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New Jersey

NON-COMPETES

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1. Enforcement—General

Under what circumstances will a New Jersey court enforce a non-compete agreement?

New Jersey's courts will enforce a non-compete agreement "if it simply protects [1] the legitimate interest of the employer, [2] imposes no undue hardship on the employee and [3] is not injurious to the public." This is known as the *Solari/Whitmyer* test.[1] "The first two prongs of the test require a balancing of the employer's interests… and the asserted hardship on the employee."[2] The third prong requires that the court consider and analyze "the public's broad concern in fostering competition, creativity and ingenuity."[3] Inquiry under the *Solari/Whitmyer* test is fact intensive, requiring that the parties' various interests be identified and then "gauged for reasonableness and legitimacy."[4]

1 Ingersoll-Rand Co. v. Ciavatta, 110 N.J. 609, 628, 542 A.2d 879, 888 (1988); Solari Industries, Inc. v. Malady, 55 N.J. 571, 264 A.2d 53 (1970); Whitmyer Brothers, Inc. v. Doyle, 58 N.J. 25, 274 A.2d 577 (1971).

2 Maw v. Advanced Clinical Communications, Inc., 179 N.J. 439, 447, 846 A.2d 604, 609 (2004) (quoting Ingersoll-Rand, 110 N.J. at 634–35, 542 A.2d at 892).

3 *Id.* (quoting Ingersoll-Rand, 110 N.J. at 639, 542 A.2d at 894).

4 *Id.*

2. Protectable interests

Define the legitimate or protectable interests that give rise to enforcement of a non-compete agreement or other restrictive covenant.

Employer-employee relationship

Under New Jersey law, confidential and proprietary information is protected even in the absence of an agreement to that effect.[5] This subject is more fully addressed in section 10 below.

Customer relationships are protectable interests via restrictive covenants.[6] There must be evidence that the employer's customers represent a significant investment of time, effort, and money which is worthy of protection.[7] Simply because customers' names are publicly available, the fact that they are the employer's customers may not be known, and the confidential nature of the relationship between the employer and employee *vis-à-vis* that information may mandate protection.[8] The fact that a former employee was the key contact with the customer, who would have to be replaced in that relationship, is a factor favoring enforcement.[9] An employee's unique status may be a protectable interest.[10]

A non-compete agreement may not be used to preclude customer contacts that experienced employees originally brought with them to the job. Just as a tradesman might bring his own tools, or a scientist his own knowledge, an employee cannot be stopped from taking information gained on one job to the next job.[11] "An employee leaving an employer is entitled to use the basic expert abilities that he or she has acquired in the field."[12] The employee cannot be expected to "erase all of the technical expertise he obtained over the course of… years of hands-on experience in the industry."[13]

A court will enforce a non-compete when contacts with clients were formed during the time with the employer, and the employer was "instrumental in cementing the relationship between [the employee] and the new [client] contact," although this does not automatically extrapolate to employees with long years at the employer.[14] Restrictive covenants involving doctors are not per se unenforceable. Protectable interests may include: "(1) protecting confidential business information, including patient lists; (2) protecting patient and patient referral bases; and (3) protecting investment in the training of a physician."[15] Restrictive cove-

[5] Lamorte Burns & Co. v. Walters, 167 N.J. 285, 298, 770 A.2d 1158, 1166 (2001).

[6] Jackson Hewitt, Inc. v. Childress, 2008 U.S. Dist. LEXIS 4640, at *20 (citing Whitmyer Brothers, 58 N.J. at 33); A.T. Hudson & Co. v. Donovan. 216 N.J. Super. 426, 433, 524 A.2d 412, 415 (App. Div. 1987).

[7] Laidlaw, Inc. v. Student Transportation of American, Inc., 20 F. Supp. 2d 727, 760 (D.N.J. 1998).

[8] Platinum Management, Inc. v. Dahms, 285 N.J. Super. 274, 295, 298, 666 A.2d 1028, 1038, 1040 (Law Div. 1995).

[9] United Board & Carton Corp. v. Britting, 63 N.J. Super. 517, 533–34, 164 A.2d 824, 833 (Ch. Div.), *modified by* 61 N.J. Super. 340, 160 A.2d 660 (App. Div. 1960), *cert. denied*, 33 N.J. 326, 164 A.2d 374 (1960) (court considered time needed to replace employee).

[10] Platinum Management, Inc. v. Dahms, 285 N.J. Super. at 294, 666 A.2d at 1037.

[11] Coskey's Television & Radio Sales and Service, Inc. v. Foti, 253 N.J. Super. 626, 602 A.2d 789 (App. Div. 1992); Platinum Management v. Dahms, 285 N.J. Super. at 294, 666 A.2d at 1038.

[12] Thomas & Betts Corp. v. Richards Manufacturing Co. 2008 U.S. Dist. LEXIS 47238, at *168, *rev'd on other grounds*, 342 F. App'x 754; 2009 F. App'x 16837 (3d Cir.).

[13] *Id.*

[14] Coskey's v. Foti, 253 N.J. Super. 626; Platinum Management v. Dahms, 285 N.J. Super. at 294.

[15] Community Hospital Group, Inc. v. More, 183 N.J. 36, 58, 869 A.2d 884, 897 (2005).

nants *are* unenforceable against licensed psychologists.[16] Covenants that restrict lawyers' activities are also unenforceable.[17]

The employer is generally not entitled to enforce the restrictive covenant if it is "principally directed at lessening competition."[18]

Information unworthy of protection includes "matters of general knowledge within the industry" and "routine or trivial differences in practices and methods."[19]

Sale of a business or other transaction

New Jersey's courts will enforce restrictive covenants in the sale of business context, and in doing so will "afford more deference to restrictive covenants ancillary to the sale of a business than those that accompany employment contracts."[20] Sale of business covenants are given "far more latitude" because the seller is being compensated for the business's good will, and if the seller can trade on that good will by opening a competitive business in the competitive area, it "would destroy the essence of the transaction."[21]

The buyer is considered to have paid separate consideration in purchasing the good will associated with customer relationships.[22] Thus, good will in connection with the sale of a business creates a protectable interest for restrictive covenant analysis.[23] In one case, a trial court was even permitted to read some level of a restrictive covenant into a sales agreement.[24] Where the seller stays on as an employee after the sale, courts will look at the timing of the seller/employee's departure in deciding whether to apply the employer/employee analysis or sale of business analysis.[25]

In the context of franchise agreements, non-competes are closer to restrictive covenants negotiated as part of a sale of business agreement.[26] Franchisors have an interest in the good will they develop in an area and in putting a new franchise in that area; a non-compete gives the franchisor time to transfer its customers from the former franchisee to a new franchisee.[27] Unlike a franchise agreement, however, a product distributionship agreement is not like a sales agreement, and will be tested in the same manner as an employment agreement.[28]

Business Contract

In the context of a contractor entering a business relationship with a subcontractor to perform certain services, the court refused to provide injunctive relief in the presence of a contractual non-compete agree-

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16 Comprehensive Psychology System, P.C. v. Prince, 375 N.J. Super. 273, 274–77, 867 A.2d 1187, 1189–90 (App. Div. 2005).

17 Jacob v. Norris, McLaughlin & Marcus, 128 N.J. 10, 607 A.2d 142 (1992).

18 Richards Manufacturing Co. v. Thomas & Betts Corp, 2005 U.S. Dist. LEXIS 22479, at *33 (D.N.J.), (citing Raven v. A. Klein & Co., 195 N.J. Super. 209, 213, 478 A.2d 1208, 1210 (App. Div. 1984), *rev'd on other grounds*, 342 F. App'x 754); 2009 F. App'x 16837 (3d Cir.).

19 Whitmyer Brothers, 58 N.J. at 34.

20 Athlete's Foot v. FL Consulting, 2007 U.S. Dist. LEXIS 32995, at *5.

21 Laidlaw, 20 F. Supp. 2d at 754 (quoting Coskey's v. Foti, 253 N.J. Super. 626).

22 Laidlaw, 20 F. Supp. 2d at 754.

23 Jiffy Lube International v. Weiss Brothers, 834 F. Supp. 683, 690–91 (D.N.J. 1993)

24 Graziano v. Grant, 326 N.J. Super. 328, 741 A.2d 156 (App. Div. 1999).

25 Laidlaw, 20 F. Supp. 2d at 754–61.

26 Athlete's Foot, 2007 U.S. Dist. LEXIS 32995 at *5, (citing Jiffy Lube International, 834 F. Supp. at 690–91).

27 Jackson Hewitt, Inc. v. Childress, 2008 U.S. Dist. LEXIS 4640, at **20–21.

28 Meadox Medicals, Inc. v. Life Systems, Inc., 3 F. Supp. 2d 549, 552 n.2 (D.N.J. 1998).

ment where the subcontractor allegedly did business with the client directly, cutting the contractor out of the business. This was not on the basis that the claim lacked merit, but rather that such a breach of the non-compete did not constitute irreparable harm. The court found that a contractual provision stating that the parties agreed that a violation of the non-compete by itself would constitute irreparable harm was not enforceable without further specific evidence of irreparable harm, *i.e.*, such language by itself cannot substitute for an irreparable harm analysis. The court further found that the alleged loss of business, and putative road to the destruction of the contractor's business through the subcontractor's conduct in going directly to the client—absent any taking of confidential information in soliciting that business—involved a calculable monetary loss that could not constitute irreparable harm for injunctive relief.[29]

3. Reasonableness

What factors might a New Jersey court consider in determining whether the scope of a restriction is reasonable in time, geography, or with respect to the type of activity prohibited?

Courts determining whether a restrictive covenant is reasonable or overbroad will look at "its duration, the geographic limits, and the scope of activities prohibited."[30] "Each of those factors must be narrowly tailored to ensure the covenant is no broader than necessary to protect the employer's interests."[31] In the sale of business context, "the length of time that is reasonable in order to protect good will varies under the circumstances."[32] One court rejected the argument that the geographic scope should be determined by the employer's business locations at the time the non-compete was executed, rather than at the time of termination.[33] In that case, the restriction prohibited the employee from competing within fifty miles of any of the employer's branches; and the number of branches had increased subsequent to the time the parties entered the employment agreement. Because the contract language was plain, the restriction included even those newer branch locations.

Examples of reasonable covenants

- Twenty-four month non-compete in same geographic sales area in which former employee worked enforceable.[34]
- Six month, twenty-five mile, non-competition agreement was concededly reasonable and enforceable against former employee.[35]
- After detailed analysis, court rules that fifty mile radius restriction is reasonable.[36]
- A one-year non-competition agreement against a defaulting franchisee, whom the franchisor had terminated, was held to be enforceable.[37]
- Restrictions of two years and a ten-mile radius in a franchising agreement were enforceable.[38]

[29] AV Solutions, LLC v. Keystone Enterprise Services, LLC, 2011 U.S. Dist. LEXIS 78882 (D.N.J.).
[30] Community Hospital Group, Inc., 183 N.J. at 58, 869 A.2d at 897.
[31] *Id.* at 58–59.
[32] Laidlaw, 20 F. Supp. 2d at 756.
[33] National Reprographics, Inc. v. Strom, 621 F. Supp. 2d 204, 223–224 (D.N.J. 2009).
[34] Trico Equipment, Inc. v. Manor, 2009 U.S. Dist. LEXIS 50524, *17–20 (D.N.J.).
[35] Esquire Deposition Servs., LLC v. Boutot, 2009 U.S. Dist. LEXIS 52207, **nn. 3, 12 (D.N.J.).
[36] National Reprographics, Inc. v. Strom, 621 F. Supp. 2d at 224–225.
[37] Athlete's Foot Marketing Associates, 2007 U.S. Dist. LEXIS 32995, at **5–6.
[38] Jackson Hewitt, Inc., 2008 U.S. Dist. LEXIS 4640, at **21–23.

- A one-year non-compete provision with no geographic limitation applicable to the former employee's attempts to find work with the employer's direct competitors was upheld against a telemarketer involved in the student loan business.[39]
- A one-year period with no geographic limit was enforceable where an employee of a consulting firm was restricted from going to work for the employer's current clients. The provision essentially sought to protect existing customer relationships rather than a territorial sphere of influence.[40]
- A three-year world-wide restriction in a separation agreement was enforceable.[41]
- A two-year non-solicitation period after the split up of an accounting partnership was held to be reasonable.[42]
- A two-year post-termination non-compete that covered the entire United States against a 62-year-old broker (cookie salesperson) was enforceable.[43]
- A two-year post-employment agreement not to solicit any business from, or render any services to, any business which had been the corporation's customer at any time, or "from time to time," within the two years before that individual's employment terminated, was enforceable.[44]

Examples of unreasonable covenants

- A five-year non-compete period, applied to any state east of the Mississippi or to any state where the employer operated, was held to be unenforceable where no legitimate protected interests could be established on the record before the court. A restrictive covenant will apparently never be enforced to preclude client contact when the customers are government entities and public bidding is involved, as price, not relationship, is the only determinant.[45]
- The court would not enforce a restrictive covenant with geographical restrictions potentially covering all fifty states and restricting employee "from participating in any business competitive with [former employer] or its affiliates 'heretofore now or hereafter carried on by the Group.'"[46] Such terms would require the employee to "anticipate which business activities [the former employer] and its affiliates intend to engage in so as not to run afoul of its provisions."[47]
- An agreement not to compete will not be enforced where the former employee was dealing with a common customer, but with different products.[48]
- A contractual restrictive covenant will not be enforced where it generally bars the former employee from divulging "any information" about the employer's business. Such overbroad language is "tantamount

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39 Scholastic Funding Group, LLC v. Kimble, 2007 U.S. Dist. LEXIS 30333, at **12–16.

40 Pathfinder, L.L.C. v. Luck, 2005 U.S. Dist. LEXIS 44782, at **17–20.

41 Mansol Industries, Inc. v. Singh, 1996 U.S. Dist. LEXIS 22823 (D.N.J.).

42 Schuhalter v. Salerno, 279 N.J. Super. 504, 508–17, 653 A.2d 596, 598–603 (App. Div.1995), *cert. denied*, 142 N.J. 454, 663 A.2d 1361 (1995).

43 Gach v. Century Cookies, Inc., 1985 U.S. Dist. LEXIS 18938.

44 A.T. Hudson & Co. v. Donovan, 216 N.J. Super. 426, 524 A.2d 412 (App. Div. 1987).

45 Whitmyer Brothers, Inc. v. Doyle, 58 N.J. at 37–38, 274 A.2d at 583–84.

46 Trading Partners Collaboration, LLC v. Kantor, 2009 U.S. Dist. LEXIS 48195, **15–17 (D.N.J.).

47 *Id.*

48 Intarome Fragrance & Flavor Corp. v. Zarkades, 2007 U.S. Dist. LEXIS 22870, at **8–13.

to prohibiting [an] employee from ever using in another job the experience he obtained during his employment."[49]

- A manufacturer had no protectable interest in a client base that it did not directly or indirectly assist in developing, and could not enforce the one-year restrictive covenant over a designated territory.[50]

See also, the sections of this chapter discussing blue-penciling and defenses to enforcement.

4. Customer non-solicitation agreements

Do the courts enforce covenants not to solicit customers more liberally than covenants not to compete?

Yes. "Nonsolicitation agreements are designed to protect an employer's existing client base."[51] The case law indicates that New Jersey's courts will look closely at solicitation of the employer's customers because of the potential investment of time, energy, and money devoted by the employer to obtaining those customers.[52]

Whereas both non-compete and non-solicitation agreements are concerned with the reasonableness of the duration of those restrictive covenants, "geographic limitations do not appear necessary for non-solicitation provisions."[53] Because this is a clearly identifiable legitimate employer interest that merits protection, such covenants will naturally be more frequently enforced than more general non-competes that may not encompass any protectable interests. However, even these will be subject to scrutiny. In *NASC Services*,[54] where the customer list consisted of names that could readily be put together by public internet searches, there was apparently no violation of a non-solicitation covenant even where former employees would be approaching those same customers for a competitor.

Typically though, the concern for customer protection is greater in both the non-solicitation and non-compete contexts.[55] The courts show less concern with efforts to obtain covenants not to solicit potential customers that were not actual customers.[56]

In denying a preliminary injunction motion, the court stated that "merely being in contact with former clients does not constitute solicitation."[57] This is particularly important where former employees must be in contact with clients on matters unrelated to former employment.[58] An affidavit from the employer's representative alleging communications between the former employees and the clients does not meet the high standard to obtain a preliminary injunction.[59] The withdrawal of numerous clients during a short time period does not establish solicitation, but may simply reflect the clients' own independent decisions to go

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[49] Richards Manufacturing Co. v. Thomas & Betts Corp, 2005 U.S. Dist. LEXIS 22479, at **11–12 (citing Hudson Foam Latex Products, Inc. v. Aiken, 82 N.J. Super. 508, 516, 198 A.2d 136, 140 (App. Div. 1964), *rev'd on other grounds*, 342 F. App'x 754); 2009 F. App'x 16837 (3d Cir.).

[50] Meadox Medicals, Inc. v. Life Systems, Inc., 3 F. Supp. 2d 549 (D.N.J. 1998).

[51] NASC Services, Inc. v. Jervis, 2008 U.S. Dist. LEXIS 40502, at *10.

[52] *Id.*; A.T. Hudson & Co. v. Donovan, 216 N.J. Super. at 434, 524 A.2d at 416; Coskey's Television & Radio Sales and Services, Inc. v. Foti, 253 N.J. Super. at 637, 639, 602 A.2d at 794–95.

[53] Trico Equipment, Inc. v. Manor, 2009 U.S. Dist. LEXIS 50524, *19.

[54] NASC Services, at *10 (citing to New Jersey and Connecticut law).

[55] Scholastic Funding Group, LLC v. Kimble, 2007 U.S. Dist. LEXIS 30333, at *24 (D.N.J.).

[56] *Id.* at **28–29.

[57] ING Life Ins. & Annuity Co. v. Gitterman, 2010 U.S. Dist. LEXIS 85040, *10 (D.N.J.) (citations omitted).

[58] *Id.* at *11.

[59] *Id.*

with the former employees upon learning they were leaving; which could have included a non-soliciting statement from the former employees, something they are entitled to do.[60]

5. Blue-Penciling

If the restrictions are overly broad or unreasonable, is the court permitted to modify the covenant and enforce it as modified?

Yes. "Depending upon the results of [the *Solari/Whitmyer*] analysis, the restrictive covenant may be disregarded or given complete or partial enforcement to the extent reasonable under the circumstances."[61] The test for this partial enforcement is not a "mechanical divisibility" but "whether or not 'partial enforcement is possible without injury to the public and without injustice to the parties.'"[62] Courts may also blue-pencil restrictive covenants made in connection with the sale of a business.[63]

Here are a few examples of blue-penciling in the New Jersey state and federal courts:

- A two-year restriction on practicing neurosurgery was upheld, but the 30-mile radius must be reduced to no more than 13 miles because of the public interest. The case was remanded to the Chancery Division to make a finding on an appropriate distance.[64]
- The court modified the restriction on a one-year post-termination prohibition with no geographic limitation on soliciting the former employer's customers. The definition of customers included not only actual customers, but also prospective customers that had only been solicited. The court deleted that prohibition on prospective customers.[65]
- In a case involving the sale of a business, the non-compete provision was blue-penciled down from three years to ten months.[66]
- Nine years was beyond a reasonable time for protecting good will in sale of business restrictive covenant; the court did not have to specify a proper amount of time as any such period had already passed; however, a five-year period would not have been an undue burden on the seller or against the public interest.[67]
- The court could enforce a restrictive covenant in a physician sale of practice case even in the absence of a specific written limitation. But the trial judge's imposition of a three-year limit on treating former patients and a 20-mile geographic non-compete was potentially too broad. The court remanded the case for a reasonableness determination.[68]

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[60] *Id.*

[61] Community Hospital Group, Inc. v. More, 183 N.J. 36, 57–58, 869 A.2d 884, 897 (2005); Richards Manufacturing Co. v. Thomas & Betts Corp 2005 U.S. Dist. LEXIS 22479, at *12 (citing cases), *rev'd on other grounds*, 342 F. App'x 754; 2009 F. App'x 16837 (3d Cir.).

[62] *Id.* (quoting Solari, 55 N.J. at 579, 264 A.2d at 57).

[63] Laidlaw, Inc., 20 F. Supp. 2d at 754.

[64] Community Hospital Group, Inc. v. More, 183 N.J. 36, 58–59, 869 A.2d 884, 897 (2005).

[65] Platinum Management, Inc. v. Dahms, 285 N.J. Super. at 298, 666 A.2d at 104o.

[66] Jiffy Lube International v. Weiss Brothers, 834 F. Supp. 683, 691–92 (D.N.J. 1993).

[67] Laidlaw, Inc., 20 F. Supp. 2d at 761–62.

[68] Graziano v. Grant, 326 N.J. Super. 328, 342–45, 741 A.2d 156, 164–65 (App. Div. 1999).

6. Defenses to enforcement

Failure of consideration. What constitutes sufficient consideration to support the enforcement of a non-compete agreement?

Unlike some states, consideration beyond continued employment is not required in New Jersey. "The existence of sufficient consideration to support a post-employment restraint may be found in either the original contract of employment or in a post-employment contract, where the supporting consideration is at least, in part, the continuation of employment."[69] "[T]he continued employment of an at-will employee upon his execution of an agreement not to compete may constitute sufficient consideration to support the validity and enforceability of the restrictive covenant under New Jersey law."[70]

An employer's insistence that the employee agree to the restrictive covenant provides consideration, and "[t]he continuation of plaintiff's employment for approximately three years after he signed the letter which acknowledges the covenant [not to solicit] also provides consideration for the restrictive covenant."[71] However, in an opinion not published in the bound volumes,[72] the Appellate Division found that continued employment, by itself, was not sufficient consideration, in circumstances where the employee was asked to sign a non-compete nine years after the start of employment; and was terminated only a few months later, for no clear failure on the employee's part and with no apparent warning about the intention to terminate.

Unclean hands/Prior material breach. If the employer fails to compensate the employee or provide benefits as agreed, or as provided under the law, will the covenant be enforced?

No. New Jersey's Supreme Court permits defenses asserting that the employee "was dealt with by the [employer-plaintiffs] so unworthily and in such inequitable manner as to disqualify them from relief."[73] That defense, however, must be raised and then proven.[74] In *Platinum*, an employer was found to have treated an employee shabbily during the course of employment, which would have made any restrictive covenant not to compete unenforceable, even though that same employee violated his duty of loyalty and was involved in tortious interference with the employer's business relations. That employee was unfairly fired after a leg injury, and then rehired as a part-time employee on a substantially reduced salary.[75]

In *Laidlaw, Inc.*,[76] the employer received a legal opinion on the likely unenforceability of a restrictive covenant. However, the employer attempted to apply and enforce it anyway. The court held that any inference of the employer's good faith is negated and it cannot seek equitable relief. The employer will be deemed to have acted in bad faith, and "application of the blue pencil rule would be inappropriate." In *Mailman, Ross, Toyes & Shapiro v. Edelson*,[77] the employer was found at trial to have acted in bad faith in forcing an employee to sign the restrictive covenant three days after starting work, on direction to sign or be fired. The covenant

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69 Hogan v. Bergen Brunswig Corp., 153 N.J. Super. 37, 43, 378 A.2d 1164, 1167 (App. Div. 1977).

70 Campbell Soup Co. v. Desatnick, 58 F. Supp. 2d 477, 492 (D.N.J. 1999).

71 Hogan v. Bergen, 153 N.J. Super. at 43, 378 A.2d at 1167.

72 Grinspec, Inc. v. Lance, 178 N.J. 251, 837 A.2d 1094 (2003).

73 Solari, 55 N.J. at 586, 264 A.2d at 61.

74 Platinum Management, Inc., 285 N.J. Super. at 314, 666 A.2d at 1047.

75 *Id.*

76 20 F. Supp. 2d at 765.

77 183 N.J. Super. 434, 445, 444 A.2d 75, 80 (Ch. Div. 1982).

may not be enforceable, but if entered in good faith then it could be enforceable. *See* the discussion above concerning consideration.

A court may consider the reason for termination in the undue hardship prong of the *Solari/Whitmyer* test.[78] If the termination is the result of the employer's breach, "or because of actions by the employer detrimental to the public interest, enforcement of the covenant may cause hardship on the employee which may fairly be characterized as 'undue' in that the employee has not, by his conduct, contributed to it."[79]

Involuntary termination of employment. If the employer fires the employee, will the covenant be enforced?

It is clear that termination by the employer does not per se obviate the effectiveness of restrictive covenants.[80] However, where an employee was unfairly fired and then rehired at a lower salary, this inequity weighed against enforcement.[81]

Other defenses

- An employer's code of ethics that made reference to a restrictive covenant did not create a restrictive covenant in itself.[82]
- An employee's unilateral effort to exclude a restrictive covenant from an employment agreement at a time of automatic renewal or notice of termination was ineffective.[83]
- The failure to enforce similar non-competes as to other former employees cannot be used to make an estoppel or waiver argument for the employer enforcing its contract rights against a different employee.[84]
- Summary judgment cannot be granted on a six-month non-compete where there is a dispute of fact over whether the new employer is actually a competitor.[85]

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[78] Gach v. Century Cookies, Inc., 1985 U.S. Dist. LEXIS 18938, at *10 (citing Karlin v. Weinberg, 77 N.J. 408, 423, 390 A.2d 1161, 1169 (1978)).

[79] *Id.* at **10–11(citing Karlin, (the court considered whether the termination was a result of age discrimination or a breach of an alleged lifetime employment agreement in whether to enforce a non-compete, even though the court ultimately found the arguments factually lacking)); *See also* Actega Kelstar, Inc. v. Musselwhite 2010 U.S. Dist. LEXIS 18801, *15 (D.N.J.) ("A breach of a material term of an agreement relieves the non-breaching party of its obligations under the agreement."); Trico Equip., Inc. v. Manor 2009 U.S. Dist. LEXIS 50524, *16 (employee had no defense where employer did not breach employment agreement where conditions imposed on employee after employee was arrested "did not materially alter the relationship between the parties'" and the employer's actions "were reasonable and accepted by [the employee].")

[80] Pierson v. Medical Health Centers, P.A 183 N.J. 65, 869 A.2d 901 (2005) (restrictive covenant of two years and 12-mile radius enforced against doctor terminated by health center); Athlete's Foot Marketing Associates, LLC, 2007 U.S. Dist. LEXIS 32995, at **5–6 (one-year non-competition agreement against a defaulting franchisee, whom the franchisor had terminated—enforceable); Gach v. Century Cookies, Inc., 1985 U.S. Dist. LEXIS 18938 (D.N.J.) (two-year post-termination non-compete that covered the entire United States against a 62-year-old cookie broker, who was terminated and offered commission work—enforceable).

[81] Platinum Management, Inc., 285 N.J. Super. at 314, 666 A.2d at 1047.

[82] Cancer Genetics, Inc. v. Hartmayer, 2008 U.S. Dist. LEXIS 8260, at **12–16.

[83] Platinum Management, Inc., 285 N.J. Super. at 301–02, 666 A.2d at 1041.

[84] Laidlaw, 20 F. Supp. 2d at 751.

[85] Restaurant Technologies, Inc. v. Allora, 2008 U.S. Dist. LEXIS 62405, at *27.

7. Assignment

Are covenants not to compete generally assignable by the employer? Is the covenant enforceable in the event the employer sells its stock to, or merges with, another entity?

It depends. One buying a business may seek to enforce a non-compete provision in an employment agreement previously reached by the seller of that business and one of its employees. The assignment of the non-compete provision in the employer-employee agreement need not be expressly made between the seller and the buyer, but it passes as an incident to the sale of the business.[86] However, while the sale of a business *in toto* may result in such an assignment, New Jersey's courts will look closely as to whether the business is in fact a continuation of the old business that had actually entered the restrictive covenant agreement before finding such an assignment.[87]

8. Interpreting the covenant

In the absence of a specific choice of law provision, to which state's law or Restatement principles do New Jersey courts look in interpreting the enforceability of an agreement not to compete?

In conducting a choice of law analysis, New Jersey's courts will look to the law of the state with the greatest interests in having its laws applied to a particular issue; an analysis done on an issue by issue basis.[88] New Jersey will not uphold contractual choice of law provisions in the presence of a violation of a fundamental New Jersey public policy, where New Jersey's interest is greater and its law would otherwise control, or where the state that has its law so chosen has no substantial relation to the parties or the transaction and its law would not otherwise apply.[89]

In addressing contractual restrictive covenants, New Jersey courts have enforced choice of law provisions applying New Jersey law where that law was selected in the contract,[90] and applying foreign law where that law was selected in the contract, New Jersey had no public interest and the major contacts were with the other state or country. [91]

The authors have not located a New Jersey case where there was a choice of law provision from a state with, *e.g.*, a prohibition on restrictive covenants contrary to New Jersey law or where the state with the most significant contacts had a prohibition on enforcing restrictive covenants. In *Actega Kelstar, Inc. v. Musselwhite*,[92] the court stated the fact that New Jersey law allowed blue penciling, whereas Georgia law did

86 J. H. Renarde, Inc. v. Sims, 312 N.J. Super. 195, 199, 711 A.2d 410, 412 (Ch. Div. 1998); A. Fink & Sons v. Goldberg 101 N.J. Eq. 644, 646–47, 139 A. 408 (Ch. 1927).

87 Ascencea, L.L.C. v. Zisook, 2011 U.S. Dist. LEXIS 36786, **17–21 (D.N.J.) (citing Woodbridge Medical Associates, P.A., v. Berkley, No. A-3159-08T1, 2010 N.J. Super. Unpub. LEXIS 1217, 2010 WL 2195760 (App. Div.)).

88 Ross v. Celtron International, Inc., 494 F. Supp. 2d 288, 295 (D.N.J. 2007).

89 North Bergen Rex Transportation v. Trailer Leasing Co., 158 N.J. 561, 568–69, 730 A.2d 843, 847–48 (1999); *See also* Actega Kelstar, Inc. v. Musselwhite, 2010 U.S. Dist. LEXIS 18801, *5 (D.N.J.) (applying Restatement (Second) of the Conflict of Laws §187 in determining whether to enforce choice of New Jersey law provision in contract containing restrictive employment covenants).

90 Laidlaw, 20 F. Supp. 2d at 751; Actega Kelstar 2010 U.S. Dist. LEXIS 18801, *6.

91 Iscar, Ltd. v. Katz, 1989 U.S. Dist. LEXIS 5337; *see also* Barre–National, Inc. v. Doshi 1988 U.S. Dist. LEXIS 3323, **7–8 (applying Maryland law).

92 2010 U.S. Dist. LEXIS 18801, *6.

not, did not go to a fundamental policy difference between the states; stating this was a matter of degree, not polar differences.

9. Anti-Raiding

Are covenants not to solicit or hire employees enforceable?

An employer can include a restrictive covenant in the form of a post-employment employee non-solicitation term. In one case, the employer included a contractual provision making clear that the employee could not solicit co-employees after termination, induce them to terminate employment, or to form a competing organization for a period of one year after termination. The court accepted the non-solicitation provision as valid, and found it likely on the facts presented during a preliminary injunction that this provision had been breached.[93]

In the duty of loyalty context, a current employee cannot improperly solicit his co-employees to leave the employer and join the disloyal employee in a competing enterprise.[94] A court will determine whether the solicitation is done with an intent to injure or, in the absence of an equal or greater right to seek the employees' services, determine whether tortious interference has occurred (a commonly related claim).[95]

In a raiding case, the subsidiary that is allegedly raided must be a party; and if only the parent brings the action, the case may be dismissed under Federal Rule of Civil Procedure 19.[96]

10. Non-disclosure and confidentiality clauses

Do New Jersey courts impose any restrictions on non-disclosure and confidentiality clauses? If so, what are those restrictions?

New Jersey courts will enforce contractual provisions on non-disclosure and confidentiality clauses.

Under New Jersey law, confidential and proprietary information is protected even in the absence of an agreement to that effect.[97] An employer can further protect itself contractually from misappropriation of its trade secrets and confidential information.[98] Information that does not rise to the level of a trade secret also can be protected. In determining whether a protectable interest exists, the courts will look to the relationship of the parties at the time the information is disclosed and the intended use of that information to answer questions about its subsequent misuse. Such information may be deemed confidential and proprietary in the context of that business relationship, and thus protectable.[99]

In reversing the trial court, the Third Circuit stated that the trial court should "consider whether the allegedly misappropriated information was provided to [the employee] by [the employer] in the course

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93 Scholastic Funding Group, LLC v. Kimble, 2007 U.S. Dist. LEXIS 30333, at **6, 16–17; *See also* Esquire Deposition Servs., LLC v. Boutot, 2009 U.S. Dist. LEXIS 52207, **3–4, 20–21 (D.N.J.) (court found enforceable non-solicitation agreement that kept former employee "from directly or indirectly contacting [its] clients, customers or business contacts for a period of twelve (12) months following the termination of his employment….").

94 Wear-Ever Aluminum, Inc. v. Townecraft Industries, Inc., 75 N.J. Super. 135, 182 A.2d 387 (Ch. Div. 1962).

95 Avtec Industries v. Sony Corp. of America, 205 N.J. Super. 189, 193, 500 A.2d 712, 715 (App. Div. 1985).

96 Tullett Prebon, PLC v. BGC Partners, Inc., 427 F. App'x 236, 2011 F. App'x 9823 (3d Cir.).

97 Lamorte Burns & Co. v. Walters, 167 N.J. 285, 298, 770 A.2d 1158, 1166 (2001).

98 Ingersoll-Rand, 110 N.J. at 635–36, 542 A.2d at 892–93.

99 Lamorte Burns & Co. v. Walters, 167 N.J. 285, 299–301, 770 A.2d 1158, 1166–67 (2001).

of his employment for the sole purpose of furthering [the employer's] business interests."[100] It observed that "[the employee] had a common law obligation to maintain the secrecy of his employer's proprietary information."[101] In determining whether information was provided to the employee solely to further the employer's interest, the Third Circuit instructed the trial court to "consider the following factors: (1) whether the information was generally available to the public; (2) whether [the employee] would have been aware of the information if not for his employment with [the employer]; (3) whether the information gave [the employee]—and, by extension, [the subsequent employer]—a competitive advantage vis-a-vis [the first employer]; and (4) whether [the employee] knew that [the original employer] had an interest in protecting the information to preserve its own competitive advantage."[102] The court stated, however, that: "This inquiry does not entail a 'rigorous examination of the information sought to be protected,' as in trade secret law, but rather a focus on the relationship between employer and employee, the expectations of the parties, and the intended use of the information. [103] "Moreover, it appears to us that, unlike in trade secret law, these four factors are not to be treated as essential elements of a cause of action for the misappropriation of confidential information."[104]

For purposes of an injunction, where the former employee has already turned over the confidential information to the new employer, at least as to that employee, there may be no injunctive relief possible because "if the employee has already disclosed confidential information, the harm may be irreparable, but it is not immediate."[105] An employer also may have protectable interests in "highly specialized, current information not generally known in the industry, created and stimulated by the research environment furnished by the employer, to which the employee has been 'exposed' and 'enriched' solely due to his employment."[106] Specific information that the employer provided its former employees "in the course of employment, and for the sole purpose of servicing [the employer's] customers" is protected.[107] This might include the names, addresses, telephone numbers, and fax numbers of the employer's clients, as well as details from client files, taken by the former employees for the purpose of soliciting those clients.[108] Customer lists for service businesses are protectable.[109]

Confidential files downloaded to thumb drive and given to competitor that included, *e.g.*, former employer's new client presentation module violated contractual confidentiality provision.[110]

An employer's pricing policy and sales strategy with its customers or potential customers may be protectable interests, including, *e.g.*, customer buying habits, the employer's mark-up structure and merchandising

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[100] Thomas & Betts Corp. v. Richards Manufacturing Co., 342 F. App'x 754; 2009 U.S. App. LEXIS 16837, * 12 (3d Cir.) (citing Lamorte Burns, 167 N.J. at 301).

[101] *Id*.

[102] *Id*. at **12–13.

[103] *Id*. (citations omitted).

[104] *Id*. at *13.

[105] Trico Equipment, Inc. v. Manor, 2009 U.S. Dist. LEXIS 50524, *23.

[106] Richards Manufacturing Co. v. Thomas & Betts Corp, 2005 U.S. Dist. LEXIS 22479, at **14–15 (quoting Ingersoll-Rand, 110 N.J. at 638, 542 A.2d at 894).

[107] Lamorte Burns & Co., 167 N.J. at 301, 770 A.2d at 1167.

[108] *Id*. at 298, 770 A.2d at 1166.

[109] *Id*.

[110] Esquire Deposition Servs., LLC v. Boutot, 2009 U.S. Dist. LEXIS 52207, **23–25.

plans, customer packaging requirements, sales projections, and product strategies.[111] An employer's "manner of production, its pricing formulae, its cost information, and information concerning its customer-specific needs" may also be protected.[112] Manuals describing basic salesmanship, blank bid worksheet forms with no confidentiality restrictions, and even generalized knowledge of the former employer's inner working do not create protectable interests.[113]

A court will blue-pencil overbroad confidentiality agreements, such that only information in which there is a legitimate secrecy interest will be protected.[114]

In the invention holdover context, following the law of restrictive non-competition covenants, an appellate court upheld blue-penciling, and stated that blue-penciling is not contract reformation; rather, it is partial contract enforcement. In that case, the blue-penciling consisted of the trial court's replacing the word "information" with the phrase "trade secrets and confidential information."[115]

Information that was once confidential may become stale and lose protection.[116]

Where some employees had non-competes in connection with stock options, and other employees without non-competes had access to the same purportedly confidential information, the court weighed this fact in not enforcing the stock option non-competes, deeming them merely anti-competitive.[117]

The court need not accept as self-proving a contractual statement that the employee received confidential information or that the employer suffered irreparable harm.[118]

11. Duty of loyalty

Do rank-and-file employees owe a common law or statutory duty of loyalty to their employers?

Yes. New Jersey law recognizes that an employee owes a duty of loyalty to an employer, prohibiting the employee from taking affirmative steps to injure the employer's business.[119] This duty requires that employees "refrain from disclosing or otherwise using an employer's confidential information against it." *Id.* During employment, the employee must not act contrary to the employer's interests, and has a duty not to compete with the employer.[120] Neglecting duties at a critical time may be a duty of loyalty issue as well.[121]

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[111] Platinum Management, Inc. v. Dahms, 285 N.J. Super. at 294–5, 666 A.2d at 1038.

[112] Mansol Industries, Inc. v. Singh, 1996 U.S. Dist. LEXIS 22823 (D.N.J.).

[113] Laidlaw, Inc., 20 F. Supp. 2d at 759–60.

[114] Richards Manufacturing Co., 2005 U.S. Dist. LEXIS 22479, at **13–14.

[115] Saccomanno v. Honeywell International, Inc., 2010 N.J. Super. Unpub. LEXIS 740, **9–14 (App. Div.).

[116] Laidlaw, Inc., 20 F. Supp. 2d at 759.

[117] Laidlaw, Inc., 20 F. Supp. 2d at 763.

[118] Laidlaw, Inc., 20 F. Supp. 2d at 758, 766; *but see*, Jackson Hewitt, Inc., 2008 U.S. Dist. LEXIS 4640 at *22 (where the court did consider the express language in the agreement that the restrictive covenant was "reasonable and necessary to protect [the franchisor] and its franchise system and the restrictions would not impose any undue hardship on [the former franchisee]").

[119] Palm Bay Imports, Inc. v. Miron, 55 F. App'x 52, 2002 U.S. App. LEXIS 27847, at *13 (3d Cir.); Lamorte Burns & Co. v. Walters, 167 N.J. at 305, 770 A.2d at 1169–70.

[120] P.C. of Yonkers, Inc. v. Celebrations! The Party and Seasonal Superstore, LLC., 2007 U.S. Dist. LEXIS 15216, at **38–39.

[121] Platinum Management, Inc., 285 N.J. Super. at 282, 666 A.2d at 1032.

Officers, directors and high level or key employees have to abide by a stricter standard of loyalty.[122] Defecting employee who tries to "sell" co-employees on leaving with him for competitor violates the duty, as he does in soliciting business away from current employer to future employer.[123]

If there is no post-termination covenant not to compete, and absent any breach of trust, an employee can anticipate the end of employment and doing future work for a competitor, or even setting up a competing business in competition with the former employer.[124] But the employee cannot solicit his employer's customers for his own benefit prior to termination; nor can the employee do similar acts in direct competition with the employer, because there is an undivided duty of loyalty during employment.[125] The common law will not allow the employee to prepare for future competition by purloining the former employer's confidential information with the intention of using it to compete against the former employer.[126]

The presence of a contractual non-compete is only one factor in a duty of loyalty analysis.[127] The employee's common law duties extend to non-disclosure of the former employer's trade secrets and confidential information even after termination of employment.[128]

Claims can be pursued for breach of the duty of loyalty occurring during employment. Such claims depend on the circumstances of each case and are adjudicated under rules of reason and fairness.[129] New Jersey courts look at various factors such as: whether there were contractual obligations and whether the employer knew of or assented to the employee's conduct. The court will also consider the employee's status and relation to the employer, *e.g.*, a corporate officer is going to have a higher duty than a laborer; and the nature and effect of the employee's conduct, *i.e.*, the level of direct competition.[130]

Employers can seek equitable relief, damages, or obtain forfeiture of compensation paid to the disloyal employee.[131]

12. Conclusion and Advice

There is no question that New Jersey courts will enforce restrictive covenants in connection with both employment contracts and the sale of a business—if those restrictions are reasonable. While there is more leeway in the scope of such restrictions in the sale of a business, even there the buyer cannot overreach and protect interests beyond their reasonable physical scope and life expectancy. In fact, one way to look at

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[122] *Id.* at 294–95; Cameco, Inc. v. Gedicke, 157 N.J. 504, 521, 724 A.2d 783, 791 (1999); Marsellis-Warner Corp. v. Rabens, 51 F. Supp. 2d 508, 524–25 (D.N.J. 1999).

[123] Baseline Services Inc. v. Kutz, 2011 N.J. Super. Unpub. LEXIS 2309, **7–9 (App. Div.).

[124] P.C. of Yonkers, Inc., 2007 U.S. Dist. LEXIS 15216, at **38–39 (citing Auxton Computer Enterprises, Inc. v. Parker, 174 N.J. Super. 418, 423–24, 416 A.2d 952 (App. Div. 1980)).

[125] *Id.*

[126] *Id.* at **40–41 (citing Lamorte Burns & Co., 167 N.J. at 304–05, 770 A.2d at 1169–1170).

[127] Lamorte Burns & Co., Inc., 167 N.J. at 303, 770 A.2d at 1168.

[128] P.C. of Yonkers, Inc., 2007 U.S. Dist. LEXIS 15216, at *40.

[129] Cameco v. Gedicke, 157 N.J. at 516, 724 A.2d at 789.

[130] 157 N.J. at 520–521, 724 A.2d at 791.

[131] *Id.* at 522, 724 A.2d at 791–792. *See also* Trans American Trucking Service, Inc. v. Ruane, 273 N.J. Super. 130, 641 A2d 274 (App. Div. 1994) (employee enjoined from having any business contact with former employer's key customers for 19 months after termination).

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whether a restrictive covenant will be enforceable generally is whether one side or the other is overreaching in attempting to impose, or avoid, restrictions.

Litigators deal with the results of the parties' negotiations, or lack thereof, and draftsmanship; but in this day and age, employers, employees, buyers, and sellers should be anticipating the likely fact that such terms will be in their contracts; and these parties should be looking to the case law in how to negotiate and draft those terms. A party should get good advice from its New Jersey lawyer—and, if wise, that means including a New Jersey litigator in the process—on how to draft a non-compete with reasonable terms that will stand up to scrutiny on the day of a preliminary injunction hearing. If that client wants to "take a shot" at broader restrictions, then that client should understand that the New Jersey judge will, at a minimum, blue-pencil the restriction down to reasonable terms. However, that judge could also find that the employer acted in bad faith and will refuse to enforce the restrictive covenant as a matter of equity.

What is overreaching? The New Jersey judge, for example, must look at the reasonable geographic scope of a non-compete. At first blush, restrictions covering the entire United States, or even the world, may seem *prima facie* evidence of overreaching. However, New Jersey's judges will look at the particular facts and circumstances of each relationship, and if such geographic scope is a reasonable fit for the facts, it could be enforced. Any New Jersey lawyer advising a client to pursue or defend a restrictive covenant simply cannot rely on "first blushes" or what *seems* to be outrageous or eminently reasonable, but is obligated to dig into the details of the relationship at issue to adduce the hard facts. It will be those details that will or will not convince the judge. Moreover, even before getting to the judge, the lawyer needs to understand and gain knowledge concerning the facts of the parties' relationship to give the client an honest assessment of what is likely to be the outcome if the matter is litigated—in addition to being able to put on the evidence needed to make the case if it goes that far.

The stakes may be very high for both sides. If the lawyer's investigation of the law and facts shows there is a genuine risk that a two-year covenant will be enforced, then rather than taking a long shot at preventing enforcement, it may be wisest for the employee to negotiate a settlement for one year. Similarly, if it is unlikely a judge will enforce a geographic limitation covering the entire mid-Atlantic region, an employer may want to negotiate the restriction down to one relevant state, instead of risking an order that might limit the restriction to a five-mile radius.

Finally, although there is abundant case law discussing legal principles, the hand holding that blue pencil will be governed by the unique facts of each case. Thus, the perceptions and evaluations of individual judges are going to be the biggest factor determining the outcome of these cases. In New Jersey's Superior Court, that means the lawyers must gain knowledge about the Chancery Division Judge in the county where your case will be heard, or to do the same with your judge once the case is assigned in federal court. This may prove to be the biggest factor in determining how to litigate or whether to settle—and on what terms.

This takes us back to the essential point for lawyers litigating restrictive covenant cases in New Jersey: Get the facts! And when you think you have the facts down, go back and look for more.