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Pennsylvania Supreme Court:
Employers Who Want Restrictive Covenants From
Current Employees Must Give New Benefits[1]

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As we discussed in a Client Alert in the middle of 2014, employers occasionally realize that their current employees did not sign post-employment restrictive covenants when they were hired. Over the years, the company has grown or changed, and the employer wants to have such restrictions in place in case an employee leaves and joins a competitor.

For years, many employers solved this problem by simply asking their employees to sign a new agreement as a condition of continued employment, using language that the employer and employee "intended to be legally bound." In May 2014, Pennsylvania's Superior Court held that this is not enough. Socko v. Mid-Atlantic Systems of CPA, Inc., No. 1223 MDA 2013 (Pa. Super. May 13, 2014). The Court held that a company must provide tangible new and valuable "consideration" to make new restrictive covenants for existing employees valid.

The employer-defendant appealed that case to the Pennsylvania Supreme Court. For more than a year, Pennsylvania employers waited, hoping that the Supreme Court would reverse the decision. But yesterday, the Court dashed those hopes. It agreed with the Superior Court's analysis and affirmed the decision. Thus, as a practical matter, Pennsylvania employers who failed to have employees sign restrictive covenants when they were hired must now offer something extra – beyond just magic language and another day of employment – in order to get a new, enforceable agreement.

The Supreme Court's decision in Socko v. Mid-Atlantic Systems of CPA, Inc., No. 142 MAP 2014 (November 18, 2015) arose out of an employment relationship between a basement waterproofing company and a salesman. In late 2010, Socko, who was already employed by Mid-Atlantic and had previously entered into two different employment agreements, signed a third employment agreement. This agreement contained a broader restrictive covenant and indicated that the parties "intend to be legally bound."

Shortly after signing this third agreement, Socko resigned and joined a different basement waterproofing company (Pennsylvania Basement Waterproofing), located in Camp Hill, Pennsylvania, well within the geographical area forbidden by his third employment agreement.

[1] This article is designed to provide one perspective regarding recent legal developments, and is not

Mid-Atlantic sent a copy of Socko's third employment agreement to Pennsylvania Basement Waterproofing and threatened litigation. Pennsylvania Basement Waterproofing fired Socko. Socko then sued Mid-Atlantic, claiming that the third employment agreement was invalid because he never received additional consideration.

Mid-Atlantic argued that because both it and Socko had expressly stated in the employment agreement that they "intended to be legally bound," Socko was barred from challenging the lack of consideration. Under Pennsylvania's Uniform Written Obligations Act ("UWOA"),[2] a promise may not be held invalid or unenforceable for lack of consideration so long as the contract states that the parties "intend to be legally bound." And of course, there was no dispute here that the third employment agreement contained this language.

But the Supreme Court rejected Mid-Atlantic's reliance on the UWOA. While recognizing that the UWOA would ordinarily bar Socko's challenge to a lack of consideration in any *other* kind of contract, the Court concluded that agreements involving restrictive covenants are different. In light of the history of cases holding that restrictive covenants are disfavored, the Court held that it would be unreasonable to interpret the UWOA to eliminate the requirement of consideration.

So we are back to the issue we posed in our Client Alert a year and a half ago: what should an employer do? And we reiterate the options here. First, use restrictive covenants with new employees – that is by far the easiest and best time to get them signed. Second, when considering <u>new</u> restrictive covenants for existing employees, try to tie those to a specific change involving the employee. For example, think about having an employee sign new restrictive covenants when he or she is promoted, or when the employee gets a raise. Similarly, consider providing discretionary bonuses to employees tied to the signing of the new agreement. And of course, ask a lawyer to review your agreements and provide suggestions before presenting the agreements to your potential or current employees.

[2] 33 Pa. Consol. Stat. Ann. § 6 (2014).