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**NON-SOLICITATION CLAUSES  
IN EMPLOYMENT AGREEMENTS**

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## I. NON-SOLICITATION CONTRACTS AND RELATED PROVISIONS

Non-solicitation clauses are an important employer tool in preventing an ex-employee from damaging the employer's business interests by soliciting customers or employees. Without a non-solicitation covenant or the broader and often accompanying non-compete covenant, an employee is free to leave employment, solicit and serve the ex-employer's customers, recruit and hire away employees, and compete with a former employer so long as no confidential information is used. *Multitherm Corp. v. Fuhr*, 1991 WL 146233, \*20 (E.D. Pa.). An at-will employee may even take steps to prepare to solicit customers before leaving, e.g., by scheduling appointments with (but not actually soliciting) customers, so long as the employee does not solicit customers or engage in other conduct directly damaging to the employer during employment. See *The New L&N Sales and Marketing, Inc. v. Menaged*, 1998 WL 575270, \*7 (E.D. Pa. 1998).

### A. Types of Non-solicitation Clauses

1. **Customer non-solicitation covenants** typically prohibit the ex-employee from initiating any contact with customers of the employer (See, e.g., *Bell Fuel Corp. v. Cattolico*, 375 Pa. Super. 238, 544 A.2d 450 (1988), *appeal denied*, 520 Pa. 612, 554 A.2d 505 (1989); *Merrill, Lynch, Pierce, Fenner and Smith, Inc. v. Napolitano*, 85 F.Supp.2d 491 (E.D. Pa. 2000)).
  - a. Non-solicitation covenants are limited by the reasonableness requirements that govern non-competes (*Bell Fuel Corp. v. Cattolico*, *supra*, 544 A.2d at 458). Therefore, courts may limit the enforcement of these covenants as follows:
    - (1) to prohibit contacts with only those customers with whom the employee did business for the former employer. See, e.g., *Robert Half of PA, Inc. v. Feight*, 48 Pa. D. & C.4<sup>th</sup> 129 (Phila. Co. 2000).
    - (2) to prohibit only solicitation of customers for products sold by the ex-employer. See, e.g., *United Products Corp. v. Trans-Tech Manufacturing Co.*, 2000 WL 33711051

(Phila. Co. 2000).

- b. A covenant that an ex-employee may not “solicit, divert, or take away” customers allows an ex-employee to accept customers who seek out the ex-employee. *Merrill, Lynch, Pierce, Fenner & Smith, Inc. v. Moose*, 365 Pa. Super. 40, 528 A.2d 1351 (1987), *appeal denied*, 518 Pa. 641, 542 A.2d 1370 (1988); *Harry Blackwood, Inc. v. Caputo*, 290 Pa. Super. 140, 434 A.2d 169 (1981); *Rubel & Jensen Corp. v. Rubel*, 85 N.J. Super. 27, 203 A.2d 625 (1964).
- c. Covenants against accepting customers are separate and distinct from, and more stringent than, non-solicitation covenants. *See, e.g., Frank Russell Co. v. Wellington Management Co.*, 154 F.3d 97 (3d Cir. 1998); *Commerce National Insurance Services, Inc. v. Buchler*, 2003 WL 22953225, \*3 fn. 1 (D. Del.), *aff’d*, 120 Fed. Appx. 414 (3d Cir. 2004). Such covenants are less stringent than non-compete covenants that restrict an ex-employee from any employment with a competitor. *See, e.g., Advanced Fox Antenna, Inc. v. Cszaszar*, 1999 WL 54567 (E.D. Pa. 1999), and *Thermo-Guard, Inc. v. Cochran*, 408 Pa. Super. 54, 596 A.2d 188 (1991), in which the courts enjoined ex-employees from customer contact but refused to enforce the non-competes, thereby allowing the ex-employee to continue in the new employment.
- d. NOTE: The term “customer” is subject to varying definitions. If a non-solicitation clause prohibits solicitation of former customers, the courts will enforce the prohibition to the extent that the prohibition is reasonable. *See, e.g., Cooper v. Cerelli*, 2002 WL 1758351 (Phila. Co.) (“customer” defined to include clients within one year before employee’s departure); *Graphic Management Associates, Inc. v. Hatt*, 1998 WL 159035 (E.D. Pa.) (agreement prohibited employee from soliciting any entity that was a customer during the term of employee’s employment). In the absence of such an

expansive definition of customers, the courts will interpret “customers” to mean current customers at the time of the employee’s departure and will not enforce the restrictions more broadly. *Doyle Consulting Group, Inc. v. Stoffel*, 2004 WL 362316 (Phila. Co.), *aff’d*, \_\_\_ A.2d \_\_\_ (Pa. Super. Nov. 29, 2004).

2. **Employee non-solicitation covenants** or “anti-piracy” covenants prohibit employees from soliciting other employees to leave and join a new organization. *See, e.g., Unisys Corp. v. Entex Information Services Inc.*, 45 Pa. D. & C.4<sup>th</sup> 405 (Montg. Co. 2000). Courts in Pennsylvania courts have shown some reluctance to find violations of such agreements. *See, e.g., Diversey Lever, Inc. v. Hammond*, 1997 WL 28711, \*23 (E.D. Pa. 1997), *aff’d*, 116 F.3d 467 (3d Cir. 1997).

## B. **Essential Elements of a Non-Solicitation Covenant**

1. **Description of circumstances of entry** – This provision should set forth the relationship between the parties and the consideration for entry into the covenant (e.g., commencement of a job, increase in compensation, etc.).
2. **Description of restrictions** – See I, A, above.
3. **Duration of restrictions**
  - a. The covenant should prohibit some or all the activities set forth in I, A for a period of time after the employee leaves the employer.
  - b. The durational restriction may be tied to activities that took place within a stated period of time before departure (e.g., a one-year restriction on doing business with any customer who transacted business with the employer within six months before the employee’s departure). *See, e.g., Diversey Lever, Inc. v. Hammond*, 1997 WL 28711, \*5 (E.D. Pa. 1997), *aff’d*, 116 F.3d 467 (3d Cir. 1997); *M. S. Jacobs & Associates, Inc. v. Duffley*, 452 Pa. 143, 303 A.2d 921 (1973).

- c. The covenant may contain an “elastic” provision extending the covenant’s prohibitions in the event of violations by the employee. A typical “elastic” provision will postpone commencement of any restrictions until either the employee ceases all violations or a court enforces the restrictions. *See, e.g., Diversey Lever, Inc. v. Hammond, supra.* An “elastic” provision protects the employer against expiration of the covenant during the pendency of litigation, an event that will preclude enforcement of even a valid restrictive covenant. *See, e.g., Hayes v. Altman*, 438 Pa. 451, 266 A.2d 269 (1970).
  - d. DRAFTING NOTE: The triggering event for the durational restriction should be the end of employment, not the end of the contract, since an employment contract may expire before the employee’s employment. *See, e.g., Boyce v. Smith-Edwards-Dunlap Co.*, 398 Pa. Super. 345, 580 A.2d 1382 (1990), *appeal denied*, 527 Pa. 639, 650, 593 A.2d 413, 422 (1991); *Geisinger Clinic v. DiCuccio*, 414 Pa. Super. 85, 606 A.2d 509 (1992), *appeal denied*, 536 Pa. 625, 637 A.2d 285 (1993), *cert. denied*, 513 U.S. 1112, 115 S. Ct. 904 (1995). The covenant should also explicitly survive termination of the contract and the employee’s employment.
4. **Geographic restrictions** typically prevent activities within a specified geographic area (e.g., within a 100-mile radius of Philadelphia, or within a 50-mile radius of any of the employer’s offices). These are less typical in non-solicitation clauses than non-competes because non-solicitation clauses typically focus on customers and employees rather than a geographic area. As such, non-solicitation clauses contain implied geographic limitations. *Bell Fuel Corp. v. Cattolico*, 375 Pa. Super. 238, 544 A.2d 450, 458 (1988), *appeal denied*, 520 Pa. 612, 554 A.2d 505 (1989).
5. **Enforcement tools** – A non-solicitation covenant may

contain many more provisions designed to facilitate the employer's enforcement of the covenant, including the following:

- a. **Consent to injunctive relief** – *See, e.g., Merrill, Lynch, Pierce, Fenner and Smith, Inc. v. Napolitano*, 85 F.Supp.2d 491 (E.D. Pa. 2000).
- b. **Provision for partial relief** – Although such a provision may help a court to modify the covenant, Pennsylvania law allows a court to reduce the scope of a restrictive covenant even without such a clause. *See, e.g., Bell Fuel Corp. v. Cattolico, supra.*
- c. **Choice-of-law clause** – *See, e.g., BABN Technologies Corp. v. Bruno*, 1998 WL 720171 (E.D. Pa. 1998), recognizing the effect of a choice-of-law clause on the court's power to modify a restrictive covenant.
- d. **Forum selection clause** – Courts will uphold a clause establishing Pennsylvania as a forum unless it is clearly unjust, or a product of fraud or coercion. *See Behavioral Health Industry News, Inc. v. Lutz*, 24 F.Supp.2d 401 (M.D. Pa. 1998); *compare Dentsply International, Inc. v. Benton*, 965 F.Supp. 574 (M.D. Pa. 1997) (invalidating forum selection clause).
- e. **Consent to (or waiver of objection to) personal jurisdiction** – *Behavioral Health Industry News, Inc. v. Lutz, supra.*

NOTE: This clause is important for the same reason that the forum selection clause is important. It is advisable to include a consent both to jurisdiction in specified courts and to a specified manner of service of process.

- f. **Consent to expedited discovery**
- g. **Arbitration clause** – In industries such as the

securities industry, it is the practice to arbitrate all claims arising from employment, even the violation of restrictive agreements. Standard employment agreements in such industries include an arbitration clause (*See, e.g., Merrill, Lynch, Pierce, Fenner and Smith, Inc. v. Rodger*, 75 F.Supp.2d 375 (M.D. Pa. 1999)).

- h. **Consent to injunction as a carve-out from arbitration** – It may be essential to quick enforcement of a restrictive covenant to allow a proceeding for an injunction against an ex-employee as an addition to or an exception to an employment contract’s arbitration clause. (*Merrill, Lynch, Pierce, Fenner and Smith, Inc. v. Rodger*, 75 F.Supp.2d 375 (M.D. Pa. 1999)). Although the Pennsylvania courts will grant preliminary injunctive relief pending arbitration without contractual authorization (*Merrill, Lynch, Pierce, Fenner and Smith, Inc. v. Moose*, 365 Pa. Super. 40, 528 A.2d 1351 (1987), *appeal denied*, 518 Pa. 641, 542 A.2d 1370 (1988)), a court in Delaware has refused to grant injunctive relief in the absence of a contractual provision allowing this bypass of arbitration. *Merrill, Lynch, Pierce, Fenner and Smith, Inc. v. Shin*, 1984 WL 8203 (Del.Ch.).
- i. **Damages provisions**, which may include forfeiture clauses (*See Bettinger v. Carl Berke Association, Inc.*, 455 Pa. 100, 314 A.2d 296 (1974)); provisions for an accounting of profits (*See DeMuth v. Miller*, 438 Pa. Super. 437, 652 A.2d 891 (1995) *appeal denied*, 542 Pa. 634, 665 A.2d 469 (1995), *cert. denied*, 516 U.S. 1114, 116 S. Ct. 916 (1996)); or a provision for liquidated damages (*Geisinger Clinic v. DiCuccio*, 414 Pa. Super. 85, 606 A.2d 509 (1992) *appeal denied*, 536 Pa. 625, 637 A.2d 285 (1993), *cert. denied*, 513 U.S. 1112, 115 S. Ct. 904 (1995)). A provision for the award of damages is not inconsistent with the entry of an injunction (*See Bettinger v. Carl Berke Association, Inc.*, *supra*), although a plaintiff may elect to pursue only liquidated damages relief (*See Geisinger Clinic v.*

*DiCuccio, supra*).

- j. **Provision for attorney's fees** - Courts will enforce a provision awarding attorney's fees to a prevailing party (*See Profit Wize Marketing, Inc. v. Wiest*, 812 A.2d 1270 (Pa. Super. 2002) (holding that a plaintiff that settled an underlying action was not a "prevailing" party and contrasting the definition of "prevailing" party under the civil rights laws); *Mrozek v. Eiter*, 805 A.2d 535 (Pa. Super. 2002), *appeal denied*, 573 Pa. 691, 825 A.2d 639 (2003) (where court reduced scope of non-compete to prohibit solicitation only, covenant was reformed, and provision for attorney's fee recovery where covenant was breached did not apply)).
- k. **Non-waiver clauses**, authorizing the employer to enforce restrictions even if the employer has earlier declined to do so.
- l. **Assignability provisions** – In *Hess v. Gebhard & Co., Inc.*, 570 Pa. 148, 808 A.2d 912 (2002), the Pennsylvania Supreme Court held that, in a sale of assets, a restrictive covenant is not assignable to a purchasing business in the absence of a specific assignability provision in the covenant. *See also All-Pak, Inc. v. Johnston*, 694 A.2d 347 (Pa. Super. 1997) (refusing to enforce a restrictive covenant that lacked a general assignability clause where the party seeking enforcement was the successor by merger to the employer that had entered into the covenant) and *Fonda Group, Inc. v. Erving Industries, Inc.*, 897 F.Supp. 230 (E.D. Pa. 1995). *Compare Siemens Medical Solutions Health Services Corp. v. Carmelengo*, 167 F.Supp.2d 752 (E.D. Pa. 2001), holding that new owner's purchase of 100% of employer's stock did not constitute change in "employer" that would discharge employee from non-solicitation covenant. For complete assignability, the restrictive covenant should explicitly bind and benefit successors and assigns, and any purchase or sale agreement should explicitly mention assignment of the restrictive covenants (*see*

*Villanova Health Corp. v. Hawrylak*, 1998 WL 961374 (E.D. Pa. 1998)).

C. **Requirements for an Enforceable Non-Solicitation Clause**

1. **The covenant must be ancillary to employment**

- a. A non-solicitation covenant submitted to an employee as part of a comprehensive employment agreement two days after starting employment has been held to be ancillary to employment (*Beneficial Finance Co. of Lebanon v. Becker*, 422 Pa. 531, 222 A.2d 873 (1966)).
- b. The “ancillary” rule is different for unionized employees; under federal common law, a covenant in a pre-existing collective bargaining agreement is “ancillary” to employment for employees who begin work subsequently (*Prudential Insurance Co. of America v. Stella*, 994 F.Supp. 308 (E.D. Pa. 1998)).

2. **The covenant must be supported by consideration**, which may include either the extension of an initial offer of employment (even at-will employment) or a beneficial change in the terms and conditions of employment.

- a. Among the items that courts have upheld as sufficient consideration are agreements to pay increased compensation, profit sharing benefits, increased severance benefits, and stock options.
- b. The following items have been held **not** to constitute sufficient consideration to support non-solicitation covenants under Pennsylvania law:
  - (1) threat of loss of employment upon refusal to sign a restriction (*In re Verdi*, 244 B.R. 314 (Bankr. E.D. Pa. 2000));
  - (2) mere continuation of employment, even at-will employment (*National Risk Management, Inc. v. Bramwell*, 819 F.Supp.

417 (E.D. Pa. 1993)).

3. **The covenant must be reasonably necessary to protect the legitimate interests of an employer**

Courts will uphold a covenant as reasonably necessary to protect an employer's legitimate interests if the covenant is necessary to protect one or more of the following:

- a. the employer's goodwill in its customer relationships (*See Harsco Corp. v. Klein*, 395 Pa. Super. 212, 576 A.2d 1118 (1990) (refusing to enforce covenant); *Robert Half of PA, Inc. v. Feight*, 48 Pa. D. & C.4<sup>th</sup> (Phila. Co.) (enforcing covenant to limited extent; prohibiting solicitation and serving of clients served at former firm) and *In re Integrated Health Services, Inc.*, 281 B.R. 231 (Bankr. D.Del. 2002) and *DuMont Pharmaceutical Co. v. Latinsky*, 23 Pa. D. & C.2d 611 (Phila. Co. 1960) (refusing to enjoin solicitation of customers who were not exclusively ex-employer's customers)).
- b. the employer's trade secrets or confidential business information.
  - (1) Under the Uniform Trade Secrets Act ("UTSA"), now adopted in Pennsylvania, customer information may constitute a trade secret if the information (1) derives independent economic value from not being generally known to or readily ascertainable by others who could obtain economic value from disclosing or using the information and (2) is the subject of reasonable efforts to protect its secrecy. 12 Pa. C. S. § 5302.
  - (2) Before the enactment of the UTSA, courts in Pennsylvania applied similar principles to protect the following customer information in non-solicitation cases:
    - (a) a travel company's password-protected customer lists that were

specifically purchased in an asset purchase (*O.D. Anderson, Inc. v. Cricks*, 815 A.2d 1063 (Pa. Super. 2003)).

- (b) a route salesman/collector's customer information, even if used by memory with new employer (*Morgan's Home Equipment Corp. v. Martucci*, 390 Pa. 618, 136 A.2d 838 (1957)).
- (c) a security alarm firm's information about customers' businesses (*Robinson Electric Supervisory Co. v. Johnson*, 397 Pa. 268, 154 A.2d 494 (1959)).
- (d) a medical or dental practice's patient list (*Pollack v. Skinsmart Dermatology and Aesthetic Center*, 68 Pa. D. & C.4<sup>th</sup> 416 (Phila. Co. 2004); *In re Phoenix Dental Systems, Inc.*, 144 B.R. 22 (Bankr. W.D. Pa. 1992)). In *Phoenix Dental Systems, supra*, the Court allowed the departing dentist to retain only personal friends and relatives as patients but prevented access to any other patients (even those generated by the dentist's own contacts and efforts) because the patients came to the dentist as a result of the firm's facilities and services.
- (e) an insurance firm's customer directory including customer data, charges, and renewal dates (*A. M. Skier Agency, Inc. v. Gold*, 747 A.2d 936 (Pa. Super. 2000)); similar data plus customers' types of coverage, special insurance needs, and underwriting information (*Hall v. Hondru*, 29 Pa. D. & C.3d 270

(Alleg. Co. 1983)).

- (3) Customer lists or information are not protectible trade secrets if the information is widely known or readily ascertainable from an independent source, or from the employee's own efforts. Therefore, courts have refused to protect the following customer information:
- (a) route listings in the dairy business (*Carl A. Colteryahn Dairy, Inc. v. Schneider Dairy*, 415 Pa. 276, 203 A.2d 469 (1964)).
  - (b) names and styling preferences memorized by hairdresser (*Renee Beauty Salons v. Blose-Venable*, 438 Pa. Super. 601, 652 A.2d 1345 (1995) *appeal denied*, 541 Pa. 627, 661 A.2d 874 (1995)).
  - (c) the identity of customers who are widely known throughout the industry (*Agra Enterprises, Inc. v. Brunozzi*, 302 Pa. Super. 166, 448 A.2d 579 (1982); *Harsco Corp. v. Klein*, 395 Pa. Super. 212, 576 A.2d 1118 (1990)).
  - (d) a list compiled on salesman's own, largely through trade journals and telephone directories (*Spring Steels, Inc. v. Molloy*, 400 Pa. 354, 162 A.2d 370 (1960)).
  - (e) a list of hiring contacts at law firms, which could be compiled simply by calling the firms (*Robert Half of PA, Inc. v. Feight*, 48 Pa. D. & C.4<sup>th</sup> 129, 155 (Phila. Co. 2000)).
  - (f) An employee's personal business

contacts, even those made during service to an employer (*National Risk Management, Inc. v. Bramwell*, 819 F.Supp. 417, 431 (E.D. Pa. 1993)).

(g) Price information that could be obtained readily from customers. (*Olympic Paper Co. v. Dubin Paper Co.*, 60 Pa. D. & C.4<sup>th</sup> 102 (Phila. Co. 2000)).

(4) An employee who brings customers to a business from a firm that the employee owned may have the freedom to later leave the business with those same customers. *See, e.g., Fidelity Fund, Inc. v. DiSanto*, 347 Pa. Super. 112, 500 A.2d 431 (1985); *but see Merrill, Lynch, Pierce, Fenner and Smith, Inc. v. Napolitano*, 85 F.Supp.2d 491 (E.D. Pa. 2000) (employee may contractually assign customers to new employer in non-solicitation contract); and *A. M. Skier Agency, Inc. v. Gold*, 747 A.2d 936 (Pa. Super. 2000) (employee subject to non-compete in previous employment will not be treated as “bringing” customers to new employer).

c. NOTE: Under Pennsylvania law, the reasonableness of a restrictive covenant is an issue only in an action for injunctive relief to enforce the covenant; reasonableness is not at issue in an action for damages for breach of the covenant. *Boyce v. Smith-Edwards-Dunlap Co.*, 398 Pa. Super. 345, 580 A.2d 1382 (1990), *appeal denied*, 527 Pa. 639, 650, 593 A.2d 413, 422 (1991). New Jersey law considers the reasonableness of a non-solicitation clause in damage actions as well as injunctions. *Platinum Management Co. v. Dahms*, 285 N.J. Super. 274, 666 A.2d 1028, 1039 (1995).

#### 4. **The covenant must be reasonable in duration**

In general, courts will only enforce a non-solicitation covenant for so long as it is necessary for the employer to hire and train a new person to replace the departing employee, and to restore the employer's customer relations and goodwill. The maximum reasonable duration of non-solicitation covenants is typically less than the maximum reasonable duration of non-compete covenants. Courts have enforced non-solicitation agreements for three years, limited to actual sales territory, for an insurance agent in Pennsylvania (*Harry Blackwood, Inc. v. Caputo*, 290 Pa. Super. 140, 434 A.2d 169 (1981) (reduced from five years)); and for three years in New Jersey (*Pilgrim Coat, Apron & Linen Service v. Krzywulak*, 141 N.J. Eq. 212, 56 A.2d 584 (1948)).

**One year** is the most typical duration for a non-solicitation covenant. In *Merrill, Lynch, Pierce, Fenner and Smith, Inc. v. Napolitano*, 85 F.Supp.2d 491 (E.D. Pa. 2000), the District Court enforced a one-year non-solicitation covenant against a stockbroker who left Merrill, Lynch to join a rival brokerage firm. The Court's order encompassed not only the brokerage firm's customers, but the broker's own customers brought from a previous employer, which the broker had assigned to Merrill, Lynch. The Court noted that the broker had consented to injunctive relief. The broker claimed that he had not solicited accounts by announcing his new affiliation and stating to his customers that they were "free to do what they want with their accounts." The Court dismissed this argument as "disingenuous." *Merrill, Lynch v. Napolitano*, 85 F.Supp.2d at 496. For other one-year non-solicitation covenants upheld by the courts, see *Morgan's Home Equipment Co. v. Martucci*, 390 Pa. 618, 136 A.2d 838 (1957); *Source Services Corp. v. Gaul*, 1990 WL 50819 (E.D. Pa.); *RHIS, Inc. v. Boyce*, 2001 WL 1192203 (Del. Ch.); and *Terminix International v. WMPC, Inc.*, 20 Phila. Co. Rptr. 300, 1989 WL 817173 (1989), *aff'd*, 406 Pa. Super. 672, 583 A.2d 840 (1990).

5. **The covenant must be reasonable in geographic scope**

Because non-solicitation clauses typically focus on

customers and employees rather than a geographic area, non-solicitation clauses contain implied geographic limitations. *Bell Fuel Corp. v. Cattolico*, 375 Pa. Super. 238, 544 A.2d 450, 458 (1988), *appeal denied*, 520 Pa. 612, 554 A.2d 505 (1989). A prohibition against soliciting customers in the employee's actual sales territory is generally reasonable. *Certified Laboratories of Texas, Inc. v. Rubinson*, 303 F.Supp. 1014 (E.D. Pa. 1969); *Research & Trading Co. v. Pfuhl*, 1992 WL 345465 (Del. Ch.). The court may also limit the covenant to those customers known to the employee (*Diversey Lever, Inc. v. Hammond*, 1997 WL 28711 (E.D. Pa. 1997), *aff'd*, 116 F.3d 467 (3d Cir. 1997)). A court will be reluctant to enjoin solicitation in the area outside the ex-employee's territory. *Certified Laboratories of Texas, Inc. v. Rubinson*, *supra* (refusing to enforce contract prohibiting solicitation within 45 miles of the salesperson's territory); *R.L. Guttridge, Inc. v. Wean*, 8 N.J. Super. 450, 73 A.2d 284 (1950) (court refused to enjoin solicitation in Pennsylvania when salesperson was active only in New Jersey). A contrasting decision is *Rubel & Jensen Corp. v. Rubel*, 85 N.J. Super. 27, 203 A.2d 625 (1964), upholding a non-solicitation covenant in an area beyond the employee's actual sales territory; the court said that the covenant would have no effect at all because the ex-employer had no customers in this area. *Rubel*, *supra*, 203 A.2d at 630-631.

## II. NON-CONTRACTUAL PROTECTIONS AGAINST SOLICITATION

### A. Breach of Fiduciary Duty Claims

1. **The law of agency** – Under Pennsylvania law, employees and many independent contractors are agents of the hiring entity. An agent owes a duty of loyalty to the principal (the employer or hiring entity) to act solely for the benefit of the principal in all matters connected with the agency.
  - a. In furtherance of this duty, the agent must disclose all actual or potential business opportunities to the principal during the term of the agency, and may not take personal advantage of such business opportunities. *See* Restatement (Second), Agency §

393 *et seq.*; *SHV Coal, Inc. v. Continental Grain Co.*, 376 Pa. Super. 241, 545 A.2d 917 (1988), *reversed in part on other grounds*, 526 Pa. 489, 587 A.2d 702 (1991).

- b. After the termination of the agency, an agent has a duty to the principal not to take advantage of a still subsisting confidential relation created during the prior agency. *See Adler, Barish, Daniels, Levin & Creskoff v. Epstein*, 482 Pa. 416, 393 A.2d 1175 (1978), *appeal dismissed*, 442 U.S. 907, 99 S.Ct. 2817 (1979).
- c. An agent who is employed at will does not violate a fiduciary duty by preparing to compete while still employed. *United Aircraft Corp. v. Boreen*, 413 F.2d 694, 700 (3d Cir. 1969).

2. **Examples of fiduciary duty violations** – A violation of an agent’s fiduciary duty typically occurs when an agent is leaving for a new assignment, and diverts business from the former entity’s client or customer to the benefit of the new employer. Specific examples include the following:

- a. Diversion of a customer contract. *See SHV Coal, Inc. v. Continental Grain Co.*, *supra*.
- b. Solicitation of a firm’s clients. *See Adler, Barish, Daniels, Levin & Creskoff v. Epstein*, *supra*.
- c. Solicitation of other employees in a conspiracy to divert business. *See, e.g., Reading Radio, Inc. v. Fink*, 833 A.2d 199, 211 (Pa. Super. 2003), *appeal denied*, 577 Pa. 723, 847 A.2d 1287 (2004); *Frederick Chusid & Co. v. Marshall Leeman & Co.*, 279 F.Supp. 913 (S.D. N.Y. 1968).
- d. Deliberate provision of inferior products or service while working for an employer, resulting in a weakening of the employer’s competitive position. *The New L&N Sales and Marketing, Inc. v. Menaged*, 1998 WL 575270, \*7 (E.D. Pa. 1998).

3. **Remedies** – An agent’s breach of fiduciary duty will enable the principal to obtain injunctive relief where the principal’s damages are not ascertainable (*United Board & Carton Co. v. Britting*, 63 N.J. Super. 517, 164 A.2d 824 (1959)) or to obtain the following compensation:
  - a. An accounting of the agent’s profits from the breach.
  - b. Compensatory damages.
  - c. Punitive damages.
  - d. Repayment of compensation paid to the disloyal agent beginning on the date of the agent’s breach.

*See SHV Coal, Inc. v. Continental Grain Co.*, 376 Pa. Super. 241, 545 A.2d 917, 924 (1988); *SHV Coal, Inc. v. Continental Grain Co.*, 526 Pa. 489, 587 A.2d 702 (1991) (reversing Superior Court in part so as to award punitive damages).

## B. **Intentional interference claims**

1. **Elements of cause of action for intentional interference with existing or prospective contractual relations**
  - a. the existence of an actual or prospective contract;
  - b. the defendants’ purpose or intent to harm the plaintiff by preventing completion of the contract;
  - c. improper conduct (i.e., absence of privilege) on the part of defendants; and
  - d. harm resulting from the defendants’ actions.

One who, without a privilege to do so, induces or purposely causes a third party (not the party’s employer) not to (a) perform a contract with another or (b) enter into or continue a business relation with another, is liable to the other for the harm caused thereby. Restatement (Second) of Torts (1979), § 766; *Adler, Barish, Daniels, Levin &*

*Creskoff v. Epstein*, 482 Pa. 416, 393 A.2d 1175, 1182 (1978), *appeal dismissed*, 442 U.S. 907, 99 S.Ct. 2817 (1979). The tort of intentional interference may arise where a new employer or key employee encourages employees or customers to leave a business. *See, e.g., National Risk Management, Inc. v. Bramwell*, 819 F.Supp. 417, 433 (E.D. Pa. 1993); *Morgan's Home Equipment Corp. v. Martucci*, 390 Pa. 618, 633, 634, 136 A.2d 838, 847 (1957) Absence of privilege (i.e., an improper purpose) may be inferred from an employee's breach of a duty of loyalty to an employer. *See Adler, Barish, Daniels, Levin & Creskoff v. Epstein, supra*, 393 A.2d at 1184-1185.

The new employer has the obligation to conduct due diligence during the hiring process as to any candidate's post-employment restrictions. The employee has no duty to volunteer information about such restrictions. *See Zimmerman v. Commonwealth, Unemployment Compensation Board of Review*, 836 A.2d 1074 (Pa. Cmwlth. 2003) (employee who failed to disclose non-compete with earlier employer did not commit willful misconduct so as to preclude unemployment compensation). The duty to inquire about restrictions is even greater if the new employer itself imposes post-employment restrictions. *See First Health Group Corp. v. National Prescription Administrators, Inc.*, 155 F.Supp.2d 194, 234 (M.D. Pa. 2001); *Mixing Equipment Corp. v. Philadelphia Gear, Inc.*, 312 F.Supp. 1269 (E.D. Pa. 1969), *aff'd in part, reversed in part*, 436 F.2d 1308 (3d Cir. 1971).

2. **Intentional interference issues in inducing employees to leave employer**
  - a. Offering employment to another employer's at-will employee is not actionable by itself (*Morgan's Home Equipment Corp. v. Martucci*, 390 Pa. 618, 136 A.2d 838 (1957)).
  - b. Offering employment that violates an employee's restrictive covenant may constitute intentional interference (*Reading Radio, Inc. v. Fink*, 833 A.2d 199, 211-212 (Pa. Super. 2003), *appeal denied*, 577

Pa. 723, 847 A.2d 1287 (2004)).

- c. The systematic inducement of employees to leave their present employment and work with another is unlawful when the purpose is to cripple and destroy an integral part of a competitive business or organization, rather than to obtain the services of particularly gifted or skilled employees (*Morgan's Home Equipment Corp. v. Martucci*, 390 Pa. at 633-634, 136 A.2d at 847).
- d. It is actionable to induce employees for the purpose of having the employees commit wrongs, such as disclosing a former employer's trade secrets or enticing away a former employer's customers (*Morgan's Home Equipment Corp. v. Martucci, supra*).

### 3. Remedies

An employer may obtain both damages and equitable relief in an action for tortious interference with contractual relations. See *Joseph D. Shein, P.C. v. Myers*, 394 Pa. Super. 549, 576 A.2d 985, 988 (1990), *appeal denied*, 533 Pa. 600, 617 A.2d 1274 (1991).

### C. Civil Conspiracy

A claim for civil conspiracy is an ancillary tort claim, which may apply in situations where departing employees and a new employer compete improperly. Under Pennsylvania law, a "conspiracy" is a combination of two or more persons acting with a common purpose to do an unlawful act by unlawful means for an unlawful purpose, an overt act done in pursuant of the common purpose, and actual legal damage. *Reading Radio, Inc. v. Fink*, 833 A.2d 199, 212-213 (Pa. Super. 2003) *appeal denied*, 577 Pa. 723, 847 A.2d 1287 (2004).

1. Proof of malice is an essential part of a cause of action for conspiracy. *Reading Radio, Inc. v. Fink, supra*.
2. Lawful competition does not constitute a conspiracy. See

*Agra Enterprises, Inc. v. Brunozzi*, 302 Pa. Super. 166, 448 A.2d 579 (1982).

3. A corporate entity cannot be liable for civil conspiracy for actions taken with its own agents. *Patient Transfer Systems, Inc. v. Patient Handling Solutions, Inc.*, 1999 WL 54568 (E.D. Pa. 1999).

### **III. LITIGATION TO ENFORCE RESTRICTIONS**

#### **A. Proceedings for Temporary or Special Injunction**

1. F.R.C.P. 65(b) authorizes the entry of a temporary restraining order upon motion if it clearly appears from specific facts shown by affidavit or verified complaint that immediate and irreparable harm will result to the applicant before the adverse party can be heard in opposition, and the applicant's attorney certifies to the court in writing the efforts that have been made to give proper notice. Under Rule 65(b), a TRO granted without notice expires after 10 days in the absence of extension for good cause or by consent of the adverse party.
2. Pa. R.C.P. 1531(a) authorizes entry of a special injunction without notice or hearing if it appears to the satisfaction of the court that immediate and irreparable injury will be sustained before notice can be given or a hearing held. Pa. R.C.P. 1531(d) automatically dissolves any injunction granted without notice unless a hearing on the continuance of the injunction is held within five (5) days after the granting of the injunction, or within such other time as the parties agree or the court may direct.

NOTE: The Pennsylvania Rules do not recognize a pleading titled "temporary restraining order," only a pleading entitled "special injunction." Use of the term "temporary restraining order" in Pennsylvania courts may lead to confusion with "preliminary injunction," with adverse consequences for the plaintiff's attorney if the request for injunction is denied.

#### **B. Proceedings for Preliminary Injunction**

1. General criteria for preliminary injunction

- a. **State court** – A preliminary injunction may be granted if:
- (1) the rights of the plaintiff are clear (i.e., plaintiff has a strong likelihood of success on the merits);
  - (2) an injunction is necessary to prevent irreparable harm which cannot be compensated by damages;
  - (3) greater injury would result by refusing the injunction than by granting it; and
  - (4) the preliminary injunction properly restores the parties to the status that existed immediately prior to the alleged wrongful conduct (*Bell Fuel Corp. v. Cattolico*, 375 Pa. Super. 238, 544 A.2d 450, 458 (1988), *appeal denied*, 520 Pa. 612, 554 A.2d 505 (1989)).
- b. **Federal court** – Under F.R.C.P. 65, the showings required for a preliminary injunction and for a temporary restraining order are essentially identical. The moving party must demonstrate:
- (1) a likelihood of success on the merits;
  - (2) the probability of irreparable harm if the relief is not granted;
  - (3) granting the relief will not result in greater harm to another party; and
  - (4) granting the relief is consistent with the public interest (*Merrill, Lynch, Pierce, Fenner and Smith, Inc. v. Napolitano*, 85 F.Supp.2d 491 (E.D. Pa. 2000)).

2. **Showing a likelihood of success on the merits**

A plaintiff seeking a preliminary injunction must show the following:

- a. The defendant agreed to a restrictive covenant.
- b. The covenant is enforceable (*See* I, C, above).
- c. The defendant is violating the covenant.

**3. Showing irreparable harm**

- a. Irreparable harm must be pleaded and shown; it is not sufficient to stipulate in a contract that the ex-employer will suffer irreparable harm. *See Dice v. Clinicorp., Inc.*, 887 F.Supp. 803, 810 (W.D. Pa. 1995).
- b. An employee's interference with client or customer relations or misuse of trade secrets constitute irreparable harm, since such actions are not ascertainable and not capable of full compensation in money damages. *See Ogontz Controls Co. v. Pirkle*, 346 Pa. Super. 253, 499 A.2d 593 (1985).

**4. Possible defenses**

- a. failure to sign contract – In *Records Center, Inc. v. Comprehensive Management, Inc.*, 363 Pa. Super. 79, 525 A.2d 433 (1987), the Superior Court reversed an injunction against a former employee who had never signed a restrictive covenant.
- b. lack of consideration for the restriction – An employee forced to sign a restrictive covenant or be fired may defend against enforcement of the restrictive covenant on the basis of lack of consideration. *See In re Verdi*, 244 B.R. 314, 321 (Bankr. E.D. Pa. 2000).
- c. duress in signing covenant – An employee forced to “sign or be fired” may defend against enforcement of the restrictive covenant on the basis of duress. *See In re Verdi*, 244 B.R. 314, 321 (Bankr. E.D. Pa.

2000). NOTE: If the employee was represented by an attorney, the duress defense may not apply. *See Worldwide Auditing Services, Inc. v. Richter*, 402 Pa. Super. 584, 587 A.2d 772, 777 (1991).

- d. unreasonableness in duration – *See, e.g., Cooper v. Cerelli*, 2002 WL 1758351 (Phila. Co. 2002) (reducing two year period to one year).
- e. unreasonableness in geographic area – *See, e.g., Cooper v. Cerelli, supra* (reducing 100 mile area to 25 miles).
- f. expiration of the covenant – *See Hayes v. Altman*, 438 Pa. 451, 266 A.2d 269 (1970) (refusing to enforce expired non-compete covenant) *and Excellent Laundry Co. v. Szekeres*, 382 Pa. 23, 114 A.2d 176 (1955) (dismissing as moot an appeal from an injunction enforcing non-solicitation clause because restrictions had expired).
- g. absence of proof of violation of the covenant – *See, e.g., Rollins Protective Services, Inc. v. Shaffer*, 383 Pa. Super. 598, 557 A.2d 413 (1989) (injunction refused; no proof that ex-employee had knowingly solicited customers); *KPMG Peat Marwick LLP v. Fernandez*, 709 A.2d 1160 (Del. Ch. 1998) (no violation where competitor fired recruiter who solicited employees in violation of agreement).
- h. unclean hands – In *Salomon, Smith, Barney, Inc. v. Vockel*, 2000 WL 558580 (E.D. Pa. 2000), the United States District Court for the Eastern District of Pennsylvania refused to enforce a restrictive covenant against a departing stockbroker because of the brokerage firm’s own “unclean hands” in having earlier obtained many customers from the broker’s previous employer. The Court found that the plaintiff brokerage firm had once encouraged the stockbroker to engage in the same kind of unconscionable conduct that the brokerage firm now sought to restrain.

- i. a material breach or failure of consideration, e.g., through failure to pay employee – *See, e.g., Philadelphia Ear, Nose and Throat Surgical Associates, P.C. v. Roth*, 44 Pa. D. & C.4<sup>th</sup> 427 (Phila. Co. 2000).
- j. laches or waiver, through plaintiff’s failure to pursue or develop business.
- k. unreasonableness of enforcement after employee discharge for poor performance (*See, e.g., Insulation Corp. of America v. Brobston*, 446 Pa. Super. 520, 667 A.2d 729 (1995)), or other involuntary discharge through no fault of employee (*All-Pak, Inc. v. Johnston*, 694 A.2d 347 (Pa. Super. 1997)). NOTE: This defense appears to have succeeded only against attempts to enforce a non-compete clause; no case was found applying this defense against enforcement of a non-solicitation clause. In *Olympic Paper Co. v. Dubin Paper Co.*, 60 Pa. D. & C.4<sup>th</sup> 102 (Phila. Co. 2000), the court enforced a non-solicitation/non-serve clause to a limited extent despite the employee’s discharge for poor performance. In any event, the defense is not available where an employee is discharged for misconduct. *See DeMuth v. Miller*, 438 Pa. Super. 437, 652 A.2d 891 (1995), *appeal denied*, 542 Pa. 634, 665 A.2d 469 (1995), *cert. denied*, 516 U.S. 1114, 1116 S.Ct. 916 (1996) (employee violated employer’s prohibition against “homosexuality”).
- l. harm to the defendant through interference with the right to earn a living. Courts are not sympathetic to this defense where an ex-employee has violated a reasonable restriction. *See Merrill, Lynch, Pierce, Fenner and Smith, Inc. v. Napolitano*, 85 F.Supp.2d 491 (E.D. Pa. 2000).
- m. the interest of third parties such as customers or clients. In *Merrill, Lynch, Pierce, Fenner and Smith, Inc. v. Napolitano*, 85 F.Supp.2d 491, 498-499 (E.D. Pa. 2000) and *Merrill, Lynch, Pierce, Fenner and Smith, Inc. v. Rodger*, 75 F.Supp.2d

375, 383 (M.D. Pa. 1999), the courts held that the clients' interests in preserving a relationship with a broker did not outweigh the public interest in enforcement of contracts (*Merrill, Lynch v. Napolitano, supra*) or the firm's interest in its business investments and confidential customer information (*Merrill, Lynch v. Rodger, supra*). See also *Frank Russell Co. v. Wellington Management Corp.*, 154 F.3d 97 (3d Cir. 1998).

5. **Expedited Discovery** – Neither Federal nor Pennsylvania Rules permit expedited discovery; however, federal courts have granted expedited discovery in preliminary injunction proceedings for breaches of restrictive covenants or trade secret theft. See, e.g., *Educational Commission, Foreign Medical School Graduates v. Repik*, 1999 WL 317052 (E.D. Pa.). PRACTICAL TIP: In any motion for expedited discovery, ask that the length of any expedited depositions not be counted against the one-day, seven-hour limitation in F.R.C.P. 30 (d)(2).
6. **Bond** – Bond is mandatory under both Federal and Pennsylvania Rules. See F.R.C.P. 65(c); Pa. R.C.P. 1531(b). Absent a provision for bond, an order granting a special or preliminary injunction in Pennsylvania is void, but the defect is curable by amending the order to provide for bond, and obtaining the bond (*Downs v. Smythe*, 701 A.2d 591 (Pa. Super. 1997)).

## C. Damages

1. **Compensatory damages** – Compensatory damages for breach of a restrictive covenant need to be computed with “reasonable certainty”, not absolute mathematical certainty (*Scobell, Inc. v. Schade*, 455 Pa. Super. 414, 688 A.2d 715, 718-719 (1997)). In restrictive covenant cases, damages are often difficult to ascertain; therefore, the award of damages is not inconsistent with the entry of an injunction (*Bettinger v. Carl Berke Association, Inc.*, 455 Pa. 100, 314 A.2d 296 (1974)). In *Judge Technical Services, Inc. v. Clancy*, 813 A.2d 879 (Pa. Super. 2002), the Pennsylvania Superior Court affirmed a damage award of almost \$1.4 million for violations of non-solicitation and non-compete

agreements; the award divided almost equally into compensatory and punitive damages. The Court also affirmed a permanent injunction.

Among the elements recognized as possible damages in non-solicitation cases are the following:

- (a) lost profits (*Certified Laboratories of Texas, Inc. v. Rubinson*, 303 F.Supp. 1014 (E.D. Pa. 1969) (recognizing right to accounting for lost profits));

new employer's profits from improperly solicited customers (*Morgan's Home Equipment Corp. v. Martucci*, 390 Pa. 618, 626, 136 A.2d 838, 843 (1957));

- (c) lost orders (*Certified Laboratories of Texas, Inc. v. Rubinson, supra* (holding damages obtainable but plaintiff's proof deficient));
- (d) lost goodwill (*Certified Laboratories of Texas, Inc. v. Rubinson, supra* (holding damages obtainable but plaintiff's proof deficient)); and
- (e) lost client revenues (*Joseph D. Shein, P.C. v. Myers*, 394 Pa. Super. 549, 576 A.2d 985 (1990), *appeal denied*, 533 Pa. 600, 617 A.2d 1274 (1991)).

2. **Punitive damages** – *See generally, Judge Technical Services, Inc. v. Clancy, supra; Joseph D. Shein, P.C. v. Myers, supra; Certified Laboratories of Texas, Inc. v. Rubinson, supra.*
3. **Liquidated damages** may be awarded in a restrictive covenant case. *See DeMuth v. Miller*, 438 Pa. Super. 437, 652 A.2d 891 (1995); *Geisinger Clinic v. DiCuccio*, 414 Pa. Super. 85, 606 A.2d 509 (1992). The existence of a liquidated damages provision does not preclude injunctive relief (*Bettinger v. Carl Berke Association, Inc.*, 455 Pa. 100, 314 A.2d 296 (1974)).
4. **Attorney's fees** are awardable in restrictive covenant litigation. *See Certified Laboratories of Texas, Inc. v. Rubinson*, 303 F.Supp. 1014 (E.D. Pa. 1969).

## D. Counterclaims

1. **Injunction against enforcement of restrictions** – See *Allegheny Anesthesiology Associates, Inc. v. Allegheny General Hospital*, 826 A.2d 886 (Pa. Super. 2003), *appeal denied*, 577 Pa. 684, 844 A.2d 550 (2004) (granting injunction against enforcement of non-compete).
2. **Declaratory judgment of non-liability** – The former employee or new employer may also bring a pre-emptive action seeking a declaratory judgment of non-liability. See *Hillard v. Medtronic, Inc.*, 910 F.Supp. 173 (M.D. Pa. 1995), in which the ex-employer then filed for injunctive relief.
3. **Tort claims**
  - a. Defamation
    - (1) The former employer’s publication of a press release on the ex-employee’s violation of a restrictive covenant led to a defamation claim that withstood a motion to dismiss in *Unisource Worldwide, Inc. v. Heller*, 1999 WL 374180 (E.D. Pa. 1999).
    - (2) An employer’s letter to a succeeding employer stating the intent to act to protect a restrictive covenant is privileged in an action for defamation (*Gresh v. Potter McCune Co.*, 235 Pa. Super. 537, 344 A.2d 540 (1975)).
  - b. Intentional interference with contractual relations
    - (1) An accurate statement of a restrictive covenant is privileged (*Gresh v. Potter McCune Co.*, *supra*).
    - (2) Employers who overstated restrictions on an ex-employee, causing a new employer to fire the employee, have incurred substantial liability for punitive damages for intentional

interference with contractual relations in *Collincini v. Honeywell, Inc.*, 411 Pa. Super. 166, 601 A.2d 292 (1991), *appeal denied*, 530 Pa. 651, 608 A.2d ; 27 (1992), *cert. denied*, 506 U.S. 869, 113 S.Ct. 199 (1993); and *Ruffing v. 84 Lumber Co.*, 410 Pa. Super. 459, 600 A.2d 545 (1991), *appeal denied*, 530 Pa. 666, 610 A.2d 46 (1992).

- c. Unfair competition
- d. Commercial disparagement – This action is available only to attack the quality of an entity’s goods or products, not an individual’s character. *See, e.g., Unisource Worldwide, Inc. v. Heller, supra.*
- e. Wrongful institution of civil proceedings – Under 42 Pa. C.S. § 8351(a) (2), this action depends upon a favorable termination of the underlying action, and cannot be brought as a counterclaim.