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Pennsylvania's Highest Court Rules Continuing Employment Insufficient Consideration for Non-Compete

By Robert B. Milligan and Paul E. Freehling

Do you have workers in Pennsylvania? If so, do you ask them to sign non-competes after they have already been employed with your company for some appreciable time? If you do, you may be obligated to provide them with sufficient consideration in exchange for their signature. Otherwise, your non-compete may be unenforceable.

In a landmark ruling of first impression, the Pennsylvania Supreme Court recently held in *Socko v. Mid-Atlantic Systems of CPA, Inc.*, Case No. 3-40-2015 (Nov. 18, 2015) that an employee's non-competition covenant, *which included the employee's pledge not to challenge the covenant for inadequate consideration*, is void unless it is accompanied by a favorable change in job status or some other significant benefit to the employee. The Court reached this result despite the applicability of a Pennsylvania statute – the so-called Uniform Written Obligations Act ("UWOA") – which provides that agreements in writing that contain the parties' express promise to be "legally bound" may not be contested on the ground of a lack of consideration.

Arguments in the Supreme Court

The employer stressed that, as a matter of law, the UWOA barred the employee from challenging the validity of the non-compete for inadequate consideration. Asserting that the statute is unambiguous and contains no exceptions, the employer insisted that the lower courts' rulings in the employee's favor effectively constituted amending the UWOA, thereby legislating under the guise of statutory interpretation. The employee countered that the employer's contentions ignored the public policy inherent in decisions invalidating restrictive covenants executed after the commencement of employment without substantial benefit to the employee.

The Supreme Court's Majority Decision

The Court said that an exchange of consideration is crucial to the enforceability of all contracts. Moreover, the analysis of non-compete covenants in the employer-employee context is unique and requires rigorous scrutiny. Therefore, since the UWOA does not provide expressly that it applies to employment-related covenants, it cannot reasonably be interpreted as abrogating the need for benefits to a continuing employee executing a non-compete.

Takeaways

First, a written non-compete signed at or about the time a new employee is hired is not invalidated by this decision because original employment is considered to be adequate consideration.

Second, the decision confirms that Pennsylvania law mandates "consideration," or "some corresponding benefit or . . . favorable change in employment status" to a continuing employee who signs a non-compete. Otherwise, the covenant is not enforceable.

Third, Pennsylvania employers who have asked existing employees to sign non-competes or are considering doing the same, should evaluate whether consideration was or will be provided for the non-compete to ensure enforcement.

Fourth, employers should audit their existing non-compete agreements with Pennsylvania workers to determine whether they should ask existing employees to sign new non-compete agreements with adequate consideration to ensure enforcement.

Robert B. Milligan is partner and co-chair of the Trade Secrets, Computer Fraud & Non-Competes practice group in Seyfarth's Los Angeles office. Paul E. Freehling is senior counsel and member of the Trade Secrets, Computer Fraud & Non-Compete practice group in the firm's Chicago office. If you have any questions, please contact your Seyfarth attorney, Robert B. Milligan at rmilligan@seyfarth.com or Paul E. Freehling at pfreehling@seyfarth.com.