initiated by the former workers in a declaratory judgment action seeking a ruling that the non-compete agreement was unenforceable.)

The knee-jerk reaction, especially in the often-contentious world of employment law, might be to blame "court bias." But some lawyers say that's not necessarily the case.

"In fact, I think [the lack of court bias] is born out by the fact that Judge Burnes cites the *Oxford* case with approval in the *Cypress* case, and Judge Woodlock, in the *Oxford* case, cites Judge Burnes' earlier cases with approval," says Shepherd, who represented the departing employees in *Cypress*. "They're on the same page [and] they're applying the same law."

In *Oxford* and *Cypress*, the divergent opinions came down to the facts of the cases — specifically, the way each staffing company ran its businesses.

Oxford's business model was based on the strong relationships developed between its employees and their clients, so the fact that the departing employees were trying to solicit former clients from Oxford's "A list" of customers had the potential for a loss of Oxford's goodwill.

In comparison, Cypress' business model was based more on volume "cold-calling," rather than on relationship building. The potential for a loss of goodwill in *Cypress*, Burnes said in her decision, was much less because there was no effort made to establish longstanding relationships with clients.

For example, in *Cypress*, when employees transferred from one Cypress office to another, they weren't allowed to take their client lists with them. That was just one of the facts that apparently made enforcement of Cypress' non-compete agreement appear less reasonable to the judge.

"The legal principles that govern non-competes are broadly stated," observes James W. Nagle, who heads the employment practice at his Boston firm, "so the devil is always in the details."

"Be familiar with the decisions that have come before, but past isn't always prologue," warns Christopher R. O'Hara of Boston. "These are very fact-intensive cases."

What Judges Like To See

As both *Oxford* and *Cypress* demonstrate, details are incredibly important in a non-compete case, so it's equally important that attorneys learn which details judges may be looking for.

Christopher R. O'Hara of Boston, the lawyer for the staffing company in *Oxford*, declines to comment specifically on the case, but notes that in goodwill cases the courts generally are looking at "relationships," while in trade-secret cases — which he says often receive more scrutiny than goodwill cases — a judge's analysis is frequently on the "nature" of the trade secret.

Consideration is also a key issue in determining the enforceability of non-compete agreements. Non-compete agreements, like all contracts, require some kind of consideration in order to be valid.

But consideration is also where there seems to be the most debate among lawyers.

In Massachusetts, Shepherd explains that "the job itself" is usually enough consideration for requiring an employee to sign a non-compete, as long as it is signed at the start of employment as a condition of employment. Most employment lawyers seem to agree with him.

However, where the waters get muddied is when an employee is told to sign a non-compete agreement in mid-employment, because the promise of continued employment might not always be enough.

"There are cases that say it's sufficient consideration, and then there are cases that say it is not," according to Ian Crawford, a Boston lawyer who says about 25 percent of his practice is now devoted to non-compete-related work, primarily in the securities brokerage industry. "When giving advice to a client, point out that there's some inconsistency."

Catherine E. Reuben of Boston agrees, noting that "if you ask two lawyers, you'll get three opinions on whether you need consideration in Massachusetts."

Both attorneys say it may be smart for companies to offer something in addition to continued employment — like stock options, suggests Crawford — in exchange for the employee signing the agreement.

Questions over consideration may result in the most debate among lawyers, but it's often a lack of *reasonableness* that causes an agreement to be deemed unenforceable.

Employment lawyers explain that while it's true that public policy supports the enforcement of contracts that are freely entered into by the parties, in the world of non-competes there is also a competing public policy interest in favor of allowing employees to work in their chosen field of work.

Judges will often look at whether the non-compete agreement is reasonable in light of the second public policy concern, attorneys say, and there are a number of common mistakes made by companies that will cause their agreements to fail the "reasonableness" test.

Avoid Overbroad Agreements

Where companies often stray from a judge's "reasonableness" standard is in the scope of the non-compete agreement.

Challenging an agreement for being "too broad" in either its geographical or durational scope is a common tactic used by attorneys attacking the validity of non-competes.

As Reuben notes in the "Non-Competition Checklist" that she gives to her clients, "[F]or fast-changing industries (e.g. high tech) shorter periods may be enforced [and generally,] agreements lasting more than a year are closely scrutinized." (Reuben's complete checklist can be found in the Important Documents section of our website, www.masslawyersweekly.com.)

A nationwide prohibition on future work in a given field may also run afoul of any reasonableness test, especially if the employer

who is pushing the non-compete agreement only has a regional presence, she adds.

Other lawyers note that agreements generally can't deny someone from working in an entire industry as well.

"You can't just do a blanket agreement," says Crawford. "You can't say 'you won't work for anybody in this industry or related industries.'"

Reuben explains that "it may not be reasonable to say you can't do anything in health care sales, for example, but it might be reasonable to say the employee is barred from selling a particular kind of [health-care-related] equipment."

Generally, attorneys say the narrower the agreement, the better the chance is that a judge or court will enforce it.

"A judge is more likely to be persuaded to enforce an agreement if he or she feels that the agreement was specifically created for this employee," says Shepherd, rather than a "boilerplate" agreement given to all employees.

Certain employees, such as lawyers and other professionals, also can't be forced to sign non-competes because of public policy concerns. Similarly, Reuben observes that some states, such as California, may not recognize all non-compete agreements.

Having these "prohibited" employees sign the same non-compete agreement as other employees may take away from a company's argument that its agreement was narrowly tailored or reasonable.

Furthermore, companies may run into trouble if a former employee can prove the agreements were only selectively enforced against certain classes of employees.

Reuben says when there's been selective enforcement of a non-compete, a judge may ask: "Where's the emergency? You've never tried to enforce [the agreement] before."

Selective enforcement may be one example of where having "unclean hands" can hurt a company's chances of enforcement, according to lawyers.

In the same vein, companies need to be careful about which arguments they're making if there is a chance they could someday find themselves on the other side of the enforceability argument.

"What's sauce for the goose is sauce for the gander," says Reuben. "If you want to say the things are enforceable, you better be careful about hiring employees from competitors who have non-competition agreements."

Can They Keep A Secret?

Employment attorneys say that defining confidential information should also be done carefully.

O'Hara advises lawyers to determine if it is "truly a proper trade secret, or is it out in the public domain?"

Shepherd says that while clients often have their own idea of what constitutes a trade secret, "they're generally wrong."

For example, he says it's common to see agreements that define confidential material as "everything we've ever given you during the course of your employment."

But that won't work, he says. "It's got to be some piece of information that you take active measures to keep secret and that gives you an advantage over other companies."

Reuben agrees and says that the inquiry is not what you *call* the so-called protected information, but how it is *treated* by the company.

Shepherd recalls one case in which a company tried to claim that its customer lists were trade secrets — an assertion that ultimately backfired when Shepherd held up a screen shot of the company's website that displayed a customer list.

"If you don't do anything to protect that information, the court doesn't care what you call it," Shepherd says. MLW

Questions or comments may be directed to the writer at jscally@lawyersweekly.com.

Avoiding Non-Compete Pitfalls

Experts in non-compete litigation in Massachusetts say that attorneys should beware of a few pitfalls if they want to become successful in this area of the law.

First off, advises James W. Nagle of Boston, is pay attention to the document itself.

Although it may sound obvious, he recalls situations in which a lawyer is in court trying to enforce a non-compete, only to find out that the employer-client never signed the agreement — a requirement in most non-compete forms — so it never took effect.

"Reading documents carefully and paying attention makes good sense," Nagle says.

Boston's Jay Shepherd recommends that attorneys also be wary of representing two parties with seemingly similar interests, such as a departing employee and his new company, because conflicts can arise if, for example, one of the parties has acted with "unclean hands."

"If you get yourself into one of these conflicts, you may find yourself not being able to represent either party," Shepherd cautions. "That's not good for you, and that's not good for the clients because that adds to their expense."

Other tips offered by employment lawyers are be proactive and offer advice before non-compete agreements come into play.

For those representing employees, lawyers say make sure that the worker knows what he is getting into before signing the non-compete agreement.

Catherine E. Reuben of Boston says employers will often be stubborn about accepting any employee-suggested changes to the agreement, but she suggests that "many times you can talk them into it once you show them the changes will make the agreement clearer and more enforceable [for] everybody."

Attorneys are also advised to make sure their corporate clients are in compliance with state and federal labor laws.

Shepherd says he hasn't seen many non-compete decisions that specifically reference labor violations, like unpaid overtime, as a reason for not enforcing an agreement, but he has come across those other charges used as bargaining chips in some cases to trade certain counts away.

"It comes up routinely in more of a tactical, quid-pro-quo kind of way," he says. "It's good advice to follow though. Make sure your hands are clean before seeking equity from the courts."

Lawyers may also be able to avoid litigation altogether, says Nagle, by trying to resolve the matter out of court.

"Send out a demand letter in advance, and ask for the conduct to cease and desist," he says. Even if it doesn't work, "if you look reasonable and the other side looks obstinate to what the legal considerations are, you'll have some momentum going into litigation."

Nagle notes that crafting a non-solicitation agreement, rather than a non-compete agreement, may be enough to protect some business interests such as goodwill.

"Some clients will learn that they don't need broad non-competes, but what they need is an agreement not to solicit customers the salesperson has had direct contact with," he explains. "If they focus their documents on what they're trying to protect, they're going to avoid a lot of conflict."

Ian Crawford of Boston says that if a case ends up in court, one of the best ways a lawyer can arm himself is to look at past opinions from the judge sitting on the case to get a feel for what he finds important.

"Some judges emphasize a bit more of the contract enforcement [aspect], while other judges will examine the facts a little more fully, and there's almost a fairness assessment there," he says, noting that "there's a fairly good body of law being developed in the Business Litigation Session — a lot of non-competes."

Others agree with Crawford, but add a word of caution.

"Be familiar with the decisions that have come before, but past isn't always prologue," warns Christopher R. O'Hara of Boston. "These are very fact-intensive cases." MLW

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