Employment Law Advisor

Material Job Changes May Void Employee's Non-Compete

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Many employers assume that non-competition agreements signed by employees at the time of hire remain enforceable even if changes occur to the employees' job. However, recent Massachusetts trial court decisions confirm that is not always so. The "material change doctrine" can be invoked by former employees to void non-competition agreements signed at the inception of employment, which may leave an employer's customer relationships, *i.e.*, "goodwill," and confidential proprietary information exposed to misuse and misappropriation. Because former employees are raising this defense more often — and with more success — employers must consider the potential impact of job changes on the enforceability of non-compete agreements.

Non-Competes: The Basics

A covenant not to compete is a type of restrictive agreement in which an employee agrees not engage in a business competitive with his or her employer for a certain period after termination of employment. Generally, to be enforceable a non-compete must (1) be necessary to protect an employer's legitimate business interests, (2) be reasonable in time and scope, and (3) be consistent with the public interest. Massachusetts courts recognize customer goodwill and confidential information as protectable business interests. We have discussed non-competes extensively in previous advisories such as:

ELA – March 2006: Enforcing Noncompetition Agreements Part I;

ELA – April 2006: Enforcing Noncompetition Agreements Part II; and

ELA – September 2004: Are your Non-Competes Enforceable?

The Material Change Doctrine Policy Include?

The material change doctrine is not new. In 2004, a trial court judge summarized the doctrine this way: "Each 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." That case, *Lycos, Inc. v. Jackson*, concerned an employee, Chun, who signed a restrictive covenant at the outset of her employment. Subsequently, Lycos promoted her, later demoted her, and then promoted her again. At the time of her second promotion, Lycos gave Chun a new offer letter to sign and return. The offer letter referenced the restrictive covenant she had signed at the start of her employment. Chun failed to sign and return the letter, and quit a few months later. In the lawsuit that followed concerning Chun's post-employment activities, the court refused to enforce the agreement Chun had signed at the outset of her employment because the changes in Chun's position were material changes in the employment relationship.

Recent Decisions Create Uncertainty

In 2012, three trial court judges have ruled that pre-existing non-compete agreements were voided by subsequent material job changes. Two of those decisions, *Grace Hunt IT Solutions, LLC v. SIS Software, LLC*, and *Protégé Software Services, Inc. v. Colameta*, involved materially adverse changes to the employees' compensation structure. In addition, in *Grace Hunt*, the employees had been asked to sign new non-competes at the time of the changes but refused, which the court found to be extremely significant because it signaled that the old employment relationship had been abandoned. In these decisions, the courts focused on whether there had been a material job change — and not whether the change was positive or adverse for the employee.

This month, Morse Attorneys Chris Perry and Maura Malone successfully opposed a motion for preliminary injunction to enforce non-competes against three sales executive clients based on the material change doctrine. In *Akibia, Inc. v. Jeffrey Hood, Ryan Gavigan and Charles Krueger* (Mass. Super. Ct. 10/9/2012), Judge Jeffrey A. Locke ruled that the non-competes the three employees had signed at Akibia were likely voided by material job changes that included promotions, demotions, increases and decreases in compensation, changes in responsibilities and sales territories, and changes in the employer's sales strategies and product offerings. As such, Judge Locke denied Akibia's motion to prevent Hood, Gavigan and Krueger from working for their current employer, IOvations. Notably, Judge Locke did not address language in the three employees' non-competes which stated that their obligations under the non-compete would continue regardless of any job changes, plainly indicating that such language did not influence his analysis.

By contrast, in another recent case, *Sentient Jet, LLC v. Mackenzie*, the judge limited the application of the material change doctrine to situations where the change negatively affected the employee, suggesting that pre-existing non-competes may not be voided by pay raises or promotions. Importantly, the judge in *Sentient Jet* noted that the employees in question had not been asked to sign new agreements, which would have indicated a belief that the change was material.

What Should Employers Do?

These decisions and the material change doctrine put employers in a difficult situation. As a practical matter, it can be difficult administratively to require a new non-compete each time an employee's position changes. Yet, if new agreements are not signed following a change that is later deemed to be "material," then an employer's pre-existing non-compete may be rendered unenforceable. The safest course is for employers to require their key employees to sign new non-competes in connection with substantial job changes.

Another approach taken by employers has been to require the employee to sign a document acknowledging the job change, and that any pre-existing non-compete agreement remains in effect. Of course, if the employee refuses to sign the acknowledgment then the employer's position may be weakened because such a request acknowledges that the job change was considered material at the time. Also, because the employee may refuse to sign such an acknowledgment (or a new non-compete), an employer should not ask for it unless the employer is willing to forego the job change, terminate the employee, or risk losing the protection of the original non-compete.

As in *Akibia*, employers have also tried to avoid the material change doctrine by including in all non-compete agreements language that anticipates job changes and states that the non-compete restrictions remain applicable. Such language, employers argue, is intended to put the employee on notice that the agreement will remain in effect for the entire period of the employee's employment with the employer — regardless of any changes in the terms and conditions of employment, including changes in duties, position, and compensation. However, as indicated by Judge Locke's decision in *Akibia*, trial judges may simply ignore such "boilerplate" where the job changes are substantial. Massachusetts appellate courts have not decided whether such language is effective in enabling an employer to enforce a pre-existing non-

compete after an employee's position has materially changed.

Because the law in this area is less than clear and former employees are increasingly more likely to try to invoke the material change doctrine to attack the enforceability of non-competes, employers should evaluate substantial changes to the roles and compensation of key employees very carefully. Employers should determine how they will approach job changes as part of their broader non-compete enforcement plan.

For more information on this topic, please contact a member of our Employment Law Group.