Fox Rothschild LLP
ATTORNEYS AT LAW

Fox Rothschild Podcast

Featuring Litigation Partner John Gotaskie in Pittsburgh

We are talking today with John Gotaskie on Fox Rothschild Podcast about whether your organization's restrictive covenants are still enforceable in Pennsylvania. John is a partner and litigator with Fox Rothschild in Pittsburgh. He represents clients in diverse legal matters, including franchising and complex commercial litigation as well as creditor's rights and social media matters. John, good morning.

John Gotaskie: Good morning. Thank you.

Question: *John, you recently wrote a post for Fox Rothschild's Franchise Law Update Blog probing into the question of whether an organization's restrictive covenants are still enforceable in the state of Pennsylvania in light of a recent Superior Court decision.*

John Gotaskie: Yes. I did. A recent published opinion from the Pennsylvania Superior Court – an intermediate state appellate court – has called into question the enforceability of some restrictive covenants in Pennsylvania. In the case, called *David M. Socko v. Mid-Atlantic Systems*, the court considered whether the Uniform Written Obligations Act, as adopted in Pennsylvania, permitted the enforcement of a restrictive covenant entered into after the beginning of employment but without the employer providing any additional consideration. The court decided in that instance, such a restrictive covenant cannot be enforced.

Question: *John, what can you tell our listeners about the background facts in the case?*

John Gotaskie: The facts of the case were pretty straightforward. Socko was a salesman, and having once left Mid-Atlantic, he signed onto a second period of employment with the company in 2009. At that time, Socko signed an employment agreement with a two-year covenant not to compete. Later, in 2010, while he was still employed by Mid-Atlantic but without Mid-Atlantic giving him any new consideration, Socko signed another employment agreement, this one also containing a two-year covenant not to compete. The terms of this new covenant not to compete would only begin to run upon termination and, importantly from Mid-Atlantic's perspective, included an expanded territorial restriction that barred Socko from working in any jurisdiction where Mid-Atlantic does business.

Question: *So what happened next?*

John Gotaskie: Well, you can probably guess. Socko left Mid-Atlantic to go to work for a competitor. Mid-Atlantic then sent a letter to that competitor, enclosing a copy of the non-competition agreement and threatening litigation. Socko was then terminated by the new

Copyright © 2014. Fox Rothschild LLP. All Rights Reserved.
All content of this podcast is the property and copyright of Fox Rothschild LLP and may not be reproduced in any format without prior express permission. Contact marketing@foxrothschild.com for more information or to seek permission to reproduce content.

employer. Now Socko didn't take this sitting down. He initiated a lawsuit against Mid-Atlantic, seeking a declaration from the court that the covenant not to compete – the 2010 one – was unenforceable because it was not supported by adequate consideration. Now Mid-Atlantic admitted that no consideration had been given to Socko in exchange for the 2010 non-compete. Instead, Mid-Atlantic argued that, because the Uniform Written Obligations Act prevents the avoidance of any written agreement for lack of consideration, the 2010 covenant had to be enforced. The trial court disagreed, granted summary judgment for Socko, and Mid-Atlantic appealed.

Question: *And so what happened with the appeal?*

John Gotaskie: On appeal, the Superior Court engaged in a really broad review of the history of non-competition agreements in Pennsylvania, as well as the decisions of federal district courts from Pennsylvania that had considered the effect of the Uniform Written Obligations Act when they were applying Pennsylvania law. In that sweeping review, the Superior Court noted that the Pennsylvania Supreme Court has long disfavored covenants not to compete because they are restraints on trade and may prevent former employees from earning a living.

Question: *So John, what does that mean from a practical standpoint?*

Answer: That's a good question. What it means is that a covenant not to compete must be entered into when beginning initial employment (which is often referred to as "ancillary to the taking of employment"). Or, it must be accompanied by new consideration, such as a corresponding benefit to the employee (for example, a bonus specifically linked to the non-compete and not related to anything else) or a beneficial change in employment status (for example, a promotion to a new position). Moreover, the Superior Court noted that the Supreme Court had regularly examined the quality of the consideration given in exchange for signing a non-compete agreement, rejecting recitations of value like "good and valuable" consideration, which are readily and generally accepted in other contractual situations.

Question: *John, what did the Superior Court find when examining the Socko scenario?*

John Gotaskie: The Superior Court looked at the record and sought to determine if Socko had actually received valuable consideration in exchange for the 2010 covenant not to compete. And it decided that it wasn't there. The language added to a contract to the effect that the parties intended to be legally bound – even if perfectly adequate for other types of contracts – would not suffice for contracts such as this one that restrain the ability of employees to earn a living. The court in fact analogized to contracts under seal, which Pennsylvania courts have long held to provide insufficient consideration to support a restrictive covenant. The court found that the Uniform Written Obligations Act had precisely the same effect as a contract under seal, "namely to import consideration into a contract and thus eliminate the need for proof of the existence of consideration."

Copyright © 2014. Fox Rothschild LLP. All Rights Reserved.
All content of this podcast is the property and copyright of Fox Rothschild LLP and may not be reproduced in any format without prior express permission. Contact marketing@foxrothschild.com for more information or to seek permission to reproduce content.

Question: *So John, what are the conclusions you are drawing from the outcome of this case?*

John Gotaskie: This decision provides a good reason for you to review any covenants not to compete with employees that are governed by Pennsylvania law. If those contracts were not entered into at the beginning of an employment relationship or supported with either a corresponding benefit like a special bonus or a positive change in job status, the Uniform Written Obligations Act is not going to save you. It's not going to supply a reason for the enforcement of restrictive covenants in Pennsylvania. Even more, while it does not seem to have happened in this case, recall that Mid-Atlantic did send a letter to the new employer threatening litigation. That letter in fact led to Socko's termination. The failure of the non-compete for lack of consideration likely means that a former employer has opened itself up to lawsuits from both the former employee and the new employer for tortious interference with contractual relations. And if the employee is a high-performing salesperson or other type of high-performing employee, success in such a suit could lead to significant damages for the former employer.

Well thank you, John. Listeners, to confidentially discuss whether your organization's restrictive covenants are still enforceable in Pennsylvania, please contact John at 412-394-5528 or at jgotaskie – that's J-G-O-T-A-S-K-I-E – at foxrothschild.com.

Fox Rothschild LLP is a full service law firm built to serve business leaders, backed by nearly 600 lawyers coast to coast. Our clients come to us because we understand their issues, their priorities and the way they think. We help clients manage risk, and make better decisions by offering practical advice. Visit us on the web at www.foxrothschild.com.

# # # #

Copyright © 2014. Fox Rothschild LLP. All Rights Reserved.
All content of this podcast is the property and copyright of Fox Rothschild LLP and may not be reproduced in any format without prior express permission. Contact marketing@foxrothschild.com for more information or to seek permission to reproduce content.