



COMMERCIAL DIVISION UPDATE

Expert Analysis

Judicial Flexibility in Enforcing Restrictive Covenants in Employment

New York courts have long exercised caution when asked to enforce provisions of employment agreements that purport to restrain an employee from competing with his or her former employer.¹ The New York Court of Appeals explained that the “judicial disfavor of these covenants is provoked by ‘powerful considerations of public policy which militate against sanctioning the loss of a man’s livelihood.’”² Accordingly, a restrictive covenant of this type will be enforced only “to the extent that it is reasonable in time and area, necessary to protect the employer’s legitimate interests, not harmful to the general public and not unreasonably burdensome to the employee.”³

Two recent opinions by justices of New York’s Commercial Division on employers’ motions for preliminary injunctions to enforce restrictive covenants against former sales employees demonstrate both the close scrutiny that such covenants receive and the willingness of the courts, in appropriate circumstances, to limit their scope to protect employees. These decisions also illustrate the differing frameworks that courts may apply when analyzing whether a restrictive covenant serves a legitimate employer interest.

‘IKON Office Solutions’ Case

In *IKON Office Solutions Inc. v. Usherwood Office Tech. Inc.*,⁴ plaintiff IKON, a company engaged in the business of selling, leasing



By
**George
Bundy Smith**



And
**Thomas J.
Hall**

and servicing office equipment, sought a preliminary injunction against seven former employees with titles ranging from “account executive” to “copier technician” who left IKON’s employment in early November 2008 to join a competitor. Each of them had signed employment agreements prohibiting them from, inter alia, soliciting any IKON

Two opinions on employers’ motions for preliminary injunctions demonstrate the close scrutiny that restrictive covenants receive.

customer or prospective customer to which that employee had been assigned, most for a period of 18 months following termination of employment. IKON alleged that a preliminary injunction was necessary to prevent these defendants from violating their employment agreements by “us[ing] IKON’s trade secrets, confidential business information, customer relationships and goodwill to divert current IKON customers to [the defendants’ new employer].”⁵

Justice Richard M. Platkin of the Albany County Commercial Division adjudicated IKON’s motion using the traditional test of whether (1) IKON was likely to succeed on

the merits, (2) irreparable harm would occur in the absence of an injunction, and (3) the balance of equities favored an injunction. The court focused its analysis on IKON’s likelihood of success, analyzing whether the restrictive covenants at issue served (1) a legitimate interest of IKON and, if so, whether (2) the scope of such covenants was no greater than necessary to protect that legitimate interest, and was reasonable in time and geographic area.

Legitimate Employer Interests. Justice Platkin explained that the New York Court of Appeals recognizes three legitimate interests that may justify enforcement of a restrictive covenant in an employment agreement, specifically: (1) protection against misappropriation of trade secrets or confidential information; (2) protection from competition by a former employee whose services are “unique or extraordinary”; and (3) protection of “customer relationships and goodwill.” Although IKON urged that the restrictive covenants at issue should be analyzed and enforced on the basis of all three of these potential legitimate interests, the court ultimately concluded that only the third type of legitimate interest—protection of customer relationships and goodwill—had been demonstrated.

Unique or Extraordinary Services. IKON argued that the defendants’ “relationships with current IKON customers and their access to confidential customer information” rendered them unique, citing the Second Circuit’s decision in *Ticor Title Ins. Co. v. Cohen*.⁶ In *Ticor*, the Second Circuit upheld an injunction prohibiting a title insurance salesman from working for a competitor because his personal relationships with the limited number of clients in the market rendered him unique. The *Ticor* court explained:

GEORGE BUNDY SMITH, former Associate Judge on the New York Court of Appeals, and THOMAS J. HALL are litigation partners with Chadbourne & Parke. ROBERT KIRBY, a litigation associate, assisted with the preparation of this article.

the focus today is less on... testing whether such person is extraordinary in the sense, for example, of Beethoven as a composer, Einstein as a physicist, or Michelangelo as an artist, where one can fairly say that nature made them and then broke the mold. Instead, now the inquiry is more focused on the employee's relationship to the employer's business to ascertain whether his or her services and value to that operation may be said to be unique, special or extraordinary....⁷

Perhaps indicating an unstated skepticism toward *Ticor's* application of the uniqueness framework to sales employees, Justice Platkin declined to apply that framework to the facts at issue, deciding that IKON's asserted interests were "more appropriately analyzed under the rubric of protecting trade secrets/confidential business information and preventing against the exploitation of customer relationships and goodwill."⁸

Trade Secrets and Confidential Customer Information. IKON also argued that it had a legitimate interest in protecting from disclosure to competitors the identity of its customers and the details of their equipment needs, preferences and contracts with IKON. The court was unpersuaded by the defendants' argument that this information was not secret because it could be duplicated using business directories and similar industry publications. To the contrary, such sources would "fail to provide insight into the specific purchasing needs, buying practices and preferences of the customer accounts that IKON seeks to protect."⁹ However, the court found "some potential merit" in the defendants' argument that the manufacturers of office equipment sold and serviced by IKON would in many cases make such information freely available to all of its vendors, including IKON's competitors. As such, the court held that IKON failed to demonstrate "a sufficiently strong likelihood of success in establishing that the information it seeks to protect qualifies as a trade secret."¹⁰

Customer Relationships and Goodwill. The court did, nevertheless, find that IKON had established a likelihood of success on the merits arising from IKON's interest in protecting its customer relationships and goodwill. The court explained that a restrictive covenant is enforceable to "prevent the competitive use of client relationships that the employer assisted the employee in developing," though

not to prevent the employee from soliciting new clients with whom the employee never developed a relationship during the employment or "personal clients" recruited through the employee's independent efforts.¹¹ With respect to the five defendants with the titles of account manager or account representative, the court reasoned that:

[i]t is apparent that the customer relationships and goodwill developed at IKON's expense will play an important role in the customer's decision-making process. IKON's customers of Canon brand equipment who are inclined to remain with a familiar and/or preferred manufacturer may well be apprehensive about turning to a new and untested vendor for their critical service and support needs. Certainly, the assurances and presence of their long-time IKON account representatives, who carry with them the goodwill cultivated over many years at IKON's expense, may well prove decisive in this calculus.¹²

The court found the same reasoning did not support an injunction against the defendant

The recent decisions in 'IKON Office Solutions' and 'Evolution Markets' show that even in arguably similar factual circumstances, the courts may apply differing analytical frameworks to the question of whether restrictive covenants further a legitimate employer interest.

who was a copier technician who serviced hundreds of accounts while employed by IKON. The court was unconvinced that this defendant's duties "fostered the type of customer relationships and goodwill that would allow him to compete *unfairly* against IKON."¹³

Scope of the Restrictive Covenants. The court held that the 18-month duration of the restrictive covenants and their geographic scope were "within prevailing notions of reasonableness"¹⁴ but found IKON had failed to offer sufficient proof to demonstrate that its "legitimate employer interest" in protecting customer relationships and goodwill extended beyond the actual customers serviced by the defendants while at IKON to prospective IKON customers.

The court left open the possibility that "IKON may ultimately be able to demonstrate that it has invested resources, time and effort in developing goodwill and relationships with prospective customers that were assigned to the defendants."¹⁵ Thus, the court issued a preliminary injunction that enforced the restrictive covenants only in part, with respect to actual—not prospective—customers serviced by the defendants during their employment by IKON.

EvoMarkets Case

In *Evolution Markets Inc. v. Penny*,¹⁶ plaintiff EvoMarkets, a company engaged in the business of brokering transactions in energy commodities such as natural gas, coal and uranium, sought a preliminary injunction against defendant Alexandra Penny, a former broker assigned to EvoMarkets' Nuclear Fuel Desk who left employment with EvoMarkets in January 2009 to join one of EvoMarkets' competitors. EvoMarkets sought an injunction enforcing the employment agreement signed by Ms. Penny that, inter alia, prohibited her from soliciting business for nine months from any client that Ms. Penny was aware of during the six months prior to her last day at EvoMarkets. Pursuant to that agreement, Ms. Penny acknowledged that the identities and contact information of EvoMarkets' clients was a trade secret.

In deciding EvoMarkets' motion for injunctive relief, Justice Alan D. Scheinkman of the Westchester County Commercial Division cited standards for the granting of preliminary injunctions and for the enforcement of restrictive covenants that were substantially the same as the standards enunciated by the *IKON Office Solutions* court. Like the *IKON Office Solutions* court, Justice Scheinkman found that the restrictive covenant at issue served a legitimate interest and that—with appropriate limitations on its scope imposed by the court—the plaintiff employer had demonstrated entitlement to a preliminary injunction enforcing that covenant. However, Justice Scheinkman relied on the trade secrets framework to find the necessary legitimate interest, rather than the "customer relationships and goodwill" framework relied on by the court in *IKON Office Solutions*.

Legitimate Employer Interest. EvoMarkets claimed that its Nuclear Fuel Contact list, which contained clients' names, contact information,

historical buying and selling activities, objectives, and position in the marketplace, constituted a trade secret, the protection of which was a legitimate interest justifying enforcement of the restrictive covenant in Ms. Penny's employment agreement. As in *IKON Office Solutions*, the court here rejected Ms. Penny's argument that the list was not a trade secret because some of the information on the list could purportedly be obtained from public sources. The court explained that:

given the highly competitive nature of the uranium brokerage market (with only 30-40 customers) and the nature of the information contained on the Nuclear Fuel Contact List, some of which Penny does not dispute is not obtainable from public sources such as client preferences and the like, the Court agrees that the Nuclear Fuel Contact List is properly protectable as a trade secret and Penny may be enjoined from soliciting those clients during the nine month non-solicitation period.¹⁷

Unlike the employee defendants in *IKON Office Solutions*, Ms. Penny did not provide evidence that there were other, nonconfidential sources from which her former employer's competitors could obtain the information on the Nuclear Fuel Contact list.

Although Justice Scheinkman did not appear to make any findings as to the uniqueness of Ms. Penny's services or the possibility that she developed exploitable customer relationships and goodwill through her employ with EvoMarkets, the court did suggest that a legitimate employer interest could perhaps have been found under these alternative frameworks.

First, the court cited *Ticor* for the proposition that the uniqueness inquiry now focuses on the employee's relationship to the employer's business, observing that:

the fact that Penny may be a recent college graduate who is relatively new to the EvoMarkets' business and less important in the overall scheme of things than [her former supervisor] is less important than the relationship that Penny had to EvoMarkets' business—being the most senior and experienced person on the Nuclear Fuel Desk and having access to important, sensitive business information, which would be valuable to a competitor.¹⁸

The court did not, however, appear to base its holding on the unique nature of Ms. Penny's services, or to state whether it was inclined to follow *Ticor*.

Second, the court's opinion contained no analysis of whether the protection of EvoMarkets' "customer relationships and goodwill" would constitute a legitimate interest, despite EvoMarkets' claim that "Penny was the face of the nuclear fuel desk" and that it would take several months for a new hire to establish a similar bond with EvoMarkets' clients. But the court did quote approvingly from a decision of the Southern District of New York when finding that in the absence of injunctive relief EvoMarkets would suffer irreparable harm:

The customers have developed a strong relationship with [defendant employee] over the year[] and ten months he spent [working for plaintiff employer]. If [defendant] is allowed to...solicit these customers, these customers are likely to follow him because of their unique relationship....[Plaintiff] would be irreparably harmed if it did not receive the benefit of its bargain and customers left [plaintiff] to follow [defendant] within the initial 120 days following [defendant's] termination.¹⁹

Scope of the Restrictive Covenants. The court found the temporal and geographic scope of the restrictive covenants to be reasonable, even though the covenants did not contain a geographic restriction. The court reasoned that "the lack of a geographic restriction is necessary given that Plaintiff's customers are from all over the world and the brokerage business is largely conducted over the telephone."²⁰

Unlike in *IKON Office Solutions*, here Ms. Penny did not object that her employer's request for a preliminary injunction was overbroad because it prohibited her from soliciting potential as well as actual clients of EvoMarkets. Nonetheless, the court raised such concern sua sponte, finding that "justice and fairness require some limitations" on the scope of the injunction. "While EvoMarkets is entitled to protection against Penny's solicitation of any client of EvoMarkets', it is not entitled to

protection against her solicitation of persons or entities who were not actually doing any business with EvoMarkets and were merely potential sources of business."²¹

Conclusion

The recent decisions in *IKON Office Solutions* and *Evolution Markets* show that even in arguably similar factual circumstances, the courts may apply differing analytical frameworks to the question of whether restrictive covenants further a legitimate employer interest. These decisions are also a reminder that even where a court finds such an interest, it may step in to narrow the scope of the covenants when it deems necessary.

.....●●.....

1. See, e.g., *Purchasing Assocs. Inc. v. Weitz*, 13 N.Y.2d 267, 272, 196 N.E.2d 245, 247, 246 N.Y.S.2d 600, 604 (1963) ("[T]he courts have generally displayed a much stricter attitude with respect to covenants [by an employee that he will not compete with his employer when he quits his job].").

2. *Reed, Roberts Assocs. Inc. v. Strauman*, 40 N.Y.2d 303, 307, 353 N.E.2d 590, 593, 386 N.Y.S.2d 677, 679-80 (1976) (quoting *Purchasing Assocs. Inc.*, 13 N.Y.2d at 272, 196 N.E.2d at 247, 246 N.Y.S.2d at 604).

3. *Reed, Roberts Assocs. Inc.*, 40 N.Y.2d at 307, 353 N.E.2d at 593, 386 N.Y.S.2d at 679.

4. *IKON Office Solutions Inc. v. Usherwood Office Tech. Inc.*, 21 Misc.3d 1144(A), 2008 N.Y. Misc. LEXIS 7059, 2008 WL 5206291 (Sup. Ct. Albany Co. Dec. 12, 2008) (Platkin, J.).

5. *IKON Office Solutions Inc.*, 2008 N.Y. Misc. LEXIS 7059 at *4.

6. *Id.* at *27 (citing *Ticor Title Ins. Co. v. Cohen*, 173 F.3d 63 (2d Cir. 1999)).

7. *Ticor Title Ins. Co.*, 173 F.3d at 65.

8. *IKON Office Solutions Inc.*, 2008 N.Y. Misc. LEXIS 7059 at *27-28.

9. *Id.* at *12.

10. *Id.* at *28.

11. *Id.* at *32-33.

12. *Id.* at *34-35.

13. *Id.* at *36 (emphasis in original).

14. *Id.* at *25-26.

15. *Id.* at *37.

16. *Evolution Markets Inc. v. Penny*, 23 Misc. 3d 1131(A); 2009 N.Y. Misc. LEXIS 1276, 2009 WL 1470451 (Sup. Ct. Westchester Co. May 20, 2009) (Scheinkman, J.).

17. *Evolution Markets Inc.*, 2009 N.Y. Misc. LEXIS 1276 at *43-44.

18. *Id.* at *39-40.

19. *Id.* at *46 (quoting *Natsource LLC v. Paribello*, 151 F.Supp.2d 465, 469 (S.D.N.Y. 2001)).

20. *Evolution Markets Inc.*, 2009 N.Y. Misc. LEXIS 1276 at *44.

21. *Id.* at *60.

Reprinted with permission from the October 29, 2009 edition of the NEW YORK LAW JOURNAL © 2009 ALM Media Properties, LLC. All rights reserved. Further duplication without permission is prohibited. For information, contact 877-257-3382 or reprints@alm.com. # 070-08-09-07

CHADBOURNE
& PARKE LLP

www.chadbourne.com