TEN HOT ISSUES IN NONCOMPETE ENFORCEMENT

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I. CONSIDERATION

(A) *Commencement of Employment*

When a restrictive covenant is agreed to at the inception of employment, the courts will find that the covenant is supported by consideration. This simple rule begs the question of when employment begins. In *George W. Kistler, Inc. v. O'Brien*, 464 Pa. 475, 347 A.2d 311 (1975), the Pennsylvania Supreme Court held that an employer who tendered a comprehensive oral employment contract to an employee before employment began, without disclosing a noncompete, was required to offer additional consideration for the noncompete tendered to the employee on the first day of work. However, the courts have found consideration where the employee had notice of the noncompete before starting work. *See Nextgen Health Care Information Systems, Inc. v. Messier*, 2005 WL 3021095, * 4 (E.D. Pa. Nov. 10, 2005) (employee signed covenant 8 days after starting work, but had notice before he began working that he would have to sign such a restriction). Even if the employee had no notice before starting work that she would have to sign a covenant, the covenant may still be treated as ancillary to employment where the employee received only a rudimentary offer letter rather than a full contract before beginning work. *Fisher Bioservices, Inc. v. Bilcare, Inc.,* 2006 WL 1517382, *10 (E.D. Pa. May 31, 2006). Where a restrictive covenant is not entered into at the inception of employment, the courts require employers to provide additional consideration to the employee in the form of a beneficial change in the terms and conditions of employment. *See*, *Arthur J. Gallagher & Co. v. Reisinger,* 2007 WL 1877895 (W.D. Pa. June 11, 2007).

(B) *Threat of Termination*

Consideration does not exist to support a restrictive covenant when a current employee is told to sign the covenant under threat of termination. *Arthur J. Gallagher & Co. v. Reisinger,* 2007 WL 1877895 (W.D. Pa. June 11, 2007). *See also In re Verdi*, 244 B.R. 314 (Bankr. E.D. Pa. 2000).

(C) *Cancellation of Invalid Non-compete*.

In *Fres-Co System USA, Inc. v. Bodell*, 2005 WL 3071755, *3-4 (E.D. Pa. Nov. 15, 2005), the United States District Court for the Eastern District of Pennsylvania held that the cancellation of an invalid restrictive covenant was not sufficient consideration to support a new restrictive covenant for an existing employee. The employer had required its employees to enter into a restrictive covenant in 1998. In 1999, the employer became concerned that the 1998 agreement might be unenforceable for overbreadth. Therefore, the employer required the employees to enter into a new restrictive covenant that reduced certain restrictions in the 1998 agreement. However, the Court held that if the 1998 agreement was unenforceable, it followed that there were no restrictions on post-employment activity, and that the 1999 agreement did not decrease, but rather increased, the

restrictions on the employee's post-employment conduct. *See Fres-Co System USA, Inc. v. Bodell*, 2005 WL 3071755, *4 (E.D. Pa. Nov. 15, 2005).

(D) *Recurring Covenants*

Separate covenants that the parties sign periodically during an employee's tenure may each provide consideration for post-employment restrictions. Consideration will exist when the employer hires the employee for discrete, recurring, short periods of employment and the employee signs the covenant at the commencement of each term of employment. *See Perry v. H&R Block Eastern Enterprises, Inc.*, 2007 WL 954129, *12 (E.D. Pa. March 27, 2007). Consideration will also be found where an employee enters into a new restrictive covenant at each promotion or at the assumption of each new position with new benefits. *See Charles Schwab and Co. v. Karpiak*, 2007 WL 136743, * 12 (E.D. Pa. Jan. 12, 2007).

(E) *Severance Pay.*

In *Coventry First, LLC v. Ingrassia*, 2005 WL 1625042, *7 (E.D. Pa. July 11, 2005), an employee's receipt of $25,000 in severance pay after termination was held to constitute new consideration that was sufficient to support a non-compete. The employee had also signed a non-competition covenant at the commencement of employment. The Court held as follows: "[B]oth before beginning work and after leaving the Company, Ingrassia agreed to abide by the restrictive covenant in exchange for an employment benefit of some type." In an ex-employee's suit for severance pay, the employee's entry into a noncompete in a severance agreement will constitute consideration for severance pay even if the noncompete is similar to an earlier noncompete. *Scherzer v. Quality Health Services, Inc.,* 1993 WL 311303 (E.D. Pa. August 11, 1993).

(F) *Uniform Written Obligations Act*

A series of federal court decisions in diversity cases have raised the question of whether Pennsylvania law requires consideration for a noncompete when the parties agree to be legally bound as required under the Uniform Written Obligations Act, 33 P.S. § 6 ("UWOA"). The UWOA provides, in its entirety: "A written release or promise, hereafter made or signed by the person releasing or promising, shall not be invalid or unenforceable for lack of consideration, if the writing also contains an additional express statement, in any form of language, that the signer intends to be legally bound." In *Latuszewski v. Valic Financial Advisors, Inc.* 2007 WL 4462739, *10 (W.D. Pa. Dec. 19, 2007), the Western District of Pennsylvania noted that neither the Pennsylvania courts nor the United States Court of Appeals for the Third Circuit had addressed the issue of the UWOA specifically for noncompetes. The issue in *Latuszewski* was the need for the employer to provide new consideration when obtaining a noncompete from a current employee. The most that could be said was that the courts had not ruled that the UWOA did not apply to noncompetes. In *Latuszewski*, the Western

District of Pennsylvania said that a statement of intent to be legally bound acts as a substitute for consideration, fulfilling the requirement under Pennsylvania law that noncompete covenants added after the start of employment be supported by consideration. The Court suggested that a statement that the parties intended to be legally bound under the UWOA would provide new consideration.

However, the Court also held that the employer had provided additional benefits that gave the employees adequate consideration. These additional benefits included a reduction in the number of protected companies with whom the employees could not compete; removal of the prohibition on solicitation of other employees; addition of the employee's ability to file suit under the agreement in a jurisdiction outside Houston, Texas; removal of the provision requiring payment of attorney's fees in the event of an adverse judgment involving enforcement of the agreement; and addition of the right to request an arbitration clause. In *Latuszewski, supra*, the Court held that benefits aside from the lessening of restrictions in an old covenant would be necessary to support a new restrictive covenant. However, the court could consider new benefits that were contingent or provided only the potential to realize financial gains. *See Latuszewski, supra.*

Other courts have held that, although consideration existed to support a restrictive covenant, the UWOA obviated the need for such consideration. *See Charles Schwab and Co. v. Karpiak*, 2007 WL 136743, * 12, n. 7 (E.D. Pa. Jan. 12, 2007) ("Even if the Agreements were not supported by consideration, they would still be enforceable [under the UWOA]", *citing and quoting from QVC, Inc. v. Tauman,* 1998 WL 156982, *4 (E.D. Pa. April 3, 1998) and *QVC, Inc. v. Starad, Inc.,* 2005 WL 742500, *4 (E.D. Pa. March 31, 2005)). The recent holdings that the UWOA may obviate the need for consideration are contrary to several Eastern District holdings in the early 1990s, to the effect that "boilerplate" UWOA language will not excuse the lack of consideration in a post-employment restrictive covenant. *Surgical Sales Corporation v. Paugh*, 1992 WL 70415 (E.D. Pa. March 31, 1992); *Young Bros., Inc. v. Hatch*, 1990 WL 18903 (E.D. Pa. February 27, 1990). The uncertainty of the law in this area suggests that it is still prudent to provide provide adequate consideration to support a noncompete for a current employee..

II. REASONABLENESS IN DURATION

Set forth below, in ascending order of length, are covenant durations that the courts have recently found to be reasonable:

A one-year restrictive covenant was held to be *prima facie* reasonable for a salesman in *See Innoviant Pharmacy, Inc. v. Morganstern*, 390 F. Supp.2d at 192 (N.D. N.Y. 2005) (refusing to enforce covenant on other grounds). *See also Fisher Bioservices, Inc. v. Bilcare, Inc.,* 2006 WL 1517382, *13 (E.D. Pa. May 31, 2006) (non-solicitation clause).

A one-year nationwide restriction on employment with, or ownership of, a competing industry or soliciting customers was upheld as reasonable in the health care records management

industry in *Nextgen Health Care Information Systems, Inc. v. Messier*, 2005 WL 3021095, * 4, * 13 (E.D. Pa. Nov. 10, 2005)

A one-year covenant without geographic limitations was held not to be unreasonable in the fire protection industry (*Victaulic Co. v. Tieman,* 499 F.3d 238 (3d Cir. 2007)) and was held to be reasonable in the specialty chemical industry (*Quaker Chemical Corp. v. Varga,* 509 F.Supp.2d 469 (E.D. Pa. Sept. 4, 2007)). A one-year nationwide restriction on employment with, or ownership of, a competing industry or soliciting customers was upheld as reasonable in the storage equipment industry in *Intermetro Industries Corp. v. Kent,* 2007 WL 1140637 (M.D.Pa. April 17, 2007).

An 18-month customer non-solicitation covenant was held to be reasonable in *Charles Schwab & Co. v. Karpiak,* 2007 WL 136743, *12 (E.D. Pa. Jan. 12, 2007).

A two-year post-employment non-competition covenant executed by a doctor in a practice treating high-risk pregnancies was upheld as to two of the five counties covered by the covenant (York and Adams Counties, Pennsylvania), but not as to the other three counties in which the medical practice served few patients (Lancaster, Dauphin, and Cumberland). *Wellspan Health v. Bayliss*, 869 A.2d 990, 1000 (Pa. Super. 2005).

A two-year, 25-mile restrictive covenant executed by an osteopathic doctor who performed services in the field of orthopedic medicine was upheld and enforced by liquidated damages of $100,000. *Lehigh Valley Bone, Muscle and Joint Group, LLC v. Puccio*, 75 Pa. D. & C.4th 176 (C.C.P. Lehigh County 2005), *affirmed w/o opinion*, 903 A.2d 61 (Pa. Super. 2006).

A three-year non-compete was upheld as reasonable and enforced by injunction in *Coventry First, LLC v. Ingrassia*, 2005 WL 1625042, *9 (E.D. Pa. July 11, 2005), but the United States/Canada/Puerto Rico geographic restriction was held to be unreasonable, and the geographic territory was limited to the five states served by the employee.

The courts have upheld much longer non-solicitation agreements in the financial services industry, e.g., a five year prohibition on soliciting and hiring employees in *Fishkin v. Susquehanna Partners, G.P.,* 2006 WL 1517397 (E.D. Pa. May 31, 2006).

Drafting Notes:

The starting point for the durational restriction should be the end of employment, not the end of the contract, since an employment contract may expire before the end of actual employment. The covenant should also explicitly survive termination of the contract and termination of 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 be tolled for the period from the employee's initial violation through the date on which a court enjoins the violations. This will protect against the shortening of the restrictive period or the expiration of the covenant before the Court hears an injunction. In *Hayes v. Altman,* 438 Pa. 451, 266 A.2d 269 (1970), the Pennsylvania Supreme Court refused to

enforce an otherwise valid noncompete because the noncompete period had expired, reversing a lower court decree for specific performance. Conversely, in *Excellent Laundry Co. v. Szekeres,* 382 Pa. 23, 114 A.2d 176 (1955), the Supreme Court dismissed as moot an employee's appeal from a lower court order enforcing a noncompete that had expired by the time of the appeal. *Compare Fishkin v. Susquehanna Partners, G.P.,* 2006 WL 1517397, *9, n. 7 (E.D. Pa. May 31, 2006) (holding that final injunction petition was moot after restrictive period had expired, but granting relief since the parties had agreed that the court should resolve issue and since injunction would affect ex-employer's ability to recover injunction bond).

III. REASONABLENESS IN GEOGRAPHIC SCOPE

(A) *Cases Upholding Broad Geographic Scope*

During the past few years, Pennsylvania law has moved toward permitting a broader- and possibly unlimited - scope for geographic restrictions where the former employer's business is worldwide or widespread. *See Victaulic Co. v. Tieman,* 499 F.3d 238 (3d Cir. 2007); *Quaker Chemical Corp. v. Varga,* 509 F.Supp.2d 469 (E.D. Pa. Sept. 4, 2007). The theory behind the enforcement of a restrictive covenant with unlimited restrictions is that the economy is increasingly global. *Victaulic Co. v. Tieman,* 499 F.3d at 238 (stating that the notion of a too-broad geographic scope has become antiquated in light of the increasingly global economy). Therefore, in *Quaker Chemical Corp. v. Varga,* the Eastern District upheld a restrictive covenant with no geographic boundaries where both old and new employers competed worldwide, and where the effect of the restriction on the employee was reasonable (the employee would work in the same state for the new employer where he had been employed by the old employer). In *Intermetro Industries Corp. v. Kent,* 2007 WL 1140637 (M.D. Pa. April 17, 2007), the court made it clear that the employer may enforce a geographic restriction in areas where the employer competes, not just where the employee competes, where the employee may possess information that may be harmful to the employer in all areas. In other words, where an employee's knowledge of confidential information extends beyond the employee's own territory, the employer may be able to enforce a restrictive covenant that extends beyond the geographic area that the employee had served. *See e.g. Intermetro Industries Corp v. Kent*, 2007 WL *supra* at *7. Factors that may allow an employer to enforce the covenant in a broader area include the employee's knowledge of sales information and strategies and pricing, product margin, and product development information for areas beyond the employee's territory. A covenant that extends beyond the employee's territory may also be permissible where the court finds that the ex-employee has a potential to cause harm outside the geographic region that he served. *See Pulse Technologies, Inc. v. Dodrill*, 2007 WL 789434 at * 10-11 (D. Ore. March 14, 2007). Applying Pennsylvania law, the court found that the ex-employee had excellent contacts in areas other than his territory, access to trade secrets for a variety of different locations, including national companies with facilities at several locations, making a nationwide covenant appropriate on four clients.

A non-solicitation covenant that has no geographic boundaries is by its nature limited to the employer's customers or prospects who are subject to solicitation. *Charles Schwab & Co. v. Karpiak,* 2007 WL 136743, *12 (E.D. Pa. Jan. 12, 2007).

(B) *Cases Limiting Geographic Scope*

A geographic restriction may not be broader than the former employer's business or market. Such a restriction will not be upheld as reasonable by a court applying Pennsylvania law. *See Wellspan Health v. Bayliss*, 869 A.2d 990, 1000 (Pa. Super. 2005) (refusing to enforce restrictive covenant in counties in which former employer/medical practice did not compete).

The area served by the employee may also limit the noncompete's geographic scope. A geographic restriction that encompassed the United States, Puerto Rico and Canada was held unreasonable in the "life settlement industry" (an industry that bought life insurance policies from individuals who had excess insurance), when the ex-employee's territory encompassed only five states – Colorado, Wyoming, Nebraska, Kansas, and Missouri. Therefore, the restrictive covenant was enforced only as to those five states, for the duration of the restrictive covenant of three years. *Coventry First, LLC v. Ingrassia*, 2005 WL 1625042, *9 (E.D. Pa. July 11, 2005).

A geographic restriction of a "30-mile radius" that is not specified, or an unspecified "customer" restriction" may be inherently unreasonable, but the courts can cure the shortcoming by "blue penciling" the covenant. *Innoviant Pharmacy, Inc. v. Morganstern*, 390 F. Supp.2d at 192 (N.D. N.Y. 2005) (refusing enforcement on other grounds).

Some geographic restrictions are too unreasonable to enforce at all. *See Fres-Co System USA, Inc. v. Bodell*, 2005 WL 3071755, *5 (E.D. Pa. Nov. 15, 2005) ; *Fres-Co System USA, Inc. v. Bodell*, 2005 WL 3071755, *5 (E.D. Pa. Nov. 15, 2005), refusing to enforce restrictive covenant *at all* when covenant extended beyond former employee's sales territory or industry. The non-competition agreement extended to the entire North American and Caribbean coffee markets for a sales representative of packaging materials and machinery for the coffee industry; the agreement was unreasonable because it extended beyond the ex-employee's former sales territory and product line. *Fres-Co System USA, Inc. v. Bodell*, 2005 WL 3071755, *5 (E.D. Pa. Nov. 15, 2005). In *Ride the Ducks, L.L.C. v. Duck Boat Tours, Inc.*, 2005 WL 670302 (E.D. Pa. March 21, 2005), the Court refused to enforce a two-year 100-mile restrictive covenant prohibiting the operation and marketing of amphibious "duck" tours and the design, manufacture or operation of amphibious vehicles that are used for any commercial purpose. The ex-employer required that all employees (whether skilled or unskilled) sign the restrictive covenant. The Court's refusal to enforce the restrictive covenant turned on the employer's lack of interest in protecting against activities by the ex-employee, the absence of any specialized skills or training, and the absence of any

confidential business information. NOTE: In contrast to a noncompetition contract, a court would modify a nonsolicitation contract even if the contract lacked any geographic or durational limits. *See Plate Fabrication & Machining, Inc. v. Beiler,* 2006 WL 14515 (E.D. Pa. Jan. 3, 2006).

IV. DRAFTING TRAPS

(A) *Assignability – Asset Sale*

In *Hess v. Gebhard & Co., Inc.*, 570 Pa. 148, 808 A.2d 912 (2002), the Pennsylvania Supreme Court held that, when an employer sells its assets, a restrictive covenant is not assignable to a purchasing business in the absence of a specific assignability provision in the covenant. The courts will disfavor assignments without an airtight assignment clause. *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). For complete assignability, the restrictive covenant should explicitly be assignable; should bind and benefit successors and assigns; and any subsequent purchase or sale agreement should explicitly assign the restrictive covenants. *See Villanova Health Corp. v. Hawrylak*, 1998 WL 961374 (E.D. Pa. 1998). In addition, the employer must follow the contractually required procedure for assignment, or risk losing the right to enforce restrictions against the assignee. *Savage, Sharkey, Reiser & Szulborski Eye Care Consultants v. Tanner*, 848 A.2d 150 (Pa. Super. 2004) (failure to notify employee of assignment precluded enforcement of non-compete).

(B) *Assignability - Stock Transfer*

The majority view is that in a stock sale, a specific assignment clause is not necessary. *Siemens Medical Solutions Health Services Corp. v. Carmelengo,* 167 F.Supp.2d 752 (E.D. Pa. 2001) (New owner's purchase of 100% of employer's stock did not constitute change in "employer" that would discharge employee from non-solicitation covenant); *Zambelli Fireworks Manufacturing Co., Inc. v. Wood,* 2009 WL 159182 (W.D. Pa. Jan. 21, 2009) (Upholding *Siemens* but considering, before rejecting, the ex-employee's argument that the new employer had significantly changed in character). In *Zambelli Fireworks,* the Western District distinguished *Joyner Sports Fitness Medicine, Inc. v. Stejbach,* 45 Pa. D. & C. 4th 242 (Dauphin Co. 1999), *affirmed without opinion,* 769 A.2d 1215 (Pa. Super. 2000), in which a Pennsylvania trial court had held that a purchaser of the employer's stock could not enforce a restrictive covenant. The convoluted facts in *Joyner* included the corporate purchaser's unilateral alteration of the employees' compensation and the fact that the nominal plaintiff was the former employer, which remained only as a corporate shell. The Court held that the old employer could enforce the restrictive covenant from the date on which the stock purchase took place.

(C) *Inadvertent Employer Cancellation of Contract*

An employer can inadvertently "terminate" a restrictive covenant for a current employee. In *Innoviant Pharmacy, Inc. v. Morganstern*, 390 F. Supp.2d 185, 193 (N.D. N.Y. 2005), the employee signed a valid one-year restrictive covenant. Two years later, the employer required the employee to sign and return an employee handbook disclaimer that disclaimed "employment agreements or other agreements of any kind". Faced with this comprehensive disclaimer, the Court held that the employer had effectively reformed and terminated the restrictive covenant, and that the covenant could not be enforced.

V. ENFORCEABILITY AFTER DISCHARGE

(A) *Discharge through no Fault of Employee*

In *Insulation Corp. of America v. Brobston*, 446 Pa. Super. 520, 667 A.2d 729 (1995), the Superior Court held that an ex-employer could not enforce a restrictive covenant against an ex-sales employee who was discharged for poor performance. The Superior Court held that since the ex-employer had deemed the ex-employee to be worthless, the ex-employer could not preclude work for a competitor. The Court held:

> Where an employee is terminated by his employer on the grounds that he has failed to promote the employer's legitimate business interests, it clearly suggests an implicit decision on the part of the employer that its business interests are best promoted without the employee in its service. . . . Once such a determination is made by the employer, the need to protect itself from the former employee is diminished by the fact that the employee's worth to the corporation is presumably insignificant. Under such circumstances, we conclude that it is unreasonable as a matter of law to permit the employer to retain unfettered control over that which it has effectively discarded as worthless to its legitimate business interests.

Insulation Corporation of America *v. Brobston*, 446 Pa. Super. 520, 667 A.2d 729, 735 (1995).

The same principle would seem to apply to other discharges that arise without the fault of the employee (e.g., economic layoff or downsizing) (*See, e.g., All-Pak, Inc. v. Johnston*, 694 A.2d 347 (Pa. Super. 1997)). In a footnote, the Superior Court in *All-Pak* expressed concern that employees might deliberately render inferior performance in order to avoid a noncompete. In *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), the courts allowed ex-employees to obtain an injunction against the ex-employer's attempts to enforce the non-compete. The ex-employer was an agency that had placed nurses at a hospital. When the hospital and the agency terminated their contract, the agency sued to prevent the nurses from continuing to work at the hospital. The agency had earlier tried to force the nurses to buy out their noncompetes by paying two years of compensation to the agency. NOTE: The *Insulation Corporation* 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.4th 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.

(B) *Discharge for Misconduct*

An employee cannot avoid a noncompete after being 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"; no consideration at the time of local non-discrimination laws). Federal courts applying Pennsylvania law have also held that an employer has a protectable interest in enforcing a non-competition agreement against an ex-employee who has been terminated for misconduct. *See, e.g. Pulse Technologies, Inc. v. Dodrill*, 2007 WL 789434 (D. Ore. March 14, 2007) (applying Pennsylvania law; employee had poor attendance records, failed and refused to comply with directives, and failed to comply with strategic plan).

(C) *Enforceability of Noncompete if Employee is in Poor Standing but not Fired*

An employee who is on the way out, but still employed, may not avoid a noncompete on *Insulation Corporation* grounds after resigning. In *Intermetro Industries, Inc. v. Kent,* 2007 WL 1140637, *7 (M.D. Pa. April 17, 2007), the court held that an employee could not defend against a noncompete on the ground that the employer had given the employee a poor review and intended to fire the employee.

(D) *Variations on the Theme*

Although the decisions in *Insulation Corporation* and *DeMuth* would seem to establish a bright line test, the decisional law (at least in federal courts) suggests otherwise. In *Coventry First, LLC v. Ingrassia*, 2005 WL 1625042, *9 (E.D. Pa. July 11, 2005), the Court partially enforced a restrictive covenant against an individual who was terminated involuntarily, without deciding whether the employee was terminated with or without fault. The Court held that the employee could work for other persons engaged in the industry, as long as he did not engage in the industry as a principal himself, and as long as he did not work within his former territory. The case turned in part on the employer's willingness to provide

severance pay as additional consideration for the noncompete in the severance agreement. Additionally, the federal courts have not always taken into account the reasons for an employee's termination in deciding whether or not to enforce a restrictive covenant. *See Perry v. H&R Block Eastern Enterprises, Inc.,* 2007, WL 954129 (E.D. Pa. March 27, 2007).

VI. THE EX-EMPLOYER'S INABILITY OR UNWILLINGNESS TO COMPETE - IS IT A DEFENSE?

(A) *Is There a "Failing Company" Defense in Non-Compete Law?*

In an action to enforce a non-compete, the ex-employer must be conscious of the fact that an ex-employee (or successor employer) may be able to show that the ex-employer's own business failings were the cause of its own harm. In *Clarke Transportation Services, Inc. v. Haskins*, 2006 WL 1620175, *2 (E.D. Pa. June 8, 2006), the Court held that the ex-employer's own "managerial transgressions" and operational problems including lost freight, significant shipment delays, failure to properly invoice customers, failure to properly apply funds to invoices and multiple computer and data processing errors had led to significant customer distress and dissatisfaction, and were the cause of the ex-employer's own irreparable harm. The Court therefore held that the ex-employer could not satisfy its burden to demonstrate that the ex-employee's breach of the restrictive covenants resulted in irreparable harm and therefore held that the employer was not entitled to injunctive relief. *Clarke Transportation Services, Inc. v. Haskins*, at *3. *See also Rapid Freight Systems v. Ofer Express LLC,* 2003 WL 1848211 (Phila. Co. Feb. 28, 2003)) (customer dissatisfaction); (*Bilec v. Auburn Associates, Inc.*, 403 Pa. Super. 176, 588 A.2d 538 (1991) (withdrawal from business); *Thomas Jefferson University v. Wapner*, 2004 WL 2474098 (Phila.Co. Oct. 22, 2004), *affirmed*, 903 A.2d 565 (Pa. Super. 2006)) (lack of desire to compete in a particular area); (*Ferarolis v. International Recovery Systems, Inc.*, 2006 WL 1371187 (E.D. Pa. May 18, 2006) (employer's lack of licensure in area where employer sought to restrict competition).

(B) *Use of the Ex-Employer's Deficiencies as a Defense to a Damage Claim*

In the right circumstances, an ex-employee or successor employer can mount a powerful defense against a damage claim in a noncompete case by showing that the ex-employer lost business by reasons of its own shortcomings, rather than through the ex-employee's misconduct. Such shortcomings may include the submission of unacceptable bids to customers or the failure to follow up on business opportunities. Under Pennsylvania law, a plaintiff suing for violation of a restrictive covenant has to establish damages with reasonable certainty, not absolute certainty (*Scobell, Inc. v. Schade,* 455 Pa. Super. 414, 688 A.2d 715, 718-19 (1997)). In order to establish a damage claim against a new employer for interfering with an employee's noncompete, the ex-employer must show (1) that the new employer obtained the business because the ex-employees went to work for the new employer and (2) that, but for the new employer's bid, the ex-

employer (rather than a third party) would have obtained or retained a contract. *Scobell, supra*, 455 Pa. Super. 414 at 423, 688 A.2d 715 at 719. Showing a list of customers that a new employer serves does not establish with "reasonable certainty" that the new employer was the proximate cause of a plaintiff's loss of business. *See Id; see also Telamerica Media, Inc. v. AMN Television*, 2002 WL 32373712 (E.D. Pa. Sept. 26, 2002). Where an ex-employer failed to pursue a business opportunity that the ex-employee had brought to the ex-employer's attention, the ex-employer was responsible for the loss of business, not the departing employee who was sued for breach of fiduciary duty. *See Patient Transfer Systems, Inc. v. Patient Handling Solutions, Inc*., 2001 WL 936641 (E.D. Pa. Aug. 16, 2001).

VII. FORFEITURES OF COMPENSATION OR EQUITY INTERESTS FOR BREACH OF RESTRICTIVE COVENANT

(A) *Introduction*

An alternative to injunctive relief or damages at trial exists for an employer enforcing a non-compete or other restrictive covenant. The employer may require the employee to forfeit an item of value, in the form of either post-employment compensation or a share in the ownership of a business. Courts in Pennsylvania and other jurisdictions have generally upheld these forfeitures, so long as the forfeiture is covered explicitly in a contract. However, the whole area of forfeitures has become the focus of increasing litigation in recent years. This litigation has led to conflicting decisions on the employer's need to show that the noncompete is reasonable in the forfeiture context (as opposed to an equity proceeding enforcing the noncompete), and on what (if any) circumstances allow the employee to avoid the forfeiture.

(B) *The "Employee Choice Doctrine" vs. the Reasonableness Standard*

The "employee choice doctrine" dispenses with any need to examine the reasonableness of a forfeiture-for-competition clause. Under this doctrine, the employee has the choice between either (1) refraining from competing and obtaining the benefit (e.g., deferred compensation or a payout of an equity share or stock rights); or (2) competing and forfeiting the benefit. Generally, under this doctrine, the non-competition/forfeiture agreement is evaluated on a pure contract basis. Federal courts applying Pennsylvania law have adopted the "employee choice doctrine" in the case of *Fraser v. Nationwide Insurance Co*., 334 F. Supp. 2d 755 (E.D. Pa. 2004). Despite this doctrine, there is a certain amount of confusion and inconsistency in the treatment of forfeitures, since courts typically discuss the reasonableness of the non-compete when imposing a forfeiture.

Pennsylvania state courts have recently evaluated forfeiture clauses for reasonableness. *See, e.g. Capozzi v. Latsha and Capozzi, P.C.,* 797 A.2d 314 (Pa. Super. 2002), *appeal denied*, 573 Pa. 620, 821 A.2d 586 (2003); *Bilec v. Auburn & Associates, Inc. Pension Trust*, 403 Pa. Super. 176, 588 A.2d 538 (1991).

These cases appear to be at odds with earlier Pennsylvania case law, including *Garner v. Girard Trust Bank*, 442 Pa. 166, 275 A.2d 359 (1971).

(C) *Compensation Forfeiture*

(1) Deferred compensation - *Fraser v. Nationwide Insurance Co*., 334 F. Supp. 2d 755 (E.D. Pa. 2004). In an insurance agent's action to recover deferred compensation, the court refused to award the agent deferred compensation ranging between $222,000 and $364,000. The agent had a non-compete providing that if the agent competed within one year within a 25-mile radius, he would lose his right to deferred compensation. The Eastern District of Pennsylvania (on remand from Third Circuit Court of Appeals, *see* 352 F.3d 107 (3d Cir. 2004)) held that the reasonableness of a non-compete was not at issue in a forfeiture case. The only principles that applied were general contract principles. The court held that the forfeiture did not interfere with the employee's ability to earn a living. Indeed, the forfeiture was more akin to an incentive program than a non-compete clause. In effect, the ex-employer offered a bonus to any employee who chose not to compete within 25 miles for one year. *Fraser, supra*, 334 F. Supp. 2d at 760. In effect, the employee had two options: (1) compete and forfeit deferred compensation; (2) choose not to compete and receive the deferred compensation. Alternatively, the court held that if it were necessary to examine the reasonableness of a non-compete in *Fraser*, the covenant was reasonably necessary for the protection of the employer and reasonable in duration and geographic scope. But *see Capozzi v. Latsha & Capozzi, P.C.,* 797 A.2d 314 (Pa. Super. 2002), which was not decided at the time of the court's first decision in *Fraser* (135 F. Supp. 2d 623 (E.D. Pa. 2001)).

(2) Profit sharing - *Garner v. Girard Trust Bank*, 442 Pa. 166, 275 A.2d 359 (1971). Garner, a leasing agent for the Binswanger real estate firm in Philadelphia, sued to obtain an unpaid vested interest of a profit-sharing pension trust. The trust document provided that any former member forfeited the unpaid vested interest if he entered into competition with the company within two years after separation from employment and prior to reaching age 65. The existence of competition was determined by the committee appointed to administer the trust. This committee had the sole discretion to decide the competition issue. Further, the contract included a delay of payout for two years after termination unless the trust administrators determined that there was no substantial risk of competition. At the close of the two-year period, the trustee (Girard) determined that the ex-employee had competed and refused to make payment to the ex-employee and, therefore, upheld the forfeiture. The employee sued to force payment and won at the trial court, but the Supreme Court of Pennsylvania reversed the trial court and held against the employee. The court found that the term "enter into competition"

was sufficiently specific to be enforceable and, therefore, that the decision to impose the forfeiture was reasonable. The court also upheld the discretion to either distribute funds before the two-year period expired or to hold funds for two years. The court distinguished cases in which it was possible to adopt a reasonable alternative construction under the terms of the plan without forcing a forfeiture. The court held that there was no way to avoid the forfeiture except by totally eliminating the non-compete portion of the Binswanger plan. The court held that the committee's decision to impose the forfeiture was subject to judicial review only to insure that the decisions were in "good faith and within the bounds of reasonable judgment." To the same effect, *See Ziring v. Heidman,* 54 Pa. D. & C. 2d 254 (Phila. Co. 1971).

(3) Commissions - *Bettinger v. Carl Berke Associates, Inc.,* 455 Pa. 100, 314 A.2d 296 (1974). The employee was subject to a one-year post-employment restriction. The restrictive covenant called for forfeiture of all commissions due to the employee. The court held that pursuit of the forfeiture remedy did not bar the employer from also seeking an injunction against the employee, where there was no provision in the agreement that the employer was limited to seeking damages, and the employer was seeking protection from the employee's competition, which would not be afforded by damages only. *Bettinger* is one of the landmark Pennsylvania cases upholding both the right to injunction and damages, and is still good law.

(4) Vacation pay - *Boyce v. Smith-Edwards-Dunlap Co.,* 398 Pa. Super. 345, 580 A.2d 1382 (1990). The employee brought suit against a former employer seeking to recover unpaid vacation pay. The court held that the employee was entitled to no vacation pay because the employee had violated a post-employment restrictive covenant, and the employer could use the violation of the restrictive covenant as a defense to a claim for vacation pay. The court held that the reasonableness of restrictive covenants was not an issue and therefore the lack of reasonableness was not a defense in an employer's action to recover for damages. In an action for damages, the analysis is a pure contract analysis – i.e., did the employee enter into the agreement?

(5) Antitrust issues - *Kaplan v. May Stern & Company*, 427 F. Supp. 978 (W.D. Pa. 1977). Plaintiff sought payments of deferred compensation and attacked the forfeiture of deferred compensation. The court held that forfeiture clauses were not prohibited by the antitrust laws. The court also considered the dispute to be moot, because the deferred compensation provision did not apply where (as was the case) the employee was earning more money in subsequent employment and the forfeiture did not apply where the employee had received written permission to compete.

(6) Invalidation of Pension Forfeiture - In *Bilec v. Auburn & Associates, Inc.* Pension Trust, 403 Pa. Super. 176, 588 A.2d 538 (1991), the Pennsylvania Superior Court refused to uphold a pension forfeiture for competition, where the non-compete did not limit the geographic reach of the restricted area. The forfeiture clause provided "[A] participant shall not be entitled to benefits . . . [if the participant enters] the services of a firm which competes with the employer." *Bilec, supra*, 403 Pa. Super. at 179, 588 A.2d at 539. Further, the forfeiture applied to existing employees, and the existing employees received no benefit that corresponded with this increased burden. The employer in *Bilec* was downsizing its business in a fashion that provided less work and fewer opportunities for the employees.

(E) *Equity Interest Forfeiture*

(1) Forfeiture invalidated - In *Capozzi v. Latsha and Capozzi, P.C.,* 797 A.2d 314 (Pa. Super. 2002), the Pennsylvania Superior Court invalidated an oral valuation agreement between shareholders of a law firm that limited the shareholder's payout if the shareholder competed. The agreement did not define the geographic area where competition was prohibited. The agreement provided that a shareholder who left the firm and then competed against the firm would only receive the amount of his initial capital contribution. A departing partner had made an initial capital contribution of $5,000. Over the years, the firm had grown to the point that gross revenues were $2.6 million.

The Superior Court held that the agreement in question was a restrictive covenant. The Court therefore applied the following factors to determine whether the covenant was enforceable: (1) whether the covenant was reasonably necessary to protect the legitimate interests of the employer; (2) whether the covenant was reasonably limited in geographic scope; and (3) whether the covenant was reasonably limited in terms of time. The Court found that the covenant failed all three tests. The Court found that the covenant imposing a forfeiture clause was not reasonably necessary to protect the interests of the employer, as follows:

> We cannot find that a forfeiture clause entitling a co-founding, named partner to only Five Thousand ($5,000) Dollars of a firm worth $2.6 million is reasonably necessary to protect the firm.

Capozzi v. Latsha and Capozzi, P.C., supra, 797 A.2d at 321.

The Court found that the agreement could not be enforced because the agreement was not limited in either its geographic scope or time.

(2) Forfeiture invalidated - In *Miller v. McNees, Wallace and Nurick*, 118 Dauphin Co. L.R. 1 (Dauphin County, Pa. 1997), a law firm partner was forced to retire from a large regional law firm headquartered in Harrisburg, Pa. The firm's partnership agreement provided, "Within five (5) years after the date of retirement, a retired partner may not . . . engage in services which are competitive with those of the partnership." The partner retired and joined another Harrisburg law firm. The partner's former firm withheld retirement benefits from the partner because the partner had gone to work for another firm. The partner sued to obtain his retirement benefits. The law firm moved for summary judgment dismissing the case. The partner opposed the motion, contending that the restrictive covenant was unreasonable. The court agreed with the partner and refused to dismiss the case, holding as follows:

> In the case *sub judice*, the restrictive covenant states no geographical limit. It bars Miller from practicing law for five years regardless of any geographical territory and in areas of the law which are "competitive with those of the partnership". McNees, as previously noted, is a large law firm with a diverse practice and a client base throughout Pennsylvania and the east coast. Because of its widespread client base and diverse practice, the majority of lawyers in Harrisburg and Pennsylvania are potentially in competition with McNees. Thus, any geographical limit in the McNees restrictive covenant would essentially bar a former McNees lawyer from practicing law. This is unreasonable.

Miller v. McNees, Wallace and Nurick, supra, 118 Dauphin Co. L.R. at 6.

The *Miller* agreement had no forfeiture clause and involved the involuntary holding of the partner's accumulated share and the failure to define "competition." The case points up the hazards of trying to go beyond the terms of a non-compete.

(3) Forfeiture upheld - *Bradford v. New York Times Company*, 501 F.2d 51 (2d Cir. 1974). The New York Times adopted an incentive

compensation plan in which key employees received company stock. The plan provided for a payout over a 10-year period after an employee's employment ended. The plan permitted the company to terminate payments if the employee violated an agreement not to compete with the company. The plaintiff was the key employee on the business side of the paper. He left the company and, several months later, took a position with another newspaper publisher in New York. The New York Times informed the ex-employee that he had relinquished all rights under the plan and stopped the stock payments permanently. Several years later, after leaving the competitor, the ex-employee requested resumption of payments. By that time, the stock had quadrupled in value. The Times refused to reinstate payments. The trial court dismissed the case and thereby upheld the New York Times' action depriving the ex-employee of all unpaid installments. The ex-employee tried to attack the company's action as an unreasonable restraint against competition, business, trade or commerce. The court held that the restriction was reasonable because the ex-employee was receiving benefits in the form of continuing payments. NOTE: The court rejected the "employee choice doctrine", in which there was no inquiry into reasonableness. Other courts in New York have applied the "employee choice doctrine", however. *See Morris v. Schroder Capital Management Corp.,* 481 F.3d 86 (2d. Cir. 2007)). Note that the result in *Bradford* might have been different if the employer had terminated the employee without cause (*Post v. Merrill Lynch, et al.,* 48 N.Y. 2d 84, 421 N.Y.S. 2d 847, 397 N.E. 2d 358 (1979)) or if the employee had been constructively discharged (*Morris v. Schroder Capital Management Corp., supra*) or where an employer had made inconsistent statements to an employee about whether a particular entity was a competitor that would trigger a forfeiture. (*Murphy v. Gutfreund,* 583 F. Supp. 957 (S.D.N.Y. 1984)).

(4) Forfeiture upheld - *Krauss v. M. P. Claster & Sons, Inc.,* 434 Pa. 403, 254 A.2d 1 (1969). Employee/stockholder left a business, and entered into an agreement for the sale back to the employer of his shares of stock. At that time, employee entered into a consulting agreement for five (5) years, which included a non-compete. The non-compete applied to the State of Pennsylvania except for the Greater Pittsburgh and Greater Philadelphia areas. The employee then began work with a competing building supply business. The employee maintained that he had not violated the non-compete because he worked for a company that was headquartered in Massachusetts (Grossman) and he did not work in Pennsylvania. The court rejected this argument: "It is not relevant under the contract that appellant might have acted for Grossman only in a capacity wholly divorced from Grossman's Pennsylvania business, as long as Grossman competed with appellee in a way forbidden by the contract." The ex-employer considered the employee to be in breach of the restrictive covenant and refused to pay further compensation. The

court upheld the ex-employer's argument, and held that the reasonableness of the restrictive covenant did not apply in a situation where the individual was filing an action for compensation.

(5) Forfeiture upheld - *Rhodes v. Superior Investigative Services, Inc.,* 437 F. Supp. 1012 (E.D. Pa. 1977). An ex-employee/stockholder sought to recover the balance allegedly due on a contract for the sale of his stock in a security guard business. The agreement for sale of the stock included a payout in two installments. The agreement included a two-year, 50-mile non-compete. Within two years, the employee engaged in the security business within 50 miles. The court held that the employee had breached the restrictive covenant.

(6) Forfeiture upheld - *Strohl Systems Group, Inc. v. Fallon*, 2006 WL 2828997 (E.D. Pa. Sept. 29, 2006). The court granted summary judgment for a plaintiff/corporation seeking to recover the stock of an employee who had breached a confidentiality agreement. The agreement required that anyone breaching the confidentiality provision had to sell stock back to the company at 50% of their appraised value. The court upheld the liquidated damages clause. The court cited *Omicron Systems v. Weiner*, 860 A.2d 554 and *Bradford v. New York Times Company, supra*.

(F) *Open Issue in Pennsylvania- Will Forfeiture be Upheld Where Employee is Discharged Through No Fault of the Employee's?*

Appellate courts in Pennsylvania have not yet applied the *Insulation Corporation* rule in the context of employee forfeiture. There are several indications that courts may be receptive to application of this rule. First, a court has refused to dismiss a claim to set aside a forfeiture in circumstances that resemble a constructive discharge. In *Fredericks v. Georgia Pacific Corp.*, 331 F. Supp. 422 (E.D. Pa. 1971), the court refused to dismiss an executive employee's claim to his share of a stock bonus plan. The plan provided for forfeiture upon voluntary termination of employment or discharge with or without cause. The employee resigned by mutual agreement after alleging that harassment by the employer made it impossible for him to perform his duties. The Court also refused to dismiss the executive's unjust enrichment claim. The court construed the bonus agreement in *Fredericks* against the drafter. *See Fredericks*, *supra,* 311 F. Supp. 422, 429. Second, the courts in New York State, which generally favor ex-employers more than Pennsylvania courts in non-compete disputes, acknowledged the availability of a constructive discharge claim in *Morris v. Schroder Capital Management Corp*., 481 F.3d 86 (2d. Cir. 2007), although the courts ultimately upheld the forfeiture clause. Third, in *Bilec v. Auburn & Associates, Inc. Pension Trust,* 403 Pa. Super. 176, 588 A.2d 538 (1991), the Pennsylvania Superior Court refused to uphold a pension forfeiture for competition, where the employer was downsizing its business in a fashion that provided less work and fewer opportunities for the employees.

In *Miller v. McNees, Wallace and Nurick*, 118 Dauphin Co. L.R. 1 (1997), the Court of Common Pleas of Dauphin County invalidated a restrictive covenant that forfeited a retiring lawyer's pension payments if the lawyer competed after mandatory retirement at the age of 70. The Court held that the forced retirement was tantamount to a termination, and relied on *Insulation Corp. of America v. Brobston*, in refusing to uphold the forfeiture.

VIII. "GARDEN LEAVE"

(A) *"Garden leave*" provisions require the ex-employer to pay the ex-employee for the period during which the ex-employee does not compete. "Garden leave" is often used in the financial services industry, and may include the requirement that the employee give a long notice of intent to leave for a competitor. During the notice period, the employee remains an employee of the old employer but typically loses access to business information and may not solicit clients or customers. *See Bear Stearns & Co., Inc. v. Sharon,* 550 F. Supp. 2d 174 (D. Mass. 2008) (refusing to enforce "garden leave").

(B) Pennsylvania courts do not appear to have addressed the "garden leave" issue to date. The courts have dealt with variations on "garden leave" include (1) a requirement that the employer pay the employee who is unable to work in suitable employment because of the noncompete (*See Minnesota Mining and Manufacturing Co. v. Gessner*, 78 F. Supp. 2d 390 (E.D. Pa. 1999)); and (2) a requirement that the ex-employer either pay the employee for a stipulated period after employment or allow the employee to compete. *See Visual Software Solutions v. Managed Healthcare Associates,* 2001 WL 1159741, *6 (E.D. Pa. Aug. 10, 2001).

IX. THE EMPLOYEE STRIKES BACK- PRE-EMPTIVE CLAIMS AGAINST NONCOMPETE ENFORCEMENT AND DEFENSES AND COUNTERCLAIMS

(A) *Declaratory judgment of non-enforceability* – The former employee or new employer may bring a pre-emptive action seeking a declaratory judgment of enforceability of a restrictive covenant. *See Hillard v. Medtronic, Inc.*, 910 F.Supp. 173 (M.D. Pa. 1995). Any declaratory judgment action against enforceability will naturally lead to a counterclaim by the ex-employer for breach of the covenant. *See Hillard v. Medtronic, Inc.*, *supra; Fishkin v. Susquehanna Partners, G.P.,* 563 F. Supp.2d 547 (E.D. Pa. 2008); *Latuszewski v. VALIC Financial Advisors,* 2007 WL 4462739 (W.D. Pa. Dec. 19, 2007); *Perry v. H&R Block Eastern Enterprises, Inc.,* 2007 WL 954129 (E.D. Pa. March 27, 2007); *Mannino v. Lazerpro Inc.,* 76 Pa. D. & C. 4th 526 (Centre Co. 2005); *Rapid Freight Systems, Inc. v. Ofer Express LLC,* 2003 WL 1848211 (Phila. Co. Feb. 28, 2003). NOTE: A review of reported decisions suggests that there is no clear advantage to filing for a declaratory judgment of non-enforceability. One clear victory for the ex employee came in *Chestnut v. Pediatric Homecare of America, Inc.,* 1991 WL 197319 (E.D. Pa. Sept. 26, 1991); in *Reporting Services*

Associates, Inc. v. Vertiext, LLC, 2003 WL 22183927 (Phila. Co. Sept. 10, 2003), the court shortened the noncompete significantly. ..

A declaratory judgment claim may also be asserted as a counterclaim in an action to enforce a restrictive covenant. *Surgical Sales Corp. v. Paugh,* 1993 WL 19723 (E.D. Pa. Jan. 26, 1993).

(B) *Affirmative Defenses Against Enforcement, Based on Employer Wrongdoing*

(1) Material breach/failure of consideration through nonpayment of employee. *See, e.g.*, *Philadelphia Ear, Nose and Throat Surgical Associates, P.C. v. Roth*, 44 Pa. D. & C.4th 427 (Phila. Co. 2000). The ex-employer will not be able to show likelihood of success on the merits, and therefore will not obtain a preliminary injunction, if the ex-employer has breached any of the conditions precedent to the restrictive covenant, particularly if the restrictive covenant mentions the breach as a factor that will defeat the restrictive covenant. *See Brentwood Industries, Inc. v. Entex Technologies, Inc.*, 2005 WL 757189, * 14 (E.D. Pa. March 31, 2005). *See also Ritz v. Music, Inc.,* 189 Pa. Super. 106, 150 A.2d 160 (1959)

(2) Estoppel through employer misconduct- *See, e.g., Durham Life Insurance Co. v. Evans,* 166 F.3d 139 (3d Cir. 1999) (sexual harassment of accused employee, resulting in constructive discharge of employee).

(3) 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.

(4) Laches or waiver through plaintiff's failure to pursue or develop business. *Bilec v. Auburn & Associates, Inc. Pension Trust,* 403 Pa. Super. 176, 588 A.2d 538 (1991).

(C) *Claim for 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). A claim or counterclaim for an injunction may succeed when the noncompete is governed by the law of another state that disfavors noncompetes (e.g., California, Virginia). *See, e.g., Lingo v. NVR, Inc.,* 2008 WL 510128 (E.D. Pa. Feb. 22, 2008). *But see Campbell Soup Co. v. Desatnick,* 58 F. Supp.2d 477 (D. N.J. 1999) (ex-employee failed in attempt to preliminarily enjoin enforcement of non-compete).

(D) *Contract/compensation claims – See Thomas Jefferson University v. Wapner,* 2004 WL 2470498 (Phila. Co. 2004), in which doctors brought a counterclaim for violations of the Wage Payment and Collection Law after the ex-employer sued for violation of a noncompete. One of the doctors won the WPCL claim, and the ex-employer was not successful on any of its claims.

(E) *Tort claims*

(1) Defamation

(i) 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).

(ii) 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)).

(2) Intentional interference with contractual relations

(i) An accurate statement of a restrictive covenant is privileged (*Gresh v. Potter McCune Co., supra*).

(ii) 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).

(3) Unfair competition

(4) 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.*

(5) 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.

X. THE COMPUTER FRAUD AND ABUSE ACT

The Computer Fraud and Abuse Act, 18 U.S.C. § 1030 ("CFAA"), is a federal criminal statute that penalizes unauthorized access to computers. The statute includes civil penalties and has seen increasing use in employee mobility cases. *See P.C. Yonkers, Inc. v. Celebrations the Party and Seasonal Superstore LLC*, 428 F.3rd 504, 510 (3rd Cir. 2005); *B & B Microscopes v. Armogida*, 532 F. Supp. 2d 744, 757 (W.D. Pa. 2007). The civil remedy is available to "[a]ny person who suffers damage or loss by reason of a violation of [Section 1030]". *See B & B Microscopes v. Armogida*, *supra.* The claimant may bring an action "to obtain compensatory damages and injunctive relief or other equitable relief." *See Id.* However, the damage provisions of the CFAA provide less relief to an ex-employer in employee mobility cases than many elements of state statute and common law. This leaves the CFAA's primary use as a way to obtain federal jurisdiction and incremental damages over and above those that may be recovered under state law.

18 U.S.C. § 1030 (a) (4) sets forth the essential elements of a violation of the CFAA:

(1) Defendant has access to a "protected computer";

(2) Defendant has done so without authorization or by exceeding authorization that was granted;

(3) Defendant has done so knowingly and with intent to defraud; and,

(4) As a result, defendant has furthered the intended fraud and obtained an item of value.

The CFAA provides for federal jurisdiction of claims for damage more than $5,000 in a one year period. *See HUB Group, Inc. v. Clancy*, 2006 WL 208684 (E.D. Pa. Jan. 25, 2006). However, the CFAA provisions that govern civil actions and remedies are confusing. Section 1030 (g) provides that a civil action under the CFAA is only available if the conduct involves one of the factors set forth in one of the five subsections of 18 U.S.C. § 1030 (a) (5) (B). A reading of § 1030 (a) (5) (B) depends upon a full reading of § 1030 (a) (5) (A) as well, however. Taken together, these sections provide that an action under the CFAA for damages must include a claim that the individual (1) knowingly caused the transmission of information that, as a result, intentionally caused damage without authorization to a protected computer (§ 1030 (a) (5) (A) (i)); intentionally accessed a protected computer without authorization, and, as a result, recklessly caused damage (§ 1030 (a) (5) (A) (ii)); or intentionally accessed a protected computer without authorization and thereby caused damages (§ 1030 (a) (5) (A) (ii)), and, *by this conduct,* caused a loss to 1 or more person during any one-year period aggregating at least $5,000 in value (§ 1030 (a) (5) (B) (i)); the modification or impairment of medical care (§ 1030 (a) (5) (B) (ii)); physical injury to any person (§ 1030 (a) (5) (B) (iii)); threat to public health or safety (§ 1030 (a) (5) (B) (iv)); or damage affecting a computer system (§ 1030 (a) (5) (B) (v)). A claim for injunctive relief is also available. *See also P.C. Yonkers, Inc. v. Celebrations the Party and Seasonal Superstore LLC*, 428 F.3rd 504 (3rd Cir. 2005).

Cases decided in Pennsylvania have been divided on the effect of the CFAA. In *B&B Microscopes v. Armogida*, 532 F. Supp. 2d 744 (W.D. Pa. 2007), the court awarded damages under the CFAA for an employee's deletion of files from an ex-employer's laptop. The court found liability for the unauthorized use of confidential information on the computer, and assessed damages of $11,400, including $10,000 for an interruption of service and $1400 for costs in performing a damage assessment. *B&B Microscopes, supra.* at 757-759.

In *Binary Semantics Limited v. Minitab, Inc.,* 2008 WL 763575 (M.D. Pa. 2008), the court held that a claim was stated under the CFAA, and therefore refused to dismiss this claim, where an individual employee accessed a protected computer and stole trade secrets. *Binary Symantec Limited v. Minitab, supra.* at * 5. *See also HUB Group, Inc. v. Clancy*, 2006 WL 208684 (E.D. Pa. Jan. 25, 2006), where the Court refused to grant a motion to dismiss on finding that a defendant exceeded the scope of authorized access; and *Hudson Global Resources Holdings v. Hill*, 2007 WL 1545678 (W.D. Pa. May 25, 2007), where the Court granted a preliminary injunction under the CFAA on finding that access was unauthorized. *But compare Quaker Chemical Corp. v. Varga,* 509 F. Supp. 2d 469, 483-484 (E.D. Pa. 2007), deferring until the damages phase any decision under the CFAA while granting a preliminary injunction for violation of a noncompete.

A notable case denying relief under the CFAA is *Brett Senior and Associates, P.C. v. Fitzgerald*, 2007 WL 2043377 (E.D. Pa. July 13, 2007). In *Brett Senior and Associates,* the Court held that a law firm employee accused of multiple employee mobility violations did not violate the CFAA because he did not have unauthorized access to the computer and did not exceed authorized access (defined in § 1030 (e) (6) as accessing a computer with authorization and using such access to obtain or alter information in the computer that the accesser is not entitled to obtain or alter). *See Brett Senior and Associates, P.C. v. Fitzgerald*, *supra,* 2007 WL 2043377 at *3. The employee had copied client files to an external hard drive and CD, created a list of clients that he serviced at the firm, and transformed the files to PDF or ZIP formats for purposes of transferring the files to a new employer, and emailed the new firm with information The Court found that because there was no allegation that the employee lacked authority to view information on the computer system, there was no CFAA violation, and granted summary judgment dismissing the CFAA claim. Additional limitations have been found under the CFAA in holdings such as that in *GWR Medical v. Baez*, 2008 WL 698995 (E.D. Pa. March 13, 2008), holding that a CD-ROM is not a computer under the Act's definitions.