SCRIBBLES SQUIBS #41 (January 15, 2016)*

THE FUNDAMENTALS OF NON-COMPETE CLAUSES IN MASSACHUSETTS EMPLOYMENT CONTRACTS (PART ONE)

By Attorney Jonathan Sauer

I. INTRODUCTION.

In Article 15 of 'Construction law articles' contained on our website is 'Employment Agreements for Key Employees'. This certainly has application to employment agreements between contractors and their employees. It also has application to construction industry service providers, such as insurance producers/agents/brokers as to their employment relationships with their employer agencies, which relationship and issues I have been involved with several times.

We included in that article a model employment contract (Agreement), which I drafted, an updated version of which follows this *Squib*. Agreement contains the following non-compete clause:

"1. John Doe (t**he Employee) shall not** directly or indirectly as owner, partner, shareholder, supervisor or sales manager or in any other capacity **engage in a business similar to the operations carried on by Any General Contractor, Inc. (the Company or Employer) for a period of two years subsequent to Employee's termination** (however that occurs) and **within a distance of one hundred miles** from the principal place of business of Employer, which is located in Any Town, Massachusetts. This Agreement includes Employee's promise, herein made, that he or she will not communicate to any future employer or business partner the information listed in paragraphs A through C above for at least the minimum period of two years from termination, however caused, and longer, if so allowed by law. **Employee further agrees that the information identified in paragraphs A through C above is sensitive and of extreme importance to Employer and that any disclosure of that information could leave Employer with no adequate remedy of law, thus entitling Employer, if necessary and in the sole exercise of Company's judgment, to protect these rights by seeking injunctive relief** in a court of competent jurisdiction, which Employee agrees is the district court or superior court having jurisdiction/venue over Any Town, Massachusetts or over the town in which Employee lives, the choice being Employer's sole election. Employee agrees that **Employer shall be entitled to an award of the reasonable attorneys' fees and costs it incurs in protecting its rights under this Agreement if Employer is successful in obtaining any form of judicial relief** but not otherwise. **Employee further agrees to return to Employer within one day of his/her termination, however caused, any Employer property he/she has in his/her possession or control without keeping any copies of the same and that a failure to do so will**

constitute a material breach of this Agreement. Both parties hereto acknowledge that nothing in this Agreement shall prohibit Employee's working as a mechanic or tradesman (i.e. 'working with the tools') subsequent to termination with Employer, however caused, which labor is not subject to the two year limitation and the one hundred mile limitation listed above." (Emphasis added)

In a later *Squib*, we will discuss some of the key issues in the above clause, which will make more sense once we have a basic understanding of Massachusetts law concerning non-compete clauses in Massachusetts.

The purpose of this *Squib*, then, is to discuss some of the basic law associated with such clauses and agreements in Massachusetts with reference to both state and federal law.

II. SOURCES OF LAW APPLICABLE TO THIS ISSUE: STATUTES.

One beginning to evaluate this issue might expect that the principles applicable to this issue are only recent in nature, coming principally from recent case law (judicial decisions). In fact, some of this law is statutory, one of which principles was announced in 1865!

For example:

A. Federal Statutes:

(1) Involuntary Servitude – 13th amendment to the United States Constitution:

"Section 1. Neither slavery nor involuntary servitude, except as a punishment for crime whereof the party shall have been duly convicted, shall exist within the United States, or any place subject to their jurisdiction.

Section 2. Congress shall have power to enforce this article by appropriate legislation."

The Thirteenth Amendment to the United States Constitution, enacted in 1865, is associated with the end of slavery in the United States. One might wonder what possibly could be the application of *that* to non-compete agreements in Massachusetts in 2016. The application is that one of the issues associated with particularly restrictive non-compete clauses is that a party resisting enforcement of the same might/can/does claim that excessive restrictions as to future employment are a form of involuntary servitude. This is an argument that courts often listen to.

(2) 15 U.S.C.A. § 1**.** Trusts, etc., in restraint of trade illegal; penalty

"Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal. Every person who shall make any contract or engage in any combination or conspiracy hereby declared to be illegal shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by

fine not exceeding $100,000,000 if a corporation, or, if any other person, $1,000,000, or by imprisonment not exceeding 10 years, or by both said punishments, in the discretion of the court."

Looking quickly at the case law, although this statutory section is discussed in various employment non-compete cases, its judicial application to specific, individual employment contracts seems infrequent. Still, it is something to keep in mind.

B.. Massachusetts Statutes:

Here are three Massachusetts statutes that have potential application to this issue:

(1) M.G.L.A. 149 § 19. Prevention of employment

"No person shall, by intimidation or force, prevent or seek to prevent a person from entering into or continuing in the employment of any person."

This is an employee-friendly statute. Certain statutes are entitled to special preference when they reflect 'public policy'. With Massachusetts being the extremely liberal state that it is, an argument that this statute represents public policy seems likely to be favorably considered by a court, if not accepted in every case.

(2) M.G.L.A. 93 § 42. Taking of trade secrets

"Whoever embezzles, steals or unlawfully takes, carries away, conceals, or copies, or by fraud or by deception obtains, from any person or corporation, with intent to convert to his own use, any trade secret, regardless of value, shall be liable in tort to such person or corporation for all damages resulting therefrom. Whether or not the case is tried by a jury, the court, in its discretion, may increase the damages up to double the amount found. The term "trade secret" as used in this section shall have the same meaning as is set forth in section thirty of chapter two hundred and sixty-six."

The importance of this last statute is that this can give an employer a potential cause of action (theory or basis to sue) against an employee leaving employment who attempts to use that employer's trade secrets even if the employee never signed an employment contract with a non-compete clause.

(3) M.G.L.A. 266 §30. Larceny; general provisions and penalties

". . . (4) Whoever steals, or with intent to defraud obtains by a false pretense, or whoever unlawfully, and with intent to steal or embezzle, converts, secretes, unlawfully takes, carries away, conceals or copies with intent to convert any trade secret of another, regardless of value, whether such trade secret is or is not in his possession at the time of such conversion or secreting, shall be guilty of larceny, and shall be punished by imprisonment in the state prison for not more than five years, or by a fine of not more than twenty-five thousand dollars and imprisonment in jail for not more than two years. The term "trade secret" as used in this paragraph means and includes anything tangible or intangible or electronically kept or stored, which constitutes, represents, evidences or records a secret scientific, technical, merchandising, production or management information, design, process, procedure, formula, invention or improvement."

So, an employee taking an employer's 'trade secrets' might not only be potentially liable in a civil court for damages. Such action might be considered, in addition, a *crime* with criminal penalties involved. One should keep in mind that the bringing of a criminal action against an individual is not something that a citizen can do on his/her/its own. Such action would be brought by a district attorney or by the Attorney General.

My experience has been that the threat of an action often exceeds the value of actually taking that action. The application of that to non-compete clauses is that an employer might bring this statutory section to the errant employee's attention, something that might possibly take the wind out of their sails. So to speak.

III. SOURCES OF LAW APPLICABLE TO THIS ISSUE: MASSACHUSETTS COURT CASES.

A great deal of the law on non-compete clauses arises out of specific legal cases testing specific non-compete clauses. The following legal authorities are a montage of various judicial decisions taken from specific Massachusetts cases. These are listed here primarily for the purposes of identifying an applicable issue rather than in an attempt to provide the latest word on current Massachusetts law. This would be impossible because each such judicial examination will involve factual situations and agreements unique to that particular case. Different judges can interpret the same factual situations differently. Also, there is a great deal of 'discretion' on the part of individual judges in evaluating what is placed before them, which is not easily overturned on appeal.

To make this easier for a non-lawyer to read, citations to specific cases in all of their technical glory are not included. Simply, this is what a variety of courts have had to say concerning this issue:

It is settled in this Commonwealth that a covenant restraining trade or competition, inserted in a contract for personal service, is not in itself invalid if the interest to be protected is

consonant with public policy and if the restraint is limited reasonably in time and space. (**ED:** 'Time' references how long the non-compete agreement will remain in effect post employment. And, 'place' references how far away from the former employer's place of business will such an agreement be enforced.)

As to 'time', one court said that non-competition agreements signed by two former employees were reasonably limited in time, as required for agreements to be enforceable under Massachusetts law, where the agreements only imposed a six month restriction. Another court said that a restrictive covenant prohibiting a former employee from selling cabinets and millwork to clients of the former employer within one year from the date of termination was reasonable, both in general and as applied to the facts.

On the other hand, one Massachusetts court said that a non-competition agreement between an employer and a former employee that prohibited the employee from selling products in competition with the employer for two years after termination was an unreasonable restraint on competition in scope, duration, and geographic limitation, under Massachusetts law. Another Massachusetts case held that a restrictive covenant executed by the employee of a manufacturer of magnetic fluid rotary seal for use in the manufacture of semiconductor chips was reasonable except insofar as it was for a five-year term.

Generally, but with exceptions, the shorter the time period of the restriction, the more likely it is that it will be enforced by a court, everything else being equal. Six months: ok. Two years or five years: maybe not ok.

But, as I said earlier, each case is unique to the particular circumstances of the employment and to the various provisions of the employment. That helps explain how a court held that a restrictive covenant which was contained in a real estate salesman's employment contract which barred a salesman from engaging in real estate business for a period of three years and in specified cities where the employer had engaged in real estate business was reasonable and would be enforced by injunction.

How about as to 'place'? One court said that an employee's covenant not to compete with the employer within 100 miles of Boston for a period of five years was not unenforceable on the theory that it imposed "undue hardship" by barring employee from earning his living in the business he did best, in absence of any change in circumstances which might cause the employee unanticipated hardship. Another court held that a covenant not to compete executed by Chapter 7 (**ED:** this a reference to bankruptcy) debtors-franchisees prohibiting debtors from owning or operating a maintenance and cleaning service within a 50-mile radius of franchised territory for period of two years after termination or nonrenewal of franchise was valid and enforceable.

An employer may prevent his employee, upon termination of his employment, from using, for his own advantage or for that of a rival and to the harm of his employer, confidential information gained by him during his employment. But, the employer may not prevent the employee from using the skill and general knowledge he/she acquired or improved upon through his/her employment.

A covenant inserted in a contract for personal service restricting trade or competition or freedom of employment is not invalid and may be enforced in equity provided that it is necessary for the protection of the employer, is not injurious to the public interest, and is reasonably limited in time and space. What is reasonable depends upon the facts. Specific performance (**ED**: within this context, the granting of a preliminary injunction) is not a matter of strict and absolute right. A petition of that nature is addressed to the sound discretion of the court. It will not be granted if the conduct of the plaintiff is savored with injustice touching the transaction, even though there is no sufficient ground for the rescission of the contract.

Covenants not to compete typically have arisen in either the employment context or in the context of the sale of a business. In the context of the sale of a business, courts look "less critically" at covenants not to compete because they do not implicate an individual's right to employment to the same degree as in the employment context.

A covenant not to compete that is designed to protect a party from ordinary competition does not protect a legitimate business interest. (Presumably, ordinary competition would not meet the stiff standards required for the issuance of an injunction.)

Some courts, but not necessarily Massachusetts courts, have required 'new consideration' in order to support a subsequent covenant not to compete. 'Consideration' is what one party provides to the other party in a contractual relationship. An employee is hired to perform a certain task in a certain way for a certain rate of pay. The pay is the consideration that the employee receives from the employer. The work that the employee will perform is the consideration that the employer receives from the employee. All of this is usually set forth in an employment contract.

Some courts looking at this issue have said that there has to be new consideration to support a covenant not to compete when that covenant was not part of the original employment agreement. This is because this issue was not bargained for in establishing the basic deal. And, since such a covenant not to compete potentially has the employee giving up significant rights as to future employment, the courts feel that the employee should be paid something or receive something (more vacation time, a bonus of some kind, etc.) for this new condition of employment.

This makes common sense. It also is generally in accord with general contract principles of law which provide that any changes to a contract have to be agreed to by both parties to the contract. One party can't simply make unilateral changes to the contract or dictate new terms, generally speaking. (Although within the construction context, we all know that this happens all of the time under the Golden Rule: he who has the gold, rules!)

Some employers have made the argument that the consideration for such a covenant not to compete clause inserted post commencement of employment is continued and future employment. This is an argument that some courts have rejected.

IV. HAVING A WRITTEN EMPLOYMENT CONTRACT WITH NON-COMPETE LANGUAGE WILL IMPROVE AN EMPLOYER'S CHANCES OF OBTAINING A PRELIMINARY INJUNCTION.

Initially, I have found some case law that suggests that a covenant to compete may be implied, not necessarily having to be in writing, although these cases seem to apply more to the sale of a business than to an individual employment relationship. I think it is highly unlikely that an employer claiming a breach of an oral covenant not to compete will be successful in obtaining an injunction because: (a) of 'he said, she said' reasons; (b) of a lack of certainty in the claimed oral agreement; and (c) of the difficulty in obtaining *any* injunction.

Since the initial mechanism by which an employer will attempt to restrain a former employee in his/her subsequent employment is a request for the court issuance of a preliminary injunction – an injunction being a court order that a defendant either do something or *not* do something - two of the key issues associated with obtaining an injunction will be greatly enhanced by having a written employment agreement with covenant not to compete language.

One of the 'tests' which has to be established to get an injunction is that the plaintiff will suffer 'irreparable harm' or will have 'no adequate remedy at law' if the injunction is not granted. An injunction is considered to be an extraordinary remedy only infrequently granted inasmuch as it may essentially result in a dispositive ruling of a case without there being any trial. If an award of monetary damages is a sufficient remedy for the employer should it win its case, obtaining an injunction is not likely.

Such as is in Agreement, an acknowledgement by the employee that monetary damages will not be a sufficient remedy for the employer in the event of an employee breach of the employment contract, helps the employer as to the 'irreparable harm' or 'no adequate remedy at law' issues because the employee has already acknowledged that this would, in fact, be the case. A former employee will be less likely to prevail on contesting the necessity of an injunction when he/she has already agreed and acknowledged that there is no adequate remedy available *without* the injunction.

A second test that is necessary to be met to obtain an injunction is 'likelihood of success on the merits'. In other words, a judge reviewing the pleadings, affidavits and oral arguments

has to come away from the hearing thinking, 'this Plaintiff is probably going to win their case'. But, without having an employment agreement such as Agreement, how does one define 'trade secrets', 'confidential information' or 'good will'? Having established definitions for these terms such as are provided for by Agreement will help in the injunction endeavor because at least the plaintiff employer will have defined terms against which to measure the defendant employee's conduct.

V. SUMMARY OF SOME OF THE BASIC IDEAS APPLICABLE TO NON-COMPETE CLAUSES.

Here are some of the basic ideas taken from the above cases involved with an analysis of the enforceability of a Massachusetts non-compete clause:

1. It has to be reasonable and with due consideration to the employer's business.

2. It has to deal with actual trade secrets and confidential information. In other words, this would not be applicable to attempting to avoid simple basic competition.

3. An employee can't be restrained from future employment from using the skill and general knowledge acquired or improved upon through his employment.

4. It has to be for a reasonable period of time.

5 It has to be for a reasonable distance from the employer's place of business.

6. If this agreement and language is executed by the employee after he/she commences employment, the non-compete clause may not be enforceable without 'new consideration' given to the employee to secure such a covenant.

7. Whether any particular clause is enforceable is a question of fact to be determined by a court.

8. A court has discretion in the interpretation and application of the factual issues applicable to the seeking of a preliminary injunction, which discretion is not easily overturned by an appellate court, even where the appellate court might have decided the question differently. 'Discretion' here is a term of art which varies from the common sense meaning of the word in that it includes the idea of having a certain degree of latitude, even flexibility and personal judgment, in applying principles of law to specific factual situations.

VI. CONCLUSION.

Three final points.

First, if you do have signed employment agreements, do *not* keep these signed agreements on site. Keep them offsite in a safety deposit box or at your home or some other place under your exclusive control. That way, the ex-employee can't destroy or carry off the evidence of what the written deal is when he/she leaves your company at night for the last time. I have seen this happen before!

Secondly, try to have both of you sign the employment agreement at the same time and in front of the same notary, having the notary emboss his/her signature with the notarial seal. This will minimize, if not prevent, claims down the road that "this isn't my signature".

There can be a big difference between using a notary as compared with using an ordinary witness. You can more easily locate a notary down the road. And, a notarial signature with a seal is better evidence that this individual actually witnessed the execution of the document and that the party allegedly signing the document was actually there and did so. There was a Massachusetts case some years ago in which the court awarded triple damages against a notary for false notarizations of signatures (the person allegedly signing was not there). A notary public provides a regulated public function, subject to a variety of rules that would not be applicable to a mere 'witness'. I would think that an ordinary 'witness' would not be subject to damage claims except under very limited circumstances (possibly, in participating in a fraud). Both of you using the same notary will also tend to minimize someone's using a 'pretend' or make-believe notary who, after whatever hits the fan, will be in parts unknown. (I can think of one case I had where an 'attorney' showed up at a motion hearing and argued for the other side. Only to find out later that this individual was not a lawyer and, in fact, no one actually knew what his real name was!)

Thirdly, the concept of a written employment contract with a non-compete clause probably will work best with supervisory or administrative personnel, with project managers and with construction service professional employees, such as insurance agents/producers/brokers. Lower tier employees will not ordinarily have access to customer lists, trade secrets and the like. As such, the real possibility of their damaging their employer's business post employment would probably be a lot less and this is something a court would very likely pick up on. (I have disagreed with any number of judges over the years but can't think of one who was dumb!)

Notwithstanding, having a simple written employment contract with lower tier employees does have its advantages even if such a contract doesn't have a non-compete clause. For example, memorializing in writing that the lower tier employee is an 'employee at will' could make an ultimate termination easier down the road, as no cause or pre-conditions or certain minimum period of employment would have to be met before termination. Certainly, issues as to wages and benefits are best handled when they are in writing.

In trying to curb my clients' inclinations away from oral agreements, I often say that maybe the other person can lie better than they can tell the truth!

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EMPLOYMENT AGREEMENT

This employment agreement (hereinafter Agreement) is made and entered into this 15th day of January, 2016 between Any General Contractor, Inc. (Employer or Company), whose usual address is Any Town, Massachusetts and John Doe (Employee). The intent of this agreement is to set out the terms and conditions of Employee's employment with Employer including, without limitation, the provision of protection to and for Employer from unfair competition, disclosure and harm with regard to all legitimate secrets and confidential information of Employer which Employee will become privy to, including, but not limited to:

A. "Good Will" - meaning, without limitation, customer goodwill, consisting of the Company's relationships with its customers (and identification of its customers) and its reputation and special expertise in the industry in which Company is engaged, described briefly as the construction of large 'Green' buildings for both public and private owners, which generates business with existing customers and new business with future customers, and;

B. "Trade Secrets" - referencing, without limitation, any formula, pattern, method of bidding or estimating, method of performing work, device or compilation of information which is used by the Company, and which Employee herein acknowledges was developed at considerable time and expense by the Company prior to his/her employment and which gives the Company an opportunity to obtain an advantage over competitors who do not know of or use it/them, and;

C. "Confidential Information" - meaning, without limitation, all trade secrets as well as all customer or supplier lists and computer files held or maintained by Employer of any kind or description, including names and all relevant information gathered through the Company's time, effort and expense both prior to and during Employee's employment including, without limitation: quotations, which are in the process of being made or which have been previously made and not yet accepted, to existing or potential customers; histories of prior purchases, prices paid, discounts offered or given; the names of designated contact persons at vendors and clients; all marketing studies and strategies of any kind or nature; advertising campaigns, slogans and methods; rolodexes or other such devices, including any form of computer files; plans for expansion or new merchandising techniques or products; methods of estimating jobs and of figuring pricing; product mixes or information regarding the success or failure of past marketing and performance techniques; the identity of all prior customers and jobs worked at or estimated by Employer, continuing throughout the period of Employee's employment with Employer.

In exchange of valuable consideration received by the Employee from the Employer, herein acknowledged as received by the Employee, including, without limitation, present or continued

employment with Employer, and the compensation and benefits listed below, the Employee and Employer herein agree that:

1. Employee shall not directly or indirectly as owner, partner, shareholder, supervisor or sales manager or in any other capacity engage in a business similar to the operations carried on by Employer for a period of two years subsequent to Employee's termination (however that occurs) and within a distance of one hundred miles from the principal place of business of Employer, which is located in Any Town, Massachusetts. This Agreement includes Employee's promise, herein made, that he or she will not communicate to any future employer or business partner the information listed in paragraphs A through C above for at least the minimum period of two years from termination, however caused, and longer, if so allowed by law. Employee further agrees that the information identified in paragraphs A through C above is sensitive and of extreme importance to Employer and that any disclosure of that information could leave Employer with no adequate remedy of law, thus entitling Employer, if necessary and in the sole exercise of Company's judgment, to protect these rights by seeking injunctive relief in a court of competent jurisdiction, which Employee agrees is the district court or superior court having jurisdiction/venue over Any Town, Massachusetts or over the town in which Employee lives, the choice being at Employer's sole election. Employee agrees that Employer shall be entitled to an award of the reasonable attorneys' fees and costs it incurs in protecting its rights under this Agreement if Employer is successful in obtaining any form of judicial relief but not otherwise. Employee further agrees to return to Employer within one day of his/her termination, however caused, any Employer property he/she has in his/her possession or control without keeping any copies of the same and that a failure to do so will constitute a material breach of this Agreement. Both parties hereto acknowledge that nothing in this Agreement shall prohibit Employee's working as a mechanic or tradesman (i.e. 'working with the tools') subsequent to termination with Employer, however caused, which labor is not subject to the two year limitation and the one hundred mile limitation listed above.

2. This Agreement is for employment of Employee as an "Employee-at-will" as understood under Massachusetts law, meaning, without limitation, that the employment is not for any particular period of time and is not, in any fashion, guaranteed for any particular length of time and that no compensation or benefits are due to Employee under this Agreement except as specifically set forth in the next paragraph.

3. This Agreement between Employer and Employee as to the terms and conditions of employment of the Employee are as follows:

· Hours expected from the Employee on a weekly basis _____

· Weekly compensation (before taxes) _____

· Other benefits shall be as follows:

. Bonus upon executing this Agreement: five hundred dollars (**ED**: This would apply more/be more necessary as to employment agreements with non-compete language presented to the employee some time after the employment relationship commences.)

No other terms and conditions with regard to hours of work expected, compensation or benefits exist for the purposes of this Agreement or for the purposes of Employee's employment with Employer.

4. Employer and Employee herein agree that if any provision(s) of this Agreement is/are unenforceable, the remaining provisions of the Agreement shall remain in full force and effect.

5. This agreement is controlled by and subject to Massachusetts law, both procedurally and substantively.

6. The above constitutes the entire Agreement between Employee and Employer, both parties acknowledging that any modification of this Agreement shall only be binding upon both parties hereto if in writing and only if signed by both parties hereto.

7. This Agreement is three pages in length.

WITNESS our hands and seals to this Agreement, executed as a sealed contract, this

fifteenth day of January, 2016.

_____
John Doe

_____, ss

On this fifteenth day of January, 2016, before me, the undersigned notary public, personally appeared John Doe, who, after being duly sworn, proved to me through satisfactory evidence of identification his identity, which was a Massachusetts driver's license, and who acknowledged to me that he signed this Employment Agreement voluntarily and that his signing of this Employment Agreement was his free act and deed.

_____
Notary Public:

My Commission Expires:

_____
Any General Contractor, Inc.
By: John Q. Public, President

_____, ss

On this fifteenth day of January, 2016, before me, the undersigned notary public, personally appeared John Q. Public, President of Any General Contractor, Inc., who, after being duly sworn, proved to me through satisfactory evidence of identification his identity, which was a Massachusetts driver's license, and who acknowledged to me that he signed this Employment Agreement voluntarily as his free act and deed in the capacity indicated and that he was authorized by Any General Contractor, Inc. to execute this Agreement on its behalf.

_____
Notary Public:

My Commission Expires:

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* A *'squib'* is defined as 'a short humorous or satiric writing or speech'. Wiktionary defines a '*squib'* as: "a short article, often published in journals, that introduces empirical data problematic to linguistic theory or discusses an overlooked theoretical problem. In contrast to a typical linguistic article, a squib need not answer the questions that it poses."

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