A Few Recent Local[1] Cases on Severance Agreements and Severance Benefits

Click **here** for FAQ on Severance Agreements.

A. The District of Columbia

Former Employee Does Not Have Libel Claim Against Former Employer for Telling Current Employer that He Breached a Noncompete Agreement: In *Murphy v. LivingSocial*, 931 F.Supp.2d 21 (D.D.C. 2013), Wendy Murphy worked at LivingSocial and signed a noncompete agreement, which stated among other things that she "agrees that following [plaintiff's] employment with the Company, the Company shall have the right to communicate the terms of this Agreement to any prospective or current employer of Employee. Employee waives the right to assert any claim for damages against Company or any officer, employee or agent of the Company arising from such disclosure of the terms of this Agreement." The parties had agreed by contract that D.C. law applied, although Ms. Murphy lived in Illinois. LivingSocial believed that Ms. Murphy was about to work for a direct competitor and thought she might have helped the competitor by helping it solicit employees and customers. In-house counsel sent her warnings not to violate the agreement, and the court described what happened next:

> Also on March 21, 2012, Brown sent a letter to Travelzoo's Human Resources Director, Kaity Benedicto, regarding the solicitation of the

[1] I am admitted to the bars of the District of Columbia and Maryland, but not to the Virginia Bar.

> LivingSocial sales representative. Compl. ¶ 70 & Ex. 4 ("Travelzoo Letter"). The Travelzoo Letter outlined plaintiff's continuing obligations under the Non–Compete Agreement and demanded that Travelzoo cease and desist further solicitation of LivingSocial employees, customers, or prospective customers. The Travelzoo Letter is the subject of Count IV and defendants' motion to dismiss.

931 F.Supp.2d at 24. Ms. Murphy sued LivingSocial and the attorney, claiming libel *per se* in that her integrity was questioned. The court held that D.C. law did apply because of the agreement, and rejected the libel claim because the letter to Travelzoo was privileged, both under the privilege for attorneys' communications sent in anticipation of litigation and under the privilege of consent. The court's discussion of the limits of these privileges are useful reminders:

> Here, the Travelzoo Letter was written by LivingSocial's attorney, advised Travelzoo of plaintiff's contractual obligations, explained that plaintiff's actions appeared to have been taken in violation of the contract, stated that LivingSocial reserved its rights "to take all legal and equitable action to protect its business interests," and demanded that Travelzoo "immediately cease and desist from any further solicitation of LivingSocial employees, customers, or prospective customers." Compl., Ex. 4. The Court finds that the statements in the letter indicate that litigation was under serious consideration. Furthermore, the statements in the letter bear a clear relationship to the dispute because they defined the nature of the dispute. Accordingly, the Court finds that the Travelzoo Letter is protected by the judicial proceedings privilege.FN3
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> FN3. Indeed, plaintiff's argument that the letter was not sent in anticipation of litigation is belied by the fact that she filed this lawsuit on March 26, 2012, only five days after the date of the letter.
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> Plaintiff's claim also fails because the statements in the letter are protected by the privilege of consent. *See Farrington v. Bureau of Nat'l Affairs, Inc.*, 596 A.2d 58, 59 (D.C.1991) ("Consent is an absolute defense to a claim of defamation."). The publication of a defamatory statement is privileged if "(1) there was either express or implied consent to the publication; (2) the statements were relevant to the purpose for which consent was given; and (3) the publication of those statements was limited to those with a legitimate interest in their content." *Id.*

> The Non–Compete Agreement contains an express provision by which plaintiff consented to LivingSocial's communicating the terms of the Non– Compete Agreement "to a prospective or current employer" of plaintiff. Non–Compete Agreement at ¶ 6(b). The statements made in the letter, alleging plaintiff had violated the restrictive covenants of the Non–Compete Agreement, were directly relevant to the purpose for which consent was given. Finally, the publication of the statement was limited to Travelzoo's human resources director, who had a legitimate interest in the content of the statements. Accordingly, the letter is protected by the privilege of consent, and plaintiff's claim fails.

931 F.Supp.2d at 26-27.

B. Maryland

Danger in relying on severance benefits for executives in Maryland nonprofit health insurance firms: On August 16, 2013, the Maryland Court of Appeals—the highest court in Maryland—handed down its decision in *Maryland Insurance Commissioner v. Kaplan*, __ A.3d __, 2013 WL 4267854 (Md. 2013). Mr. Kaplan was an executive with CareFirst, a nonprofit firm. The compensation of executives of such companies is closely regulated in Maryland. A statute, State Government Article sections 6-301(b)(4) and 6-301(b)(5), give the Insurance Commissioner the power to oversee executive compensation in the event of conversion to for-profit status, merger, or acquisition. The Court of Appeals described the purposes of the legislation:

> A key concern of that legislation is to ensure that the "public or charitable assets" of such an entity are not redirected to the private benefit of its managers or others. Any such transaction is to be scrutinized to, among other things, "ensure that no part of the public or charitable assets ... inure directly or indirectly to an officer, director, or trustee" of the organization. SG § 6.5–301(b)(4). In addition, steps must be taken to ensure that "no officer, director, or trustee of the [organization] receives any immediate or future remuneration as the result of an acquisition ... except in the form of compensation paid for continued employment...." SG § 6.5–301(b)(5). These restrictions are sometimes referred to as the "anti-inurement" and "anti-bonus" provisions of the law governing acquisitions of nonprofit health care entities.

(Footnote omitted.) In 2004, the legislation was amended to give the Insurance Commissioner general regulatory authority over executive compensation for nonprofit health insurers:

> A director, trustee, officer, executive, or employee of a [nonprofit health service plan] may only approve or receive from the assets of the corporation fair and reasonable compensation in the form of salary, bonuses, or perquisites for work actually performed for the benefit of the corporation.

The Commissioner had previously set these standards in the case of an acquisition of CareFirst by WellPoint that the Commissioner blocked. Mr. Kaplan worked as an Executive Vice President from December 2000 to April 30, 2008, when he was terminated without cause. CareFirst's Compensation Committee decided not to pay $4,034,122 in severance benefits provided in his employment agreement, because the money was not for work actually performed. The Insurance Commissioner upheld CareFirst's decision, and Mr. Kaplan challenged that in court. The Circuit Court and the Court of Appeals both upheld the decision as well.

- **Take-away from *Maryland Insurance Commissioner v. Kaplan*:** Executives of nonprofit health insurance companies in Maryland should evaluate the comparative benefits of staying or leaving with a clear view that some of the severance benefits promised them in their employment agreements may be illusory.

Fee-Shifting Clauses May Inadvertently Bite the Employers Drafting Them: Employers drafting non-solicitation or noncompete clauses in severance agreements sometimes try to raise the stakes—and thus deter violations—by requiring the loser in a proceeding to enforce the clause to pay the winner's attorney's fees. If the employee violates the agreement, the employee has to face a hefty financial sanction as well as an injunction, even if the employer cannot prove damages. Any attorney advising the employee has to point out the seriousness of the risks the employee will face for violating such clauses. However, employers also face substantial financial risk if they make claims of violations but their proof falls short. *Weichert Co. of Maryland, Inc. v. Faust*, 419 Md. 306, 312-13, 19 A.3d 393, 397 (Md. 2011), is a case in point. The court described the issues:

> In this case, Petitioner, Weichert Co. of Maryland, Inc. ("Weichert"), instituted a breach of contract claim against its former employee, Respondent, Dorothy Crago Faust ("Faust"). Weichert claimed that Faust violated the terms of her employment agreement by breaching the duty of

> loyalty, and by breaching a non-solicitation clause which was included in the contract. Under the terms of the contract, if Weichert brought a claim under the non-solicitation clause, and did not succeed on that claim, Faust would be entitled to recover attorney's fees incurred in defending against the claim. A jury determined that Faust breached the duty of loyalty, but did not violate the non-solicitation clause. After the trial, Faust petitioned for attorney's fees under the terms of the non-solicitation clause. Faust was awarded attorney's fees by the Circuit Court, and the Court of Special Appeals affirmed. We shall affirm the intermediate appellate court and hold that Faust's breach of the duty of loyalty did not result in a forfeiture of her rights under the non-solicitation clause, and thus Faust was entitled to recover attorney's fees.

Faust was awarded $946,014.50 in attorney's fees, and the Court upheld the award. The Court stated that Weichert could have treated Faust's breach of the duty of loyalty as a material breach, rescinded the contract, and cut off Faust's ability to claim fees. Instead, it chose to treat the contract as continuing in effect and sued for damages under the non-solicitation clause. The court held that Faust's right to fees for winning on that issue was not destroyed or undermined by the finding that Faust breached his duty of loyalty. There was no fee-shifting agreement on that claim because the fee-shifting provision only applied to the non-solicitation clause. Judge Adkins, joined by Judge Murphy, sharply disagreed with the majority on these issues, and concluded:

> Therefore, contrary to the majority's assertion, Weichert's pursuit of damages under the con-tract and its disavowal of the attorney's fees obligation are not mutually exclusive. See Williston on Contracts, § 63:31 (4th Ed.2002) ("[W]here the contract has merely been breached, in other words, where one party has failed or refused to perform some obligation under it, ... the wronged party may be excused from further performance and recover for loss occasioned to him.") (emphasis added).
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> D. Conclusion
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> In this case, an employee engaged in a sophisticated scheme to deprive her employer of a large portion of its work force, dealing a stunning blow to the employer's business. In doing so, she violated the "fundamental" duty of loyalty and materially breached her employment contract. Accordingly, as the injured party, Weichert is excused from any remaining contractual obligations, and Faust, as the materially breaching party, is not entitled to the contractual benefit of attorney's fees. The jury's finding that she did not breach her non-solicitation clause does not mitigate her disloyal

scheme to decimate her employer's workforce. Indeed, Faust had no need to solicit after she left Weichert, as she had already filched the other employees while still on the payroll herself. For these reasons, I cannot accede to the majority's decision to re-ward Faust's underhanded actions, and I respectfully dissent.

419 Md. at 342-43, 19 A.3d at 415.

- **Take-Away from *Weichert Co. of Maryland, Inc. v. Faust*:** In light of the strong disagreement between the majority and minority, and in light of the fact that this happened to an extremely capable defense attorney, it is critical to obtain sound legal advice about how to proceed in similar situations in light of this decision. It may also be a good idea to insert into the severance or employment agreement provisions governing options for the injured party in the event of breach, and the survival of claims for pre-rescission breach of the contract.

An example of curing some of these problems by careful drafting was provided in *Maternal-Fetal Medicine Associates of Md., LLC v. Stanley-Christian*, 2013 WL 3941970 (Md.App. 2013) (not officially reported). There, the Court of Special Appeals stated at p. *15:

> These contractual provisions are asymmetric. If Maternal–Fetal brought an action to enforce the Non–Competition Provision and prevailed, it could recover its fees and expenses. On the other hand, it had no contractual right to recover its fees if it sought to enforce another provision, for example, Christian's obligation to reimburse Maternal–Fetal for prepaid malpractice insurance premiums. Christian, on the other hand, could recover her fees if she prevails in any action brought by Maternal–Fetal but only if she was in compliance with all of the provisions of the Agreement. Asymmetry, however, not necessarily unreasonable. By potentially shifting the costs of an action to enforce the Non–Competition Provision to her, § 14(d) provided an incentive to Christian to comply with it. Christian is barred from taking advantage of the fee-shifting provision if she is otherwise in breach of the Agreement, thus providing a reason for her to perform the other provisions of the Agreement. FN9
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> FN9. The drafters of § 14(d) thus addressed the anomalous situation presented in *Weichert v. Faust*, in which a party who breached her duty of loyalty to her employer nonetheless recovered under a fee shifting clause because she had not breached its non-competition provisions. See *Weichert*,

> 419 Md. at 331 ("I cannot endorse the majority's conclusion that an employee who violated the 'fundamental' duty of loyalty can still benefit from the employment contract that she so egregiously breached." (Adkins, J., dissenting)).

The Period of Limitations for Enforcing a Noncompete Clause in Maryland Does Not Stop Running While Going through a Required Arbitration Proceeding: Employers drafting noncompete, nonsolicitation, and severance agreements often include ADR (alternative dispute resolution) clauses in the agreements to try to save the time and expense of litigation. A recent case in the Maryland Court of Special Appeals reminds innocent parties that it is important not to sleep on their rights when such contracts are breached. In *Kumar v. Dhanda*, 198 Md.App. 337, 17 A.3d 744 (Md.App. 2011), the contract between these physicians contained an agreement to nonbinding arbitration and allowed them to go to court if either did not like the decision of the arbitrator. This can be a useful device to let the parties how a qualified impartial outsider views the rights and wrongs of their dispute, so that they can re-evaluate their decisions on settlement before proceeding in court. Here, however, there were unusually lengthy delays. Drs. Kumar and Dhanda severed their professional relationship on August 31, 2003. Dr. Dhanda sued Dr. Kumar in 2003, and on April 3, 2003 Dr. Kumar won a motion to compel arbitration. The court stated that nothing happened for more than two years, and then Dr. Kumar sued Dr. Dhanda in April 2005 and again asked for an order compelling arbitration. That order was granted on November 20, 2006. A year and a half later—on March 28, 2008—the arbitration was held. The June 20, 2008 arbitration award denied all relief to Dr. Kumar and gave a small award to Dr. Dhanda on his counter-claim. Almost nine months later, Dr. Kumar sued Dr. Dhanda in court again. The court held that the period of limitations can be suspended by private agreement, but will keep running during a mandatory nonbinding arbitration where the parties did not reach such an agreement. 198 Md.App. at 350, 17 A.3d at 752.

Claims that a Former Employee Disclosed Trade Secrets or Violated the Nondisparagement Clause of an Employment Agreement Are Dismissed Where the Former Employer's Complaint Was Not Specific: *Structural Preservation Systems, LLC v. Andrews*, 931 F.Supp.2d 667 (D.Md. 2013), dismissed the plaintiff company's claims against three former California employees, that they had disclosed trade secrets in violation of the confidentiality provisions of their employment agreements, and in violation of the Maryland Uniform Trade Secrets Act, because the company had failed to plead the essential facts:

> The Court finds that the Complaint lacks sufficient factual allegations and clarity to present a plausible claim that the information relied upon is protectable as a "trade secret" under the MUTSA. For example, it is unclear what the term "established customer relationships" means and how such "relationships" are plausibly construed as a trade secret. If SPS is referring to customer lists, it must say so with specificity and consistency. *See NaturaLawn of Am., Inc. v. W. Grp., LLC*, 484 F.Supp.2d 392, 399 (D.Md.2007) (finding "customer lists" of national franchisor of organic based lawn care services to be trade secrets where customers were not widely known outside company and customer lists were carefully guarded).
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> The Complaint does not allege facts upon which a reasonable inference can be drawn that the claimed "trade secrets" hold independent economic value because such information is not generally known to or readily ascertainable by others in the relevant business. Further, the Complaint does not allege what "trade secret(s)" it is that Andrews (or any particular Defendant for that matter) misappropriated.

931 F.Supp.2d at 679. The court also granted defendants' motion to dismiss the company's claim that defendant Andrews had violated the nondisparagement clause of his employment contract. The company's Complaint alleged that Andrews had made "[S]everal disparaging remarks and false accusations against SPS including but not limited to that SPS is involved in a bid rigging scheme, has raided other corporate entities and interfered with other business's ventures, and is engaged in racism and discrimination." *Id.* at 680. The court held that "SPS does not allege the particular nature of the remarks or to whom or when such remarks were made." The court found that the company had failed to plead essential facts. Finally, the court upheld the parties' contractual choice of Maryland as the forum State.

Open-Ended Terms in Employment Agreements Do Not Make the Contract Unenforceable: *Manning v. Mercatanti*, 898 F.Supp.2d 850 (D.Md. 2012), is an important case. The employment contract of the two plaintiffs read in part as follows:

> Under the Employment Agreements, the Mannings are obligated to provide "advisory services" with respect to both radio stations, although they are not "required to devote any mini-mum number of hours," nor are they required to be "physically located at any office of [Nassau] or at the [radio s]tations." Id. ¶ 2. In exchange for these services, the Mannings are to receive two million dollars each, payable over ten years, ending in July

> 2015. Complaint *854 ¶ ¶ 7, 9. And, under Paragraph 3 of the Employment Agreements, their compensation is due "regardless of whether [the Mannings have] resigned" or been "fired, with or without cause."

898 F.Supp.2d at 853-54. Plaintiffs sued when they did not receive some of the payments allegedly due. The defendant moved to dismiss, arguing that there was no consideration for the payments, and thus that there was no enforceable contract. The court agreed on the need for consideration, and agreed that illusory contracts were unenforceable, but held that the contract was not illusory because it was merely open-ended. The court explained:

> As noted, ¶ 2 of the Employment Agreements provides: "Employee shall devote such business time as Employee deems reasonably necessary to provide [advisory] services but shall not be required to devote any minimum number of hours." Despite Mercatanti's claim, this language does not give the Mannings the "unilateral right to perform zero hours of work for Nassau," so as to render the Mannings' promises illusory and the Employment Agreements unenforceable. MTD Memo at 7. Rather, it is typical of "open terms" contracts, by which the parties are bound despite the presence of "non-specific contractual standards." *First Union Nat. Bank v. Steele Software Sys. Corp.*, 154 Md.App. 97, 174, 838 A.2d 404, 449 (2003) (holding a "best efforts" clause enforceable despite its lack of specificity), *cert. denied*, 380 Md. 619, 846 A.2d 402 (2004); *accord Baron Fin. Corp. v. Natanzon*, 509 F.Supp.2d 501, 513 (D.Md.2007) ("[C]ontractual 'best efforts' terms are enforceable under Maryland law, even when parties to a contract have chosen not to define those terms or expressly provide a standard by which to measure a promisor's performance.").
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> "'[O]pen term' performance contracts are premised upon a mutually enforceable agreement that the non-specific standard selected by the parties will be interpreted and applied by a fact-finder 'after the fact,' based on all the circumstances surrounding the parties' course of dealing." *8621 Ltd. P'ship v. LDG, Inc.*, 169 Md.App. 214, 229–30, 900 A.2d 259, 268 (citation omitted), *cert. denied*, 394 Md. 480, 906 A.2d 943 (2006); *see also* Mark P. Gergen, *The Use of Open Terms in Contract*, 92 COLUM. L. REV. 997, 1000 (1992) ("Gergen") (stating that contracts using open terms usually require performance "under a negligence-like term" such as reasonableness). Of import here, open contract terms do "not preclude formation of an enforceable contract if that is what the parties intended." *First Union Nat. Bank*, 154 Md.App. at 173, 838 A.2d at 449. *See 8621 Ltd. P'ship*, *supra*,

169 Md.App. at 228, 900 A.2d at 267 ("Lack of specific terms ... does not necessarily make a ... clause in a contract meaningless.").

898 F.Supp.2d at 858-59. The court also referred to the presumption under Maryland law that the parties to a contract will act in good faith and deal fairly with the other parties. It explained: "This principle 'governs the manner in which a party may exercise the discretion accorded to it by the terms of the agreement.' . . . In performing, the 'party with discretion is limited to exercising that discretion in good faith and in accordance with fair dealing.' . . . Accordingly, there is no merit to Mercatanti's assertion that the language of the Employment Agreements allows the Mannings to work 'zero hours' and still receive compensation." *Id.* at 859. In addition to all this, the court held that "the 'non-compete' and 'confidentiality' clauses of the Employment Agreements constitute valid consideration." *Id.* Accordingly, the court denied the defendant's motion to dismiss the Complaint.

C. Virginia

Unintentionally repudiating one's own severance benefits: What happens when a highly-compensated executive ($360,000 a year), tells his employer four months into his job that he wants $1,000,000 a year and other changes in his employment agreement and will consider himself terminated if he does not get these changes, does not get the changes but continues to work for a time while trying to negotiate his demands, was fired three months later, considers himself terminated without cause, and then sues for a year's pay in the severance benefits promised in his Executive Employment Agreement if he does not resign and is not terminated for cause? *Bennett v. Sage Payment Solutions, Inc.*, 282 Va. 49, 710 S.E.2d 736 (Va. 2011), provides the answer: The employee repudiated his contract by leaving, and this breach enabled his employer to avoid paying the promised severance benefits.

- Take-away: It is always difficult to get a favorable decision when pushing the envelope too far. The courts tend to favor parties who are reasonable.

Applying Georgia Law, a Virginia Federal Court Held that a Nonsolicitation Agreement Without a Time Limit is Unenforceable: *General Assur. of America, Inc. v. Overby-Seawell Co.*, 893 F.Supp.2d 761 (E.D.Va. 2012). Enough said.

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