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PENNSYLVANIA EMPLOYMENT LAW ALERT- RESTRICTIVE COVENANTS[1]

Pennsylvania: Even Creative Attempts Will Not Make a New Restrictive Covenant Enforceable Without Giving New Benefits To An Existing Employee

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Pennsylvania courts have long required that when an employee signs an agreement that contains post-employment restrictive covenants, he or she must receive something in return. In legal terms, there must be "valuable consideration" to the employee in exchange for the promise not to compete or solicit after the employment ends. Many times, this is not a problem for employers, because Pennsylvania courts have been clear that restrictive covenants that are signed upon hiring have sufficient consideration (the new job itself is the consideration).

The more difficult issue arises when an employer wants to impose restrictive covenants on existing employees. In this situation, the employer must offer something in return. Traditionally, such things as a job promotion, a raise, a discretionary bonus, or similar inducements are provided to ensure that the restrictive covenants are enforceable.

On May 13, 2014, the Pennsylvania Superior Court clarified that such "valuable consideration" is required even when the language of the agreement makes it clear that the parties "intend[ed] to be legally bound." In doing so, the Court reaffirmed the view that (1) restrictive covenants are generally disfavored; and (2) where they are to be enforced, an actual exchange of consideration is a *sine qua non* of such an agreement.

In Socko v. Mid-Atlantic Systems of CPA, Inc., No. 1223 MDA 2013 (Pa. Super. May 13, 2014), the Superior Court affirmed the lower court's holding that refused to enforce new restrictive covenants

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1 This article is designed to provide one perspective regarding recent legal developments, and is not intended to serve as legal advice, nor does it establish an attorney-client relationship with any reader of the article where one does not exist. Always consult an attorney with specific legal issues.

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signed by an existing employee.[4] In Socko, a basement waterproofing company hired a salesman in 2007, at which time he signed an employment agreement containing a two-year non-compete clause. The employee resigned in early 2009, but was rehired a few months later. He then executed a contract with the same non-compete provision. Then, in late 2010, the company and the employee entered into a third employment agreement containing a broader restrictive covenant, which added a geographical limitation on where the employee could work if he left the company.

Shortly after signing this third agreement, the employee resigned and joined a competitor business. The original employer sent a demand letter to the competitor business, which terminated the employee. The employee then filed suit, claiming that his third employment agreement was invalid for lack of consideration. For example, he pointed out that there had been no change to his job status or responsibilities between 2009 and 2010.

The employer argued that it was not required to provide the employee with any new consideration because under Pennsylvania's Uniform Written Obligations Act ("UWOA"),[5] 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." There was no dispute here that the employee's third employment agreement did in fact contain this language.

However, the Superior Court was not persuaded. While such language is important in all contracts, the Court explained that restrictive covenants are different. The contractual language stating that the parties "intend to be legally bound" was insufficient to overcome the fact that the employee was not getting anything in return for agreeing to the terms of the new restrictive covenant.

Importantly, the Superior Court's decision did not address whether the employee could still be bound by either of the first two restrictive covenants that he had signed upon his initial hire and his 2009 rehire, and nothing in the Court's opinion appears to invalidate restrictive covenants generally. Rather, the Court merely affirmed the long-standing requirement that restrictive covenants signed during the course of employment must be supported by adequate new consideration, such as additional job responsibilities or benefits.

So what's an employer to do? First, use restrictive covenants with new employees – that is by far the easiest and best time to get them signed. Second, when considering new restrictive covenants for existing employees, it is useful 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. Similarly, consider a bonus for an employee that is tied to the signing of the new agreement. In short, always keep in mind the concept that the restrictive covenant is just a contract – a business deal like any other – and that both sides have to get something out of the deal for it to be enforceable. And of course, ask a lawyer to review your agreements and provide suggestions before presenting the agreements to your potential or current employees.

If you have any questions about the issues discussed in this article, please contact Jason Murtagh at jmurtagh@rubinfortunato.com or 610-408-2059.

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4 Socko v. Mid-Atlantic Systems of CPA, Inc., No. 1223 MDA 2013 (Pa. Super. May 13, 2014).

5 33 Pa. Consol. Stat. Ann. § 6 (2014).