Anti-Raiding Provision Upheld by Massachusetts High Court

By Erik J. Winton

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Restrictive covenant matters rarely make it through the appellate courts. This is true for a number of reasons, including the fact that the time-sensitive nature of restrictive covenant litigation often compels parties to achieve a resolution before their case can work its way through the court system. The dearth of appellate case law is even more pronounced for anti-raiding covenants, which appear to provoke fewer lawsuits than non-compete and customer non-solicitation covenants.

Notably the Massachusetts' Supreme Judicial Court (SJC or the Court) issued a comprehensive opinion evaluating the validity of an anti-raiding provision on Tuesday, January 14, 2020. *See Automile Holdings, LLC v. McGovern*, SJC-12740 (Mass. Jan. 14, 2020). Even more noteworthy, perhaps, was that the SJC upheld the provision despite the current climate of anti-restrictive covenant headwinds.

In addition to the reforms set forth in the Massachusetts Noncompetition Agreement Act, non-competes and other restrictive covenants have come under intense scrutiny at both the federal (See articles dated February 18, 2019, March 25, 2019, November 18, 2019, and November 21, 2019) and state (See articles dated April 2, 2018, March 26, 2019, May 8, 2019, and June 7, 2019) levels. Anti-raiding covenants have not been spared from those efforts. In 2019, Maine and Washington State enacted restrictions on no-poach agreements. Meanwhile, the U.S. Department of Justice continues to treat no-poach agreements as potential antitrust violations (see articles dated January 25, 2018, April 25, 2018, and July 17, 2018), while the Federal Trade Commission recently signaled its willingness to promulgate a rule banning or limiting such agreements as well.

The *Automile* Decision

In November 2007, Matthew McGovern (McGovern) became a founding member, as well as the Chief Financial Officer, of Prime Motor Group (Prime). Nearly a decade later, after a change in position to Vice President of Operations, McGovern was fired by Prime in connection with disagreements over the company's future.

After McGovern's termination, and in connection with the sale of his ownership interest in Prime, McGovern agreed not to "directly or indirectly ... solicit for hire or hire [Prime employees] or encourage [Prime employees] to leave the employment" of Prime for a period of approximately sixteen months.

Following the execution of the agreement, and while the restricted period was still running, McGovern solicited and/or hired several Prime employees. In response, Prime filed suit against McGovern, seeking injunctive relief as well as monetary damages.

As an initial matter, the lower court determined that the anti-raiding provision was legal and enforceable, and that McGovern violated it. However, and not surprisingly, the court declined to reverse the hires, concluding that it could not restore the employees' relationships with Prime, and that ordering their terminations from McGovern would be punitive to the employees without conferring any benefit to Prime. Instead, and notwithstanding the absence of a tolling provision in the agreement, the court extended the duration of the restricted period by one year.

McGovern appealed the lower court's ruling on two grounds. First, he argued that the anti-raiding provision was invalid because it did not serve to protect a legitimate business interest. Second, he asserted that the lower court abused its authority when it extended the duration of the provision's restricted period despite the absence of a tolling provision in the agreement. Notably, the Supreme Judicial Court, which acknowledged that it had not addressed either issue in prior decisions, transferred the appeal from the appellate court to the Supreme Judicial Court on its own motion.

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The Anti-Raiding Provision Was Valid

Under Massachusetts common law, a restrictive covenant must satisfy the following conditions in order to be enforceable: (a) it must be necessary to protect a legitimate business interest; (b) it must be reasonably limited in time and space; and (c) it must be consonant with public policy. However, as the Court explained, the standard for evaluating those conditions is more stringent in a traditional employment relationship as compared to the sale of a business or a business interest. That is because the seller of a business or business interest generally has greater bargaining power than a run-of-the-mill employee, and the heightened ability to negotiate with the employer reduces the expected hardship caused by the promise.

In reviewing whether McGovern's anti-raiding provision was supported by a legitimate business interest, the Court noted that the lower court described Prime's business interest as a desire to prevent the raiding of employees. Per that description, the purpose of the anti-raiding provision would seemingly fall outside of the typical "legitimate business interests that may be protected ... in the employer-employee context," which both the common law and the Massachusetts Noncompetition Agreement Act limit to "trade secrets, confidential information, and good will." However, the Court concluded that McGovern entered into the agreement in the context of the sale of a business interest, and in such context, a restrictive covenant need not be supported by the above-referenced business interests.

Notwithstanding the above distinction, the Court indicated that the anti-raiding provision was also necessary to protect Prime's confidential information. As the Court explained, McGovern's employment with Prime gave him "inside knowledge of the company, including its salary structure and internal management dynamics," which he could exploit in order to solicit and hire Prime's best employees for the benefit of his competing business. By invoking the business interest of protecting its confidential information, it could be argued that the Court endorsed anti-raiding provisions in both the traditional employment and buyer-seller contexts.

The SJC's invocation of employee salary information as protectable confidential information is interesting, given that the Massachusetts Equal Pay Act makes it unlawful in certain circumstances to restrict the disclosure of employee compensation information. On the other hand, it is not unheard of for courts to cite an employee's knowledge of such information as justification for the imposition of an employee non-solicitation covenant. *See, e.g., Carlson Envtl. Consultants, PC v. Slayton*, 2017 U.S. Dist. LEXIS 154191, *10 (W.D. N.C. 2017) ("Slayton ... had direct knowledge of employee salaries and bonuses at CEC, thus making his employee non-solicitation provision particularly important, because he possessed information that could enable him to lure employees away were he to join a competitor.").

The Lower Court Erred by Equitably Tolling the Restricted Period

The Court next reviewed the lower court's decision to toll the duration of the anti-raiding provision as a form of equitable relief. In doing so, the Court was guided by two principles. First, Massachusetts common law "greatly disfavor[s] restrictions on an individual's ability to freely earn a living." Second, Massachusetts law closely abides by the general principle that parties are held to the express terms of their contract.

Interestingly, the Court found that the first principle favored Prime because the anti-raiding provision "does not ... preclude anyone from earning a living." Moreover, notwithstanding the general rule against deviating from the express terms of a contract, the Court affirmed the theoretical legitimacy of "awarding equitable relief that extends the scope of the restrictive covenant beyond its plain terms[.]" where appropriate. However, the Court held that such relief is only proper where the party seeking such relief "has demonstrated that monetary damages would provide inadequate relief." Concluding that the company did not establish that element, the Court reversed the lower court's decision to toll McGovern's anti-raiding provision beyond the terms of the agreement.

Conclusion

The *McGovern* decision is one of the rare instances in which a Massachusetts court has expounded on the types of protectable interests that would support an anti-raiding provision. It also provides a useful guide for how Massachusetts courts can be expected to confront restrictive covenants that are not covered by the Massachusetts Noncompetition Agreement Act (which specifically excludes employee non-solicitation covenants from coverage).

The decision also contains important nuances that should be understood by employers who are considering the use of anti-raiding provisions. While the decision endorses the use of anti-raiding provisions in connection with the sale of a business, the Court's reasoning suggests that such provisions may also be enforceable in the traditional employment context, provided the employer can demonstrate that they are necessary to protect its confidential information, trade secrets, or good will.

This is what many practitioners have long assumed to be the case, despite the lack of clear case law confirming that position. Further, while the Court rejected equitable tolling in this particular case, it also indicated that such action could potentially be permissible had the plaintiff clearly established the insufficiency of monetary damages. Of course, the easiest solution, as the Court suggested, would be to simply include a tolling provision in the restrictive covenant agreement.

As always, employers are encouraged to consult an experienced non-compete attorney at Jackson Lewis before drafting or enforcing an employment-related agreement that contains restrictive covenants.