Employment Law Advisor: Restrictive Covenant Law

Recent Cases Clarify Issues In Restrictive Covenant Law

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Three recent Massachusetts cases, two in the federal district court and one in superior court, have clarified some unresolved issues in Massachusetts law regarding restrictive covenants. The first, in the federal district court, addresses questions concerning employee non-solicitation agreements and the doctrine of inevitable disclosure. The other two recent decisions further refine the so-called "material change" doctrine in non-competition law, which has been recognized in Massachusetts since 1968.

Corporate Technologies: Non-Solicitation, Inevitable Disclosure and Indemnification

In *Corporate Technologies, Inc. v. Brian Harnett, et al*, Civil Action No. 12-12385-DPW (D. Mass. May 3, 2013), Judge Woodlock of the United States Court for the District of Massachusetts addressed several questions concerning employee non-solicitation agreements. In *Corporate Technologies*, Harnett had been a successful IT salesman for Corporate Technologies since 2003. When he joined the company, Harnett signed a Non-Disclosure and Non-Solicitation Agreement, which precluded him from divulging confidential information he learned while employed by Corporate Technologies, and also precluded him from soliciting business from Corporate Technologies' customers for a one-year period following his departure from Corporate Technologies. The Agreement signed by Harnett did not contain a standard non-competition agreement, and only prohibited non-solicitation by Harnett.

In 2012, Harnett received a job offer from a direct competitor of Corporate Technologies, OnX. As part of the job offer, OnX agreed to indemnify Harnett fully for any disputes with Corporate Technologies over breach of the Non-Disclosure and Non-Solicitation Agreement. Harnett accepted the job offer and resigned from employment with Corporate Technologies. On his last day in the office, Harnett met with Corporate Technologies' human resources manager, and confirmed that he understood his obligations under the Non-Disclosure and Non-Solicitation Agreement and that he would comply with those obligations. Upon his departure from Corporate Technologies, Harnett took with him about 25 pages of notes regarding his employment from the period 2010-2012, which he kept on a personal iPad. He also copied his 2012 consumer price quotes onto a USB memory drive.

On Harnett's first day of employment with OnX, OnX sent an announcement to approximately 100 potential clients notifying them of Harnett's position with OnX. Included in this group of potential clients were Harnett's eight largest clients in 2012 at Corporate Technologies. Four of Harnett's former clients responded to the announcement, and Harnett met with each of them.

Corporate Technologies filed suit against Harnett and OnX, and sought an injunction against both Harnett and OnX. The suit against Harnett was based on Harnett's alleged breach of the Non-Disclosure and Non-Solicitation Agreement. The suit against OnX was based on OnX's alleged interference with Harnett's duties under the Non-Disclosure and Non-Solicitation Agreement. Ultimately, Judge Woodlock ordered a preliminary injunction against Harnett, but declined to do so against OnX.

In defending against the motion for a preliminary injunction against Harnett, Harnett and OnX argued that Harnett had not engaged in "solicitation," because the potential clients had merely responded to the initial OnX announcement, and that Harnett had simply "followed up" with the potential clients thereafter. Judge Woodlock disagreed. While Judge Woodlock acknowledged that the clients were not bound to the Non-Disclosure and Non-Solicitation Agreement and were free to seek IT services from OnX, he found that the "first contact" argument made by Harnett drew "an artificial distinction in order to argue that Harnett's admitted and open business dealings with his former CTI clients do not constitute solicitation and do not implicate the confidential information he learned while working at CTI." Judge Woodlock went on to conclude that "[n]either the Agreement nor the law, however, draws such a distinction."

In substance, Judge Woodlock held that, where there exists a valid and binding non-solicitation agreement, the efforts that a salesperson would customarily employ in order to attract clients to a new employer constitute solicitation. As Judge Woodlock stated "[n]either the plain meaning of the word solicit, nor the plain meaning of the word entice requires some kind of first contact." And in reviewing relevant Massachusetts cases on the subject, Judge Woodlock found that "[c]ontrary to Defendants' contention, Massachusetts courts do not draw a bright-line distinction between those actions following first contact by the client and those following first contact by the employee." The ruling in *Corporate Technologies*, while not an appellate ruling, certainly signals that employers will have an increased chance of enforcing non-solicitation agreements where there is any type of meaningful and ongoing contact between a former employee and his/her former clients.

The ruling in *Corporate Technologies* is notable for its apparent broadening of Massachusetts law under non-solicitation agreements and under the "inevitable disclosure" doctrine.

In addition, Judge Woodlock found that Harnett had clearly violated the non-disclosure obligations of the Non-Disclosure and Non-Solicitation Agreement. First, he concluded that the information Harnett took when Harnett left Corporate Technologies was "confidential" as defined by Massachusetts law under the Non-Disclosure and Non-Solicitation Agreement. Next, Judge Woodlock addressed another area of law that has been somewhat unclear in Massachusetts – the "inevitable disclosure" doctrine. In response to Harnett's and OnX's claims that Harnett had no intention of using Corporate Technologies' confidential information, Judge Woodlock disagreed. Drawing on two other recent Massachusetts federal district court cases, Judge Woodlock wrote that in view of "the similarity of Harnett's position at both companies, he cannot simply forget the confidential information he learned about his clients while employed by CTI, and he will inevitably call on this information in any dealings with his former clients during the course of his employment with OnX." Thus, the *Corporate Technologies* ruling may provide more ammunition for employers in the "inevitable disclosure" area, especially in disputes with former sales or IT personnel.

Finally, while Judge Woodlock declined to order injunctive relief against OnX for other substantive reasons, he did find that Corporate Technologies demonstrated a likelihood of success on its claim for tortious interference with contractual relations against OnX. In so finding, Judge Woodlock noted that OnX had made an initial employment offer to Harnett, which Harnett had declined to accept. In response, OnX made another offer to Harnett. Unlike the first employment offer, the second (which Harnett did accept) included OnX's agreement to indemnify Harnett for any liability on the basis of the Non-Disclosure and Non-Solicitation Agreement. "The specific offer to indemnify Harnett after he rejected OnX's first employment offer demonstrates the likelihood of improper motive …" on the part of OnX.

The ruling in *Corporate Technologies* is notable for its apparent broadening of Massachusetts law under non-solicitation agreements and under the "inevitable disclosure" doctrine. It also serves as a not-so-subtle warning for employers who may contemplate agreeing to indemnify new employees for their violations of restrictive covenants with predecessor employees.

A.R.S., Rent-A-PC, Inc. and the "Material Change" Doctrine

Two recent decisions, one in the United States District Court for the District of Massachusetts and one the Massachusetts Superior Court demonstrate the continued evolution of the "material change" doctrine in Massachusetts. The "material change" doctrine, first recognized in *F.A. Bartlett Tree Expert Co. v. Barrington*, 233 N.E.2d 756 (Mass. 1968), provides that a non-competition agreement entered into at the inception of an employment relationship may be invalid years later where there have been material changes to the employee's terms and conditions of employment. In the past, we have discussed the "material change" doctrine in prior publications. See this article on Material Job Changes.

The two recent decisions are *Rent-A-PC, Inc. d/b/a Smartsource Computer & Audio Visual Rentals v. Robert March, et al*, Civil Action 13-10978-GAO (D. Mass. May 28, 2013) and *A.R.S. Services, Inc. v. Daniel Morse, et al*, Civil Action No. 2013-00910 (Middlesex Super. April 5, 2013). The facts in each case are quite similar. In each, defendant former employees had signed what appear to be valid one-year non-competition agreements that were governed by Massachusetts law. Each of the defendant former employees remained employed from the early 2000's, and each had undergone material changes in his terms and conditions of employment. These changes included promotions, relocations, compensation changes and movement between different departments. In the *A.R.S.* case, the non-competition agreement signed by Morse contained the following provision: "[t]he terms and conditions of this Agreement and its enforceability shall continue to apply and be valid notwithstanding any change in [Morse's] duties, responsibilities, position or title with [A.R.S.]" (the "Material Change Clause"). In the *Rent-A-PC* non-competition agreement, no such Material Change Clause existed.

The *A.R.S.* case is significant because it is the first reported decision in Massachusetts which squarely addresses the validity of a Material Change Clause and finds that such a clause is valid and enforceable.

In the *Rent-A-PC* case, Judge O'Toole of the federal district court denied the plaintiff's motion for a preliminary injunction in fairly short order. The defendants, predictably, argued that their non-competition agreements were invalid based on the *Bartlett* case and the material changes in their terms and conditions of employment. Judge O'Toole agreed. He wrote that "*F.A. Bartlett* is a significant problem for the plaintiff." Citing the case of *Lycos, Inc. v. Jackson*, 2004 WL 2341355, at 3* (Mass. Super. August 25, 2004), he quoted that "[e]ach time an employee's employment relationship with the employer changes materially such that they have entered into a new employment relationship a new restrictive covenant must be signed." The *Rent-A-PC* case is largely consistent with the Massachusetts cases interpreting *Bartlett*.

In the *A.R.S.* case, Judge Leibensperger of the Massachusetts Superior Court reached a different result, and did so in clear reliance on the Material Change Clause. In doing so, he expressly declined to follow a case successfully litigated by Morse, Barnes-Brown & Pendleton, *Akibia, Inc v. Hood, et al*, and relied on by the defendants in A.R.S. In *Akibia*, defendants successfully argued that a "material change" had occurred such that non-compete agreements were invalid, despite the existence of Material Change Clause. Reviewing the *Akibia* case, Judge Leibensperger noted that, in denying *Akibia's* appeal of the Superior Court's denial of its motion for injunctive relief, a Single Justice of the Massachusetts Appeals Court had observed that there had been no appellate case which had reviewed the validity of a Material Change Clause. In construing the Material Change Clause, Judge Leibensperger observed that "the parties understood the Agreement was intended to be enforceable notwithstanding a potential change in employment responsibilities." On the same topic, he went on to state that "[n]o persuasive reason is advanced by Morse for ignoring the terms of the Agreement." And, unlike Judge Woodlock in the *Corporate Technologies* case, Judge Leibensperger went on to conclude that the preliminary injunction should extend to Morse's new employer as well, and prohibited the new employer

from encouraging or permitting Morse to breach his non-competition agreement with A.R.S.

The *A.R.S.* case is significant because it is the first reported decision in Massachusetts which squarely addresses the validity of a Material Change Clause and finds that such a clause is valid and enforceable. This is extremely helpful to employers and to employment counsel. Since *Bartlett*, the "material change" has proved a difficult hurdle to overcome when considering the validity of an otherwise valid non-competition agreement. At this point, all prudent employers should consider reviewing their existing non-competition agreements. If an existing non-competition agreement does not contain a valid Material Change Clause, employers should 1) revise current non-competition agreements to contain such a clause, and 2) develop an appropriate, and enforceable, mechanism in order to have the revised non-competition agreement executed by existing employees (as well as new employees).

For questions about this topic, please contact any member of our Employment Law Group.