# THE DUTY OF LOYALTY IN THE EMPLOYMENT RELATIONSHIP: LEGAL ANALYSIS AND RECOMMENDATIONS FOR EMPLOYERS AND WORKERS

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## ABSTRACT

*Capitalism, free markets and competition are all concepts and practices that are deemed to be good for the growth, development and sustainability of the economy while also benefiting consumers through more variety and lower prices. Of course, this assumption only holds true if markets and competition are open, honest and fair to all parties involved, including employers as every organization is entitled to faithful and fair service from its workers. The common law duty of loyalty in the employment relationship ensures fair competition and faithful service. Of course, a duty of loyalty is often violated when an employee begins to compete against his or her current employer. As such, the employee must not commit any illegal, disloyal, unethical or unfair acts toward his/her employer during the employment relationship. Accordingly, in this article, we provide a review of how the courts "draw the line" between permissible competition and disloyal actions. We discuss the key legal principles of the common law duty of loyalty, their implications for employees and employers and we provide practical recommendations for all parties in the employment relationship.*

**Keywords**: Duty of Loyalty, Faithless Servant, Fiduciary Relationships, Replevin, Common Law.

## INTRODUCTION

This article examines the duty of loyalty in the employer-employee relationship. The focus is on the duty of the employee to act in a loyal manner while being employed by the employer. This duty of loyalty was created by and principally today based on the common law, that is, judge-made decisions that interpret and apply the duty of loyalty to employment cases and controversies. As such the article analyzes common law decisions which illustrate and explicate this fundamental employment obligation. The article also reviews current legal and management commentary that further explain the duty of loyalty.

After this brief introductory section, the authors state the limitations of this article. Next, the article provides an extensive legal analysis of the topic by initially covering an overview of the duty of loyalty and why it is an integral part of a fiduciary relationship. Next, the authors discuss and supply illustrations for several key factors that the courts cite in determining whether an employee has breached his or her duty of loyalty to the employer, to wit: Whether the employee has engaged in direct or indirect competition against the employer, whether the employee has engaged in competition as opposed to mere business preparation, whether the employee's allegedly disloyal acts were done in secret or known by the employer and the rank of the employee, that is, whether the employee is a high-level executive or managerial employee or merely a rank-and-file employee. Then the authors discuss and illustrate several problem areas that arise in this area of the law, to wit: The employee hiring co-workers, contacting customers and clients of the employer, using and taking customer lists and criticizing his or her employer, including on social media. Next, the authors state and illustrate the remedies available to the employer when the employee breaches the duty of loyalty, including contractual, tort and equitable remedies as well as forfeiture of salary or compensation. We review three related legal doctrines that could impact duty of loyalty situations, to wit: Covenants-not-to-compete which may be found in the employment contract, the tort of intentional interference with contract or contractual or business relations and civil as well as criminal wrong of misappropriation of trade secrets. The next major section of the article is the discussion of the practical and legal implications of the duty of loyalty as explicated by the case law and legal and management commentary. The authors discuss the implications of these legal principles from the perspectives of both the employee and the employer. Next, based on the aforementioned legal analysis and the discussion of implications we supply recommendations to the employee on how to avoid liability pursuant to the duty of loyalty and also to the employer on how to protect its legitimate interests yet without unduly burdening the employees' right to make a livelihood and to better him or herself economically. The article concludes with a brief summary and conclusion followed by a bibliography.

## LIMITATIONS

This article focuses on the duty of loyalty as created by the common law, that is, judge-made, case-law decisions. The article consequently does not cover duties of loyalty which are set forth explicitly by statutes, for example, the duty of loyalty imposed on employees pursuant to the federal Computer Fraud and Abuse Act (For example, Tech Systems, Inc. v. Pyles, 2015; Instant Technology, LLC. v. Elizabeth DeFazio, 2014; Dodson, 2012). Also, this article is presented as a general overview of the law for the benefit of employers and employees. As this body of law is state-specific any duty of loyalty controversy that arises in a particular state will have to be resolved by the specific law of that state, especially any pronouncements from the state's highest court-the state supreme court and thus reference to that discrete state corpus of jurisprudence must be made by the parties involved and their legal counsel. Although the fiduciary duty of principals and agents will be addressed in this article as that duty relates to the duty of loyalty, the article will not extensively examine agency law and the rights, duties and liabilities of principals and agents. However, the article will cover the "faithless servant" doctrine of agency law, which prohibits an agent from obtaining a profit from any misfeasance, malfeasance or misconduct in performing the duties of the agency (Christopher James Bailey v. Fast Model Technologies, LLC. 2012), since that doctrine is used for the forfeiture remedy in disloyal employee cases too.

Furthermore, this article neither will deal with the fiduciary duty nor the duty of loyalty of corporate directors to their corporations (For example, In Re Goldman Sachs Mortgage Servicing Shareholder Derivative Litigation, 2012; Gray, 2000), such as pursuant to the "corporate opportunity doctrine" (For example, Engenium Solutions, Inc. v. Symphonic Technologies, Inc., 2013; Gray, 2000). A final limitation is that although the situation of whether an employer criticizing his or her employer violates the duty of loyalty will be addressed herein the context will be private sector employment; and as such the constitutional 1st Amendment free speech rights of public sector employees to criticize their government employers (For example, Joyce Rock v. Dan Levinski, 2015; Tommie Jo Marsilio v. Victor Vigluicci, 2013) will not be covered in this article.

## LEGAL ANALYSIS

Employee loyalty is an element of employee commitment (Mujtaba, 2014) which professional managers try to secure by effectively planning, organizing, leading and controlling what they and their teams do in a strategic manner. At the meantime, management teams must remain open, honest, ethical and regularly engage their employees in relevant tasks and jobs in order to keep them highly productive and satisfied (Mujtaba and McCartney, 2007). Consequently, managers and their employees should be aware of the duty of loyalty to their employers, their fiduciary relationship responsibilities, liability issues if they choose to start a new business in their areas of expertise and other such elements of their employment.

### Common Law Duty of Loyalty

The fundamental common law rule is that an employee has a legal duty not to engage in any disloyal acts against his or her employer during the employment relationship (For example, Futch v. McAlister Towing Inc., 1999; Insurance Field Services, Inc. v. White & White Inspection & Audit Services, 1980; Tuschman, 2016). This duty of loyalty does not depend on the existence of a written employment contract (Warren and Pedowitz, 2011). The employee can be an employee at-will and is still bound by the duty of loyalty (Audio-Visual Group, LLC. v. Christopher Green, 2014). The duty is implied by virtue of the common law (Futch v. McAlister Towing Inc., 1999). As such, the employee must act in an honest, faithful and loyal manner and must discharge all of his or her employment duties for the sole benefit of the employer (Warren and Pedowitz, 2011). If the employee acts in a self-serving manner which is contrary to the employer's interests, the duty of loyalty is violated (Futch v. McAlister Towing Inc., 1999). Similarly, if an employee fails to disclose matters that are inimical to the interests of employer the duty is violated (Futch v. McAlister Towing Inc., 1999). If the employee takes an undisclosed payment or receives an undisclosed benefit from a third party the duty is violated (Futch v. McAlister Towing Inc., 1999).

Being merely a poor performing employee at-will does not automatically equate to a breach of the duty of loyalty to one's employer. For example, in the case of Wilson v. Nevada Affordable Housing Assistance Corporation (2017), the employer (NAHAC) fired a negligent controller (Wilson) for improperly releasing a wire transfer, sharing her bank token (key to authorize wire transfers) with other employees and various other alleged performance failures.

However, the employer did not proffer evidence to the court that the ex-employee was self-dealing. The court issued summary judgment in favour of the ex-employee by explaining:

> *NAHAC offers no evidence that Wilson acted contrary to NAHAC's interests, disclosed its confidential information to outside sources to NAHAC's detriment, competed against NAHAC or usurped a NAHAC opportunity. NAHAC's claim is based entirely on Wilson's violation of internal policies regarding the proper authorization of a wire transfer and the proper handling of bank tokens. NAHAC employees admit NAHAC suffered no injury from these internal policy violations. Wilson's conduct does not support a claim for breach of the duty of loyalty (Wilson v. Nevada Affordable Housing Assistance Corporation, 2017).*

One court dismissed the employer's breach of loyalty claim against multiple employees who were allegedly sleeping, using their personal cell phones, reading personal mail and newspapers and viewing pornography in an electrical breaker room for extended periods of time, which went well beyond any break periods. According to that court, such activities by these employees did not amount to a valid disloyalty action, even if their misconduct occurred (Laba v. Chicago Transit Authority, 2016). That court relied upon prior precedent which established that an employee who fails to perform his or her work, whether he or she spends time and "work" sleeping on the job, day-dreaming or "surfing" the internet; yet nonetheless the employee still accepts a full pay check but this action simply is not comparable to an employee who steals or embezzles from his or her employer when analysing breach of loyalty claims against regular employees (Laba v. Chicago Transit Authority, 2016).

Of course, once the employee leaves the job (employer's employ) he or she no longer owes the duty of loyalty and is free to compete against his or her former employer, absent any contract provisions to the contrary (Instant Technology, LLC. v. Elizabeth DeFazio, 2014).

**Fiduciary Relationship**

In the context of employment law, the fiduciary duty is generally a one-way street benefitting only the employer. This has been a focus on various commentaries questioning if fiduciary duty of loyalty pressed upon an employee is fair since it is so one-sided in the employment context. The logic by such criticisms can be summarized as follows:

> *Under fiduciary law, only one of the two parties must be "loyal" to the other; the employer has no fiduciary duties with respect to the employee. As a result, employees are arguably made to be fiduciary dupes: They are loyal to an entity that owes no loyalty to them. This disparity plays out in the at-will presumption, which allows employers to fire employees at any time and for a variety of reasons having nothing to do with performance. The duty of loyalty seems particularly onerous when framed in terms of the "faithless servant." According to this doctrine, an employee who violates the duty of loyalty must disgorge the entirety of her wages for the period of disloyalty. These doctrines work to disempower the employee. The employee can be let go at any time and for a variety of reasons, but the employee must always act in the interest of the employer. Although at-will employment and the employee's duty of loyalty are not necessarily contradictory, they highlight a larger problem of employee vulnerability. If fiduciary law is justified as a protection for the vulnerable, as is often stated, then why does it protect employers and not employees? Even if an employee might hold discretionary legal power in her hands, is there any doubt about who holds the real power in the relationship? (Bodie, 2016).*

Nevertheless, even if the fiduciary duty in the workplace is unbalanced and favouring only the employer who can legally focus on its own self-interest, this duty exists like an obligation upon the agent, which will be seen forthwith and thus cannot be ignored.

**The Principal-Agent Relationship v. the Employer-Employee Relationship**

First, it is necessary to distinguish between the employer-employee relationship and the principal-agent relationship. An employee is a person who works for an employer and who is subject to the right and the power of the employer to control the manner of the physical manner of the work. Typically, an employee does not have a great deal of discretion in performing work duties. Moreover, as a general rule, the employer-employee relationship is not deemed to be a fiduciary one. Whereas, an agent is a person who not only works for a principal but represents and "stands-in-the-shoes of" the principal, mainly to effectuate contractual and business dealings for the principal (Cavico and Mujtaba, 2014). One of the key characteristics of the principal-agent relationship is that it is a fiduciary one; that is, the parties stand in a fiduciary relationship (Restatement (Second) of Agency). The fiduciary relationship is one imposed by law; it is a relationship of trust, confidence, integrity, good faith, good conscience and fair dealing between the parties thereto (Cavico and Mujtaba, 2014; DeMott, 2006). The fiduciary relationship also encompasses a duty of fidelity and loyalty that the parties owe to one another (Cavico and Mujtaba, 2014; Dodson, 2012). As such, an agent must always act solely and entirely for the benefit of the principal in any matter within the scope of the agency relationship (Cavico and Mujtaba, 2014; DeMott, 2006; Reuschlein and Gregory, 1979).

**The Fiduciary Relationship v. the Implied General Duty of Loyalty**

The duty of loyalty in the employer-employee relationship is at times referred to by some courts as a fiduciary duty (Base One Technologies, Inc. v. Mohammed Ali, 2015; Shamrock Power Sales LLC. v. John Scherer, 2015; Synthes, Inc. v. Emerge Medical, Inc., 2014; Hennegan Co. v. Arriola, 2012; Tuschman, 2016). As one court stated, applying New York law, the duty of loyalty in the employment relationship goes "in tandem" with the fiduciary relationship (Shamrock Power Sales LLC. v. John Scherer, 2015). Moreover, this duty of loyalty is often premised on and extrapolated from the Restatement (Second) of Agency's (1958) and Restatement (Third) of Agency's (2006) imposition of the fiduciary relationship to principals and agents (Scanwell Freight Express, Inc. v. Chan, 2005; Selmi, 2012; Synthes, Inc. v. Emerge Medical, Inc., 2014). However, even if the duty of loyalty is not one premised on a fiduciary duty, the more "generic" and general duty of loyalty still exists to be applied to a case (Grebe, 2002). This common law general duty of loyalty presupposes faithful, honest, ethical, diligent and attentive conduct on the part of the employee (Grebe, 2002).

Claims for breach of fiduciary duty and breach of the duty of loyalty can overlap and consequently be duplicative of each other. In Mimedix Group, Inc. v. Fox (2017), the employer terminated Mr. Fox for encouraging subordinates to sell competitor medical device products; and consequently the employer sued for multiple counts including breach of fiduciary duty and breach of duty of loyalty. The court explained that in order to state a claim for breach of fiduciary duty, a plaintiff must allege: (1) That a fiduciary duty exists; (2) that the fiduciary duty was breached; and (3) that such breach proximately caused the plaintiff's injury; and as such the court dismissed the duty of loyalty claim as it was identical to the breach of loyalty count and based on the same operative facts (Mimedix Group, Inc. v. Fox, 2017).

## Critical Factors in Determining Liability

### Direct v. Indirect Competition

There are several factors to be taken into consideration when determining if an employee has breach the duty of loyalty. First and foremost, directly competing against one's employer while working for the employer clearly violates the duty of loyalty (Doyle v. Camp, 2001; Futch v. McAlister Towing Inc., 1999; Selmi, 2012). As one federal district court related, applying District of Columbia law: "It is well established that an employee is prohibited from acting in any manner inconsistent with his or her employment and must exercise good faith and loyalty in performing his or her duties and may not use his or her principal's time, facilities or proprietary information to build a competing business" (Base One Technologies, Inc. v. Mohammed Ali, 2015).

For example, in the South Carolina Supreme Court case of Futch v. McAlister Towing Inc. (1999), the court ruled that the duty of loyalty was breached when the employee initiated a competing business, undercut his employer on pricing, targeted current customers of the employer asking them to commit to the new company and lured co-workers to work for the new company. However, even if the competition against the employer is indirect a court may still find that the duty of loyalty was breached (Cameco, Inc. v. Gedicke, 1999). As such, the employee can act to harm the employer to benefit a competitor of the employer or to otherwise benefit the competitor, which may be a potential employer for the employee (Selmi, 2012; Boyle, 2000). To illustrate, in the New Jersey Supreme Court case of Cameco, Inc. V. Gedicke, 1999) the court ruled that assistance provided to a competitor of the employer, for example, by co-mingling shipments of goods of the employer and two competitors and by having the competitors' goods delivered first, although indirect behavior nonetheless harmed the employer and thus violated the employee's duty of loyalty. A comment by the Supreme Court of New Jersey in the case of Cameco, Inc. v. Gedicke (1999) is instructive, as the court opined that if the assistance to a competitor of the employer is even slight a breach of the duty of loyalty nonetheless could occur; whereas if the assistance is indirect the employer would have to show that the competitor received substantial assistance.

One clear example of an employee breaching her duty of loyalty to her employer by simultaneously competing against the employer is the case of Adesanya v. Novartis Pharmaceuticals Corporation (2016). Pursuant to an employment agreement, the employee agreed to "devote [her] best efforts and full business loyalty to [her] ability to perform [her] employment with Novartis and not to hold other employment or engage in any other business which may adversely affect [her] ability to perform [her] job responsibilities at Novartis." Novartis' conflicts policy prohibited holding a second job that competed with the interests of the company or own, directly or indirectly, any interest in a competing business. However, the employee violated the forgoing from the onset of her employment with Novartis by failing to disclose that she and her husband jointly owned a sub-S corporation that collaborated with other pharmaceutical companies to develop and market their products in direct competition to Novartis. This court granted summary judgment in favour of Novartis' counter-claim of breach of duty of loyalty and breach of the conflict of interest policy. In doing so, the court explained that under New Jersey's breach of duty of loyalty theories, the employer must show 1) an employee-employer relationship; 2) breach of the duty of loyalty; and 3) harm to the employer. The court then summarized the facts to find that the employee breached the duty of loyalty, who originally sued as a plaintiff for breach of employment agreement and past due payments due from the employer. The following findings are an example of how an employee can deprive his or her employer of "full loyalty":

> *Here, there is no dispute that the Plaintiff and Defendant had an employee-employer relationship. It is also unquestionable that Plaintiff violated both her common law duty of loyalty and her contractual obligations under Novartis's Conflicts Policy. Both prohibit Plaintiff from acting in a manner contrary to Novartis's interest or competing with the company. The Conflicts Policy explicitly prohibits an employee from holding a "second job with or providing any services to a competitor of" Novartis or "engaging in any outside employment or other activity which encroaches on the time or attention that should be devoted to [Novartis's] affairs, otherwise detracts from your ability to perform your responsibilities" or deprives Novartis of "your full loyalty." By actively soliciting and accepting consulting positions with Novartis's competitors and subsequently billing hundreds of hours to them without disclosing or seeking approval for that outside work, Plaintiff impermissibly competed with her employer and divided the loyalty she owed Novartis. It is also clear that Defendant was harmed. Novartis paid Plaintiff for a full-time position, but Plaintiff siphoned off time she owed Novartis to other activities. As such Defendant lost the money it paid her for time she did not commit to the company (Adesanya v. Novartis Pharmaceuticals Corporation, 2016).*

### Competition v. Mere Business Preparation

Plainly, as emphasized, the employee's commencing and carrying on a competing business while working for an employer will be deemed to be a disloyal and illegal act (Furmanite America, Inc. v. T.D. Williamson, Inc., 2007). Mere preparation, however, to open a competing business, even active preparation while in the employer's employ, may be permissible (For example, McGowan & Company v. Roger F. Brogan, 2015, applying Texas law; Harllee v. Professional Services Industries, Inc., 2012; Tuschman, 2016 Synthes, Inc. v. Emerge Medical, Inc., 2014, applying Pennsylvania law). As one federal district court stated, merely making "preparations" or "arrangements" to compete, including planning on buying or even buying a rival business may be permissible, so long as no customers are solicited for the rival business, no confidential information is misappropriated, no conduct directly damaging the employer or directly competing with the employer is done while in the employer's employ (Synthes, Inc. v. Emerge Medical, Inc., 2014). Moreover, incorporating a business to compete with the employer as well as developing competing products or designs may also be permissible so long as the employer's time resources are not utilized and no confidential information is wrongfully used, such as the employer's new product pipeline and plan and pricing proposals and data (Synthes, Inc. v. Emerge Medical, Inc., 2014). As one court stated, "certainly, using (employer's) resources for the purpose of starting a competing company rises to the level of improper 'competition'" (Synthes, Inc. v. Emerge Medical, Inc.).

However, as Gray (2000) points out, "this line separating mere preparation from active competition may be difficult to discern." This critical issue is often deemed a question of fact to be decided by the trier of fact, typically a jury, which will have to look at all the facts and circumstances of the case (Synthes, Inc. v. Emerge Medical, Inc., 2014). An example of mere planning or preparation before leaving the employer's employ would be submitting forms to create a new corporation or business (Gray, 2000). To further illustrate mere preparation, such acts as organizing the competing business, opening a bank account or securing office space have been deemed permissible and not disloyal actions by the employee (Harllee v. Professional Services Industries, Inc., 2012; Fish v. Adams, 1981). However, in the process of preparing for this competing business if the employee harms his or her employer by soliciting customers or clients and/or co-workers, diverting business to the new firm, for example, by forwarding quote requests from potential clients to the new firm or sabotages or impedes performance or otherwise harms the employer, the employee is liable (McGowan & Company v. Roger F. Brogan, 2015; Selmi, 2012). Another example of a situation where the employee "crossed the line" between mere preparation and illegal direct competition is the federal district court case of Synthes, Inc. v. Emerge Medical, Inc., 2014). The case dealt with a high-level employee, called Marotta, who contended that he was merely planning and then formed a competing medical device business, called Emerge, with his former employer, called Synthes. The court, applying Pennsylvania law, ruled that as a matter of law the duty of loyalty was breached by the former employee. The court explained as follows:

> *Thus, while the mere act of soliciting and meeting with potential investors for Emerge may not, on its own, constitute competitive conduct, meeting with potential investors–who are also customers of Synthes–with the intent of luring them away from Synthes may be competitive. Moreover, while meeting with accounting firms and lawyers alone may be deemed preparatory, meeting with such individuals during Synthes business time and billing such time to Synthes may be deemed competitive. Although Marotta may have been entitled to engage an outside vendor for design and development of initial product offerings, misappropriating confidential Synthes information in order to facilitate the design and development of competing products is not permissible. Finally, the simple use of an Emerge email address may not be problematic, but the use of an Emerge email address to communicate with potential customers that are existing customers of Synthes could rise to the level of competition (Synthes, Inc. v. Emerge Medical, Inc., 2014).*

Nevertheless, employees who actively interfere with their then current employer's business dealings in efforts to later compete against that same employer have breached the duty of loyalty. That is what occurred in the case of Hearing Associates, Inc. v. Downs (2017), where the disloyal employee doctor was actively planning to leave the plaintiff's employ and open her own competing audiology clinic by enticing the landlords to cancel certain commercial office space leases with the plaintiff and enter replacement leases with her new competing company during the last two months she was still employed with the plaintiff. That court recognized, however, that there is no precise line between impermissible competition and permissible preparation. Accordingly, whether an employee's actions constitute a breach of the duty of loyalty is a question of fact to be determined, typically by a jury, based on the totality of the circumstances. Of course, once the employee terminates employment with the employer he or she can compete with the former employer, absent any contract provisions to the contrary or misappropriation of confidential information (Hedgeye Risk Management, LLC v. Paul Heldman, 2016).

### Secrecy of Employee Activities v. Knowledge by the Employer

Whether the employee's allegedly disloyal activities were done in secret or known by the employer is another important factor in determining liability. Secrecy implies active wrongdoing and makes the case stronger that the duty of loyalty has been breached (Selmi, 2012). To illustrate, in one federal appeals court case the court upheld a finding of disloyalty by the employee when the employee sold certain second-hands products to retailers of the employer even though the employee thought the products were his own because the employer was not informed of the sales (Colgate-Palmolive Company v. Tandem Industries, 2012). To compare, Warren and Pedowitz, (2011) relate a federal district court case applying New Jersey law, Hahn v. OnBoard, L.L.C. (2011), where the court dismissed the employer's disloyalty claim based on the employee promoting at focus group meetings his own blog and distributing his own blog cards, which did not mention the employer, while attending a trade conference on his employer's behalf, because the employer had pre-existing knowledge of these activities and did not object to these actions.

### Level of the Employee-High Level Managerial v. Non-Managerial Employees

There is a relationship between the position and responsibility of an employee and the duty of loyalty. Accordingly, the duty of loyalty is more likely to be applied to higher level employees who are in a position of trust and confidence and thus have access to confidential information than to lower level employees who perform basic tasks (Selmi, 2012; Boyle, 2000). However, it is important to note that an employee does not have to be a management employee or a high-level employee to have the duty of loyalty imposed by the courts on the employee. As succinctly stated by one federal district court, "even nonmanagerial employees…can undertake certain duties and obligations that entail the duty of loyalty" (Aquent LLC v. Mary Stapleton, 2014). As such, the employee violating the loyalty duty can be a low-level one (Base One Technologies, Inc. v. Mohammed Ali, 2015; Fish v. Adams, 1981; Tuschman, 2016). Lee (2006, P13) also notes that "some courts…have concluded that the duty of loyalty applies to all employees, regardless of status as an officer, director or manager of a firm."

In McClure v. Imperial Woodworking Company (2017) the employee was engaged as the Vice President and Project Executive for a company that was in the business of creating and building luxury retail and hospitality interior finishes and fixtures worldwide. The company counterclaimed against the employee who was seeking unpaid bonuses. The company alleged that the employee breached the duty of loyalty when he underbid a project; failed to resolve disputes with a client; failed to settle disputes with a subcontractor; and travelled to Hong Kong at the employer's expense to solicit a woodwork supplier to terminate its relationship with the company. The court rejected the former employee's motion to dismiss the claim based on the allegation that these were just performance failures and the plaintiff failed to allege any he economically benefitted from his actions and inactions. Instead the court held that deliberate failure to maintain business relationships and actively attempting to taint the company's relationship with a critical wood supplier could plausibly constitute a breach of duty of loyalty and thus the case could proceed forward (McClure v. Imperial Woodworking Company, 2017).

The level of the subject employee allegedly disloyal to their employer also plays a part in a court's evaluation of personal jurisdiction over that individual in an employer's breach of duty of loyalty claim. In Numeric Analytics, LLC v. McCabe, (2016), the court was dealing with multiple claims by an employer against five non-resident x-employees who allegedly breached their duty of loyalty by violating non-solicitation agreements by leaving the plaintiff company's employ, starting a competing business and poaching plaintiff's clients. The five non-resident defendants worked remotely outside of the state of Pennsylvania where their employer's principal place of business was located and where the employer filed suit. The court held that the e-commerce activity by the x-workers was too tenuous to support personal jurisdiction over them, expect one who was the president of the company. However, the court held that there was personal jurisdiction over the former employee who held the position as president with the following explanation:

> *By definition, the President of a company, as an officer, has both a fiduciary duty and a duty of loyalty to the company. Regardless of its geographic reach, Numeric Analytics is a Pennsylvania company, both founded and headquartered here. Its legal address of record with the Delaware Corporate Bureau is Chadds Ford. Necessarily, a breach of fiduciary duty or duty of loyalty by the President of a company affects the viability and fortunes of that company and is felt wherever the principal place of business may be. McCabe's duty as to this claim arises out of her status, not her conduct and that status is inextricably bound to Pennsylvania, which is where Numeric Analytics, for corporate purposes, exists. By accepting the responsibility of corporate officer ship, McCabe distinguished herself from regular employees and aimed her actions into her company's home state in a way that the regular employees did not. McCabe cannot accept the mantle of corporate officership for a Pennsylvania-based business and then renounce any meaningful contacts with the state where it is headquartered (Numeric Analytics, LLC v. McCabe, 2016).*

## Problematic Legal Areas

### Soliciting or Hiring Co-workers of the Employer

The employee's soliciting co-workers prior to the end of his or her employment to join a new competing company likely will be construed by the courts as a violation of the duty of loyalty (For example, Base One Technologies, Inc. v. Mohammed Ali, 2015; L-3 Communications Corporation v. Jaxon Engineering & Maintenance, Inc., 2015; Futch v. McAlister Towing Inc., 1999; Aquent LLC v. Mary Stapleton, 2014; Insurance Field Services, Inc. v. White & White Inspection & Audit Services, 1980; Semi, 2012; Gray, 2000). However, one federal district court, applying Colorado law, counselled that whether the solicitation of co-workers is a breach of the duty of loyalty is a "fact intensive inquiry" requiring consideration of several factors, to wit: 1) The nature of the co-worker's employment relationship with the employer, that is, whether at-will or pursuant to a contract; 2) the impact of the solicitation on the employer's operations; 3) the extent of any promises or inducements made to co-workers; 4) whether the co-workers were "key officers or employees"; 5) whether the co-workers left simultaneously; and 6) was the employer given an "opportunity to hire and train replacements" (L-3 Communications Corporation v. Jaxon Engineering & Maintenance, Inc., 2015).

To illustrate solicitation violations, in the federal appeals case of Stuart C. Irby Company, Inc. v. Brandon Tipton (2015), the court ruled that there was sufficient evidence for a trial on the issue of the duty of loyalty being breached when the employee, while still being employed by his employer, solicited fellow employees to work for a competitor of the employer, whom the employee resigned to work for, by means of several telephone calls, emails and text messages to the co-workers as well as arranging a meeting at the competitor's facility which included "beer and a tour." In the federal district court case of Riggs Investment Management Corp. v. Columbia Partners, LLC (1997), the employee provided to a competitor of the employer confidential and detailed information about co-workers before resigning to work for the competitor's company. The competitor then used the information to recruit employees away from the former employer. The court ruled that the employee violated his duty of loyalty because he did not act for the benefit of his employer and that he acquired in interest adverse to his employer (Riggs Investment Management Corp. v. Columbia Partners, LLC, 1997).

However, when the employee leaves the employer's employ the former employee is allowed to state to his or her former co-workers that he or she is commencing a new business, give them a business card or the equivalent and ask them to join the former employee's new firm (Cavico and Mujtaba, 2014). Of course, such solicitation will not be permitted if the former employee is bound by a non-solicitation or non-piracy clause in the contract with the former employer (Cavico and Mujtaba, 2014).

**Customer Lists**

A violation of the duty of loyalty clearly occurs if the employee while working for the employer uses customer lists and customer contact information to contact the employer's customers to lure them to the employee's competing business (For example, Shamrock Power Sales, LLC v. John Scherer, 2015). As a general rule the employee may not use written lists of clients or customers which he compiled during the course of his employment and took with him or her on departure because such lists will be construed as the confidential and proprietary property of the former employer (Reuschlein and Gregory, 1979, Chapter 7, Section 68). However, if the former employee has developed the list him or herself and there are no contractual restrictions on the employee's taking and using the list there is some authority that the employee can take and utilize the list (Harllee v. Professional Services Industries, Inc., 1992; Tuschman, 2016). Similarly, if the employee developed the list by soliciting clients on her own or before her employment with the employer, then there would be no violation of the duty of loyalty (Judy Poller v. Bioscript, 2013). In First Financial Bank, N.A. v. Bauknecht (2014) a loan officer left his bank to take a job with a competing lending institution. He allegedly copied or compiled a "Master Database" that contained names of 615 individuals and includes contact information for a portion of them, notes about them and other miscellaneous data. The plaintiff employer alleged that the compiling and taking of such a digital list was a breach of loyalty. The bank alleged their x-employee breached his fiduciary duty of loyalty in five ways: "(1) using Plaintiff's computer system to create the master database of customers that he later used to compete against Plaintiff; (2) conducting targeted inquiries into Plaintiff's customer's loans so he could bring that information and deposit account information to Graymont [competing financial institution]; (3) stealing bank property from Plaintiff; (4) denying Plaintiff access to his work phone, which he used to compete against Plaintiff even before he resigned; and (5) coordinating with Graymont about moving over Plaintiff's loans" (First Financial Bank, N.A. v. Bauknecht, 2014). The court denied both parties' cross summary judgment motions as there were issues of fact contested, but did explain that "Employees breach their fiduciary duty when they take action, such as downloading or copying employer data, in order to compete with the employer after their employment has ended...This includes, for example, improperly taking customer lists" (First Financial Bank, N.A. v. Bauknecht, 2014).

**Contacting and Soliciting Customers and Clients of the Employer**

The employee's soliciting of clients and/or customers of the employer prior to the end of employment will also be construed by the courts as a disloyal act (L-3 Communications Corporation v. Jaxon Engineering & Maintenance, Inc., 2015; Futch v. McAlister Towing Inc., 1999; Insurance Field Services, Inc. v. White & White Inspection & Audit Services, 1980; Gray, 2000). In the aforementioned case of (Riggs Investment Management Corp. v. Columbia Partners, LLC, 1997) the court also found that the duty of loyalty was breached because the former employee also provided to a competitor of the employer detailed information about his employer's clients before he resigned to join the competitor, which information the competitor used to solicit and obtain clients from the former employer. Another example is the federal district court case of Shamrock Power Sales, LLC v. John Scherer (2015), where the employee, a sales representative, while being employed, secretly set up a competing business, misappropriated and copied client contact information, price lists and other sensitive and proprietary information, secretly contacted customers and tried to lure them away from the employer, deleted the employer's name from purchase orders and instructed customers not to send their purchase orders to the employer. The court ruled that the evidence showed that this conduct was unfaithful, disloyal, not isolated and thus substantially violated the duty of loyalty (Shamrock Power Sales, LLC v. John Scherer, 2015). In the federal district court case of Audio-Visual Group, LLC. v. Christopher Green (2014), applying Virginia law, the court ruled that the employee, a sales engineer breached the duty of loyalty by invoicing for a separate business 34 customers who were also customers to whom his employer had provided quotations; moreover, the employee was in the process of quoting 29 separate projects to existing or potential customers of his employer.

Moreover, it is irrelevant that the employee did not initiate the contact with the employer's customer. There is still a breach of the duty of loyalty if the employee agrees to do the work for the employer's customer without informing the employer (EDI Precast, LLC v. Raymond K. Carnahan, Jr., 2013). As explained by one federal district court, in such a situation "there is no reasonable view of 'honesty and fair dealing' that would allow (the employee) to take for himself work that was offered to him by (employer's) customer, while employed by (the employer), without informing employer or the customer that he was taking that opportunity for himself. And such a usurpation clearly is inconsistent with any sense of ‘loyalty” (EDI Precast, LLC v. Raymond K. Carnahan, Jr., 2013).

Yet, as one federal district court, applying Colorado law pointed out, “…an employee may advise customers that he or she intends to leave his or her employment, but may solicit those customers to defect to a competing business while the employee remains with the employer” (L-3 Communications Corporation v. Jaxon Engineering & Maintenance, Inc., 2015). So, as pointed by Reuschlein and Gregory (1979), the employee, “should he be fortunate enough to remember who his former employer’s customers…were, will be permitted to solicit business among them” (Chapter 7, Section 68). As such, when the employee leaves the employer’s employ the former employee is allowed to state to his or her former clients or customers that he or she is commencing a new business, give them a business card or the equivalent and ask them to be served by the former employee’s new firm or position (Cavico and Mujtaba, 2014). Of course, such solicitation will not be permitted if the former employee is bound by a non-solicitation or covenant-not-to-compete clause in the contract with the former employer (Cavico and Mujtaba, 2014).

## Criticizing the Employer

### The General Rule

An employee criticizing his or her employer or harming the reputation of the employer can certainly be grounds for finding that the employee has acted in a disloyal manner (Warren and Pedowitz, 2011; Lee, 2006). The leading employee disloyalty case premised on the employee criticizing the employer is the federal district court case of Marsh v. Delta Airlines (2011), applying Colorado law, where a Delta customer service agent published a letter to the editor in the Denver Post criticizing the airline for hiring hourly contract employees to replace full-time employees who were laid off. The customer service agent was ultimately terminated, which discharge the court upheld due to a violation of the implied duty of loyalty (Marsh v. Delta Airlines, 2011).

### Exceptions for Public Policy, Whistleblowing and Labor Relations

There are exceptions to the general rule, however, where the employee’s criticism of the employer will be superseded by other concerns and pertinent legal doctrines. Most states have created judicially an exception to the employment at-will doctrine, called the “public policy” exception, where an employee, even an employee at-will with no contractual protection, cannot be discharged for violating the fundamental public policy of the state, which encompasses actions, such as informing on the employer, to protect the health and safety of the people in that state (Cavico and Mujtaba, 2014). For example, in the aforementioned case of Marsh v. Delta Airlines (2011), the court did note, in ruling for the employer, that the employee’s criticism of the airline was not an effort to inform the public of a safety concern and the court also noted that the employee did not utilize the company's grievance system, which facts may have changed the decision to favour the discharged employee.

### Social Media and Blogging

Today, with the prevalence of social media at the workplace and otherwise the scope of the employee's duty of loyalty and the consequences for violations have been extended considerably to the "virtual" world (Cavico, Mujtaba, Muller and Samuel, 2013, 2013a; Warren and Pedowitz, 2011; Lee, 2006). Consequently, the employee criticizing or disparaging his or her employer or the employer's clients or customers on social media or by blogging can be construed as a violation of the employee's duty of loyalty (Lee, 2006). The duty of loyalty can also be breached if the employee posts confidential information on social media. Of course, the employer must know the identity of the offending employee. Consequently, a major practical and legal problem if the postings or blogging are done in an anonymous manner. Lee (2006) succinctly explains: "…What about the circumstances where the anti-employer blogger hides behind the shadow of internet anonymity to make disloyal anti-employer comments or disclosures? The problem for anonymity for the employer seeking to reveal who it is that is posting negative comments about the firm is profound because anonymous speech is constitutionally protected."

## Relief to Employer

### Legal Remedies

**Breach of Contract Damages:** There are a variety of legal remedies that an aggrieved employer can seek against a disloyal employee. These remedies can be legal remedies; equitable ones or can sound in tort. First, the employer can sue the disloyal employee for the legal remedy of breach of contract with the damages being the extent of financial harm, loss or expense suffered by the employer, including profits lost by the employer as well as the benefit received by the employee (Boyle, 200; Gray, 2000; Reuschlein and Gregory, 1979).

### Forfeiture of Compensation

The employer is also allowed to recover as damages any benefits given to the employee while the employee was violating the duty of loyalty, including wages and compensation paid to the disloyal employee (Warren and Pedowitz, 2011; Boyle, 2000; Gray, 2000). This remedy is typically called "forfeiture" and is based on the "faithless servant" doctrine of principal and agency law, where a faithless servant forfeits all compensation earned during the period of his disloyalty even if the services benefitted the employer to some degree (Base One Technologies, Inc. v. Mohammed Ali, 2015; Shamrock Power Sales, LLC v. John Scherer, 2015). To illustrate, in the aforementioned federal district court case of Riggs Investment Management Corp. v. Columbia Partners, LLC (1997), one remedy imposed by the court was the forfeiture of compensation the employee received by his former employer from the date he breached his duty of loyalty by disclosing confidential information about clients and co-workers until the day he left the former employer's employ. Furthermore, the court held that as a matter of law the former employee severed the employment relationship with his former employer when he violated the duty of loyalty and not when he actually departed from the former employer's employ (Riggs Investment Management Corp. v. Columbia Partners, LLC, 1997). Boyle (2000) and Gray (2000), however, point out that some states will not automatically award the forfeiture remedy for disloyalty; rather, these states use a balancing test to determine forfeiture by looking at the performance of the employee, the disloyal acts and the harm to the employer. The objective is to ascertain whether the employer received some value from the employee's work and whether the employee would be unjustly enriched by keeping his or her salary or wages (Gray, 2000).

In the case of VCOM International Multi-Media Corp. v. Gluck (2017) the employer (VCOM) sold projector screens online through its website ScreenStore.com and employed Mr. Gluck as a sales manager who eventually set up a competing website Screen.com while still in the employ of VCOM. VCOM eventually discovered that ScreenStore.com had hidden text links embedded within it to redirect online users who clicked on internal links to be sent to Screen.com. VCOM confronted its employee Gluck who denied any wrongdoing. Ultimately VCOM terminated Mr. Gluck and sued him for multiple claims, including breach of duty of loyalty to his employer and sought "discouragement" of salary during the period of his alleged disloyalty. The court allowed the claims to go to trial as there were genuine issues of fact in dispute, but affirmatively concluded that if such claims were proven true by VCOM, then that employer was entitled to the remedy of "discouragement" of the employee's salary.

Ultimately, it is up to a jury to apportion what part of the salary or pay should be forfeited by the employee during the period of time it is proven that the employee violated the duty of loyalty; and such an apportionment will not be disturbed on appeal if there was sufficient testimony and documentary evidence to support that a jury carefully considered the specific period of disloyalty (West Plains, LLC v. Retzlaff Grain Company Inc. (2016). Furthermore, the New Jersey Supreme Court in Kaye v. Rosefielde (2015) held that:

> *…the remedy of equitable disgorgement is available to a trial court even absent a finding that the employer sustained economic loss by virtue of the employee's disloyal conduct. In accordance with the broad discretion afforded to courts fashioning equitable remedies that are fair and practical, a trial court may order disgorgement of an employee's compensation as a remedy for a breach of loyalty in an appropriate case. If a court determines that disgorgement is an appropriate equitable remedy, it should apportion that compensation and compel disgorgement of only the compensation that the employee received during pay periods in which he or she acted in violation of the duty of loyalty (Kaye v. Rosefielde, 2015).*

At least one court has refused to extend the "faithless servant" doctrine to independent contractors who allegedly breached their fiduciary and loyalty duties to their principal. In Federal Insurance Co. v. Mertiz, Jr. (2015), the Mertiz Company was owned and operated by the defendant who was hired by Chubs Insurance Company to provide it with independent and accurate estimates of the scope and cost to repair building damage that is covered by a Chubb insurance policy. Chubb claimed that the Mertz Defendants (Mertz), from 2004 through 2010, submitted fraudulently inflated estimates on which Chubb relied to settle and pay claims to repair insured homes. According to Plaintiffs, Mertz would then solicit the insured to hire his company to make the repairs to their homes, perform the repairs at a substantially lower cost than the initial estimate provided and pocket the difference. Chubb alleged that under New York law, the Mertz Defendants were faithless servants to Chubb and by breaching their fiduciary duty owed to Chubb, the faithless servant doctrine required forfeiture of all compensation received for the entire period of their disloyalty. The trial court ruled in favour of the Mertz defendants and refused to extend the faithless servant doctrine to independent contractors. In doing so explained:

> For these reasons, absent clear guidance from New York courts on this issue, the Court declines to extend the faithless servant doctrine to independent contractors who owe a duty of loyalty to, but have no agency or employment relationship with, a defendant." To decide otherwise would risk expanding the damages recoverable in an ordinary duty of loyalty case to include all compensation received by the breaching party. It would also represent a significant departure from the original purpose and context of the faithless servant doctrine (*Federal Insurance Co. v. Mertiz, Jr.* 2015).

### Tort Damages

The breach of a fiduciary duty is regarded as a tort for which tort damages may be awarded, including monetary redress in the form of compensatory and emotional distress damages (McGowan & Company v. Roger F. Brogan, 2015, applying Texas law; Restatement (Second) of Torts, Section 874, 1979; Selmi, 2012; Reuschlein and Gregory, 1979). However, the breach of a fiduciary duty is not considered in and of itself to be an intentional tort since the violation may be unintended, for example, by means of a party’s negligence or a failure to exercise reasonable care in the performance of one’s responsibilities (DeMott, 2012). However, if the breach of the fiduciary duty was committed in an intentional and malicious, hateful or spiteful manner punitive damages may also be awarded for the breach to punish the wrongdoer and to act as a deterrent to future potential bad actors (Cavico and Mujtaba, 2014; DeMott, 2012). For example, in one federal case the court upheld a $50,000 punitive damage award against the employee for his breach of the duty of loyalty when the employee deliberately diverted a warehouse deal to a competitor of the employer when the employer was in negotiations with the competitor and where as a result the employer suffered $385,000 in actual damages (George Chapes, III v. Pro-Pac, Inc., 2012). Accordingly, if a particular jurisdiction maintains that the employer-employee relationship, perhaps involving a high-level, managerial employee, is a fiduciary one and if the duty of loyalty contravened therein by the employee amounts to a breach of the fiduciary duty, then tort damages may be recoverable by the aggrieved employer. However, if the breach is “merely” one of the generic duty of loyalty a state may not recognize such a breach as an independent tort (Grebe, 2002, citing North Carolina law). Other torts theories are possible against a disloyal employee, such as the intentional tort of conversion if misappropriation of property occurs when the employer’s confidential business documents are “pirated” away by the employee (First Financial Bank, N.A. v. Bauknecht, 2014).

### Equitable Remedies

**Injunction:** The employer in addition to the previous legal remedies can also seek equitable redress. The employer may be able to obtain an injunction against the disloyal employee if the employer can show threatened irreparable harm, for example, the use or disclosure to a competitor of confidential information or trade secrets or preventing the employee from further solicitation of the employer’s customers and/or other employees (Audio-Visual Group, LLC. v. Christopher Green, 2014; Base One Technologies, Inc. v. Mohammed Ali, 2015; Reuschlein and Gregory, 1979). The injunction can be based on the violation of trade secret law as well as a breach of the duty of loyalty (Installed Building Products, LLC v. Scott Cotrell, 2014); but the burden of proof for a preliminary injunction is high. To illustrate, in Blackbird Technologies, Inc. v. Joshi (2015), the employer (Blackbird) was in the business of creating specialized, hyper-accurate and precise internet search analytics for e-commerce companies. Blackbird employed Mr. Joshi as a technical developer who pirated new analytical technology from Blackbird and set up a competing business while still employed by Blackbird. Blackbird realized this activity when the employee posted a YouTube video disclosing its newly developed confidential technology soon to be available through the employee’s new business venture. The employer moved for an injunction and restraining order preventing the x-employee from proceeding forward with its competitive venture and deployment of “PlutoSearch” technology which paralleled Blackbird’s internet search technology. The court granted that relief noting that Blackbird carried its heavy burden of proof with credible evidence. The court explained the evidence as follows:

> *The elements of a cause of action for breach of a duty of loyalty, by analogy to a claim for breach of fiduciary duty, are as follows: (1) The existence of a relationship giving rise to a duty of loyalty; (2) one or more breaches of that duty; and (3) damage proximately caused by that breach." …the preponderance of the evidence, when examined in its entirety, demonstrates that Defendant likely breached his duty of loyalty to Blackbird. Indeed, whether or not the PlutoSearch technology is an exact copy of Blackbird's technology and regardless of whether Defendant developed the technology on his own time using his own equipment, the facts show that Defendant took actions "inimical" to his former employer when he made significant progress toward organizing a competing business, in secret, while still a Blackbird employee. The evidence also strongly suggests that Defendant started this new venture using confidential and proprietary information he had obtained from Blackbird, given the date upon which the YouTube video appeared and his sudden discovery of Blackbird source code in his possession, as well as Defendant's on-going circumvention of any order compelling the production of PlutoSearch code to a third-party expert (Blackbird Technologies, Inc. v. Joshi, 2015).*

**Replevin:** Another equitable remedy, called “replevin” under the old common law, would be an action by the employer seeking the transfer back to the employer by the disloyal employee of any property which the employee wrongfully received (Cavico and Mujtaba, 2014; Reuschlein and Gregory,1979). Selmi (2012) adds that “…in rare cases, a court might go so far as to award to the plaintiff the defendant’s business as a remedy for a breach of the duty of loyalty.”

### Constructive Trust

One of the most difficult remedies to secure, based on breach of loyalty by employees, is an employer's attempts to place the revenues generated by the subject ex-employees into a constructive trust to preserve their existence until the claims to them could be adjudicated. In the case of Wells Fargo Insurance Services USA, Inc. v. Tyndell, (2016), the employer (Wells Fargo) sued a number of ex-employees who were allegedly setting up competing insurance brokerage firms while being the employee of Wells Fargo and pirating away over 200 client accounts immediately after leaving their employ. Wells Fargo sued the x-employees for breach of their non-competition agreements and breach of their duty of loyalty seeking an injunction against them and imposition of a constructive trust upon the revenue the x-employees were receiving from the former Wells Fargo clients that were pirated away. The court denied such an extraordinary remedy as there were disputed issues of acts and then explained its preliminary ruling as follows:

> *WFIS sought relief that courts disfavour and rarely grant a mandatory preliminary injunction ordering Defendants to place revenue from certain clients in a constructive trust. Such a trust would not maintain the status quo but alter it since Defendants would be forced to create the proposed trust, place a majority of their revenue in it and they would be forbidden from accessing the vast majority of the assets in it. At oral argument, Plaintiff offered to allow Defendants access to enough money as needed to continue their business operations. Even this suggestion, however, would place a mandatory injunction on Defendants. Granting such a request demands that WFIS meet a high burden. Based on the record before the Court as detailed above, Plaintiff has not met its burden. Therefore, the Court DENIES Plaintiff's motion (Wells Fargo Insurance Services USA, Inc. v. Tyndell, 2016).*

## Related Legal Doctrines

### Covenants-Not-To-Compete

There are three legal doctrines that can arise and are often seen in duty of loyalty cases. First, covenant-not-to-compete law intersects with duty of loyalty law as well as trade secret law. A covenant-not-to-compete, also called a restrictive covenant, consists of for the purposes herein a promise made in an employment contract where the employee promises not to compete directly or indirectly against the former employee for a period of time and within a geographic area. Covenant-not-to-compete law is based primarily on state common law, though some states also have statutes on point (Cavico, Mujtaba and Muffler, 2016; Cavico and Mujtaba, 2014; Cavico, 2001). Generally, for a covenant to be deemed valid, legal and enforceable (by means of civil damages and an injunction) the time period and geographic area must be reasonable. Moreover, most states also required that the employer be able to demonstrate a legitimate business interest for the covenant, such as the employee having access to confidential business information or trade secrets, such as customer lists (Cavico, Mujtaba and Muffler, 2016; Cavico and Mujtaba, 2014; Cavico, 2001). If the covenant is overbroad in either time or place or if the employer cannot demonstrate a legitimate business reason to support the covenant, it will then be struck down by the courts as unreasonable and invalid and stricken from the contract (Cavico, Mujtaba and Muffler, 2016; Cavico and Mujtaba, 2014; Cavico, 2001). A restrictive covenant in a contract, therefore, will prevent the employee from competing against the employer when the employee leaves the employer's employ even if there is no violation of the duty of loyalty in the case where the employee was "merely" planning and preparing to leave and to compete.

Similar to covenants-not-to-compete are non-solicitation or non-piracy agreements whereby an employee promises not to solicit former clients, customers and/or employees when he or she leaves employment. Issues pertaining to these agreements also arise in duty of loyalty legal disputes. Generally, these agreements are governed by covenant law principles and thus the non-solicitation and non-piracy agreements must be reasonable as to time and place and justified by legitimate business reasons (See, for example, Instant Technology, LLC. v. Elizabeth DeFazio, 2014; Cavico and Mujtaba, 2014). If valid and enforceable these agreements will prohibit the former employee from solicitation even after leaving the employer's employ for the time and area specified.

### The Tort of Intentional Interference with Contract

In addition to the breach of a duty of loyalty the independent tort of intentional interference with contract or business relations can arise in a disloyal employee situation (Cavico and Mujtaba, 2014; Cavico, 2001). This tort required the existence of a contract or a business relationship with a defendant purposefully interferes with by improper means, for example, by improper solicitation of the employer's customers (Audio-Visual Group, LLC. v. Christopher Green, 2014; Installed Building Products, LLC v. Scott Cotrell, 2014; Cavico and Mujtaba, 2014; Cavico, 2001). Some courts require the existence of a valid and enforceable contract and not a mere business relationship for there to be a violation (Instant Technology, LLC. v. Elizabeth DeFazio, 2014). However, it is a basic principle of law that merely hiring the employees of one's competitor is not sufficient for a claim of tortious interference with contract or other legal wrong (assuming, of course, that no covenant-not-to-compete is breached and no trade secrets are misappropriated) (For example, Stuart C. Irby Company, Inc. v. Brandon Tipton, 2015). As one court stated, conduct that is "sharp or unfair" is not actionable under this tort (McGowan & Company v. Roger F. Brogan, 2015). Rather, to sustain this tort evidence will be required that the defendant employee intentionally induced a co-worker by improper means to break a contract with the employer and then work for the defendant former employee (Cavico and Mujtaba, 2014; Cavico, 2001).

### Misappropriation of Trade Secrets under the Common Law and Statutes

There also is a relationship between the employee's breach of the duty of loyalty and the employee's misappropriation of trade secrets. Trade secret law, is a separate, though related, body of law based on the common law as well as a statute, the Uniform Trade Secret Act (UTSA) which a majority of the states have promulgated into law (For example, Instant Technology, LLC. v. Elizabeth DeFazio, 2014, applying Illinois law; Cavico and Mujtaba, 2014). A trade secret consists of valuable proprietary information, such as customer lists, that one has taken reasonable steps to maintain the secrecy of, for example, by means of confidentiality and non-disclosure agreements in contracts (Cavicoorta, Muffler and Mujtaba, 2014; Cavico and Mujtaba, 2014; Cavico, 2001). Misappropriating, that is, wrongfully acquiring or using, trade secrets is a civil wrong which can be redressed by money damages and an injunction (if there is a showing or irreparable harm) as well as a criminal wrong (typically a theft crime under state law) (L-3 Communications Corporation v. Jaxon Engineering & Maintenance, Inc., 2015; Cavicoorta, Muffler and Mujtaba, 2014; Cavico and Mujtaba, 2014; Cavico, 2001).

The duty of loyalty may be breached by the employee using, disclosing or otherwise misappropriating confidential information. For example, an employee sending confidential emails to her with client information could be a breach of the duty of loyalty if the email information was used by the employee to compete with her employer (Judy Poller v. Bioscript, 2013). As such, if this information consists of legally protected trade secrets pursuant to the Uniform Trade Secrets Act then the employer has a statutory remedy, which encompasses civil damages, an injunction and criminal law penalties, typically for theft (Audio-Visual Group, LLC. v. Christopher Green, 2014; Cavicoorta, Muffler and Mujtaba, 2014; Cavico and Mujtaba, 2014; Selmi, 2012; Cavico, 2001). An example would be the aforementioned federal district court case of Shamrock Power Sales, LLC v. John Scherer (2015), where the court not only found a violation of the duty of loyalty by the employee's setting up a competing business and seeking to lure the employer's customers away but also a misappropriation of trade secrets by the employee copying and using confidential customer lists and contact information and other sensitive information, such as price lists.

It also should be pointed out that a common law legal action for breach of the duty of loyalty for misappropriating confidential information may be pre-empted and superseded by a state statute dealing with the misappropriation of trade secrets pursuant to the Uniform Trade Secrets Act (UTSA (Ameritox, LTD v. Robert Savelich, 2015; International Paper Company v. David G. Goldschmidt, 2012). Moreover, the damages recoverable under the statute may be different from and perhaps lesser than, the common law remedy, particularly if the violation of the duty of loyalty is construed as a tort wrong (Cavico and Mujtaba, 2014).

However, if the common law claims for breach of the duty of loyalty is based on other actions or conduct beyond the misappropriating of trade secrets there will not be pre-emption of the loyalty claim (Advanced Fluid Systems, Inc. v. Kevin Huber, 2014). For example, in a situation of improperly inducing co-workers to quit competing with their former employer, the breach of loyalty claim will not be pre-empted by the UTSA even if there was also a misappropriation of trade secrets (Bankers Life and Casualty Company v. Richard Miller, 2015). Another example of how an employee's breach of their common law duty of loyalty is a stand-alone claim not pre-empted by misappropriation of trade secret claims or individual states trade secret statutes, like the Tennessee Uniform Trade Secrets Act ("TUTSA"), is the case of Ram Tool & Supply Company, Inc. v. HD Supply Construction Supply Ltd., (2016). In that case, one employee actively recruited some of the employer's current employees to work for a competitor along with simultaneously pirating trade secrets from the company while in their employ. The employer sued alleging breach of the duty of loyalty along with violation of the TUTSA. The employee defendant prevailed at the trial level in its defence that the TUTSA pre-empted the breach of duty of loyalty claim. The appellate court overturned the trial court's ruling summary judgment ruling in favour of the x-employee and in doing so explained that the breach of duty of loyalty theory was broader and encompassed more conduct than the TUTSA claim. Thus, both were viable counts against the defendant x-employee which should have survived the defendant's summary judgment motion. When addressing the breach of the duty of loyalty claim the appeals court emphasized that precedent had established that:

> *Although an at-will employee is free to end his or her employment relationship and is free to compete against his or her former employer once the relationship is terminated, an employee's duty of loyalty precludes the employee from competing against the employer during the employment relationship. An employee who solicits his or her co-workers to leave their jobs to work for a competitor while the soliciting employee is still being paid by the employer is in violation of his or her fiduciary duty and duty of loyalty (Ram Tool & Supply Company, Inc. v. HD Supply Construction Supply Ltd., 2016).*

To summarize the legal analysis, we can say that inherent in any employment relationship is the legal obligation of the employee to be a loyal, trustworthy and faithful employee. If this duty of loyalty is violated the employer can seek redress against the wrongdoing employee. This legal section has sought to analyse the pertinent case law and legal and management commentary that make up the corpus of duty of loyalty employment law. In the next section, we discuss the implications that arise for employers and employees pursuant to the legal principles and their explication and illustration herein.

## IMPLICATIONS

Initially, it must be pointed out, as the discerning reader has perceived, that this area of employment law is a bit convoluted and confusing. First, it is very fact-specific as well as state-law-specific. There is first the critical issue that must be ascertained as to whether the duty of loyalty in an employment relationship in a particular state rises to the level of the fiduciary duty in the traditional principal-agent relationship. Second, assuming it does not the existence and scope of the duty loyalty must be determined pursuant to state common law. This is a challenging task indeed since one will confront general principles, several variables affecting liability, problem areas, as well as related legal doctrines with contract, tort and criminal law ramifications.

Again, as the discerning reader can perceive, there is neither clear and precise definition of duty of loyalty nor the type of conduct by the employee that will contravene that duty. There are several general principles and factors that will apply to the facts of a particular case. Important considerations derived from the case law and legal and management commentary are as follows: Was the employee's conduct direct or indirect competition, was it competition or mere business preparation, was it secret and was the employee a high-ranking employee. The application of these considerations and the conclusions derived therefrom will vary based on the law of a particular state and the facts of a particular case. Such is the nature of duty of loyalty employment law.

Generally, therefore, the employer, in contemplating litigation against the employee or former employee for breach of the duty of loyalty must ask itself several relevant questions such as: First, what is the nature of the employment relationship; second, did the employer have a reasonable expectation of loyalty from the employee; and third, did the employee's conduct contravene that expectation.

As to the important line the law draws between mere preparation and illegal competition, one federal district court, applying New York law, very nicely provided a succinct summary:

> *When an employee uses an employer's proprietary or confidential information when establishing a competing business, the employee breaches his or her…duty to the employer….Although an employee may, of course, make preparation to compete with his employer while still working for the employer, he or she may not do so at the employer's expense and may not use the employer's resources, time, facilities or confidential information; specifically, whether or not the employee has signed an agreement not-to-compete, the employee, while still employed by the employer, may not solicit clients of his employer, may not copy the employer's business records for his own use, may not charge expenses to his employer, which were incurred while acting on behalf of his own interest and may not actively divert the employer's business for his own personal benefit or the benefit of others. In addition, even in the absence of trade secret protection, employees are not allowed to copy their employer's client list and such acts have been deemed to be an egregious breach of trust and confidence (Shamrock Power Sales, LLC v. John Scherer, 2015).*

The employee, however, is permitted to resign from employment, set up his or her own business, even a competing one and further is allowed at that time to solicit business from the former employer's clients and customers, so long as the former employee does not violate any contractual provisions, such as non-disclosure and/or covenant-not-to-compete restrictions, misappropriate any trade secrets and does not defame the employer in any way.

## RECOMMENDATION

Based on the preceding case analysis, legal and management commentary and the authors own knowledge and experience the following recommendations are offered to employers and employees:

### Employers

- The employer is advised whenever possible under state law to attempt to characterize the breach of loyalty as a breach of a fiduciary duty since the latter is viewed as a tort with more expansive tort damages. Such a characterization would have greater weight when applied to higher level employees.
- The employer is advised to be wary of inserting arbitration clauses in contracts since if a breach of the duty of loyalty is viewed as a contract dispute it may be governed by the arbitration clause and the arbitration process, where the damages and right to appeal are limited.
- However, if the breach of the duty of loyalty is viewed as the violation of a fiduciary duty then a tort remedy is available, which is one that will be independent of any arbitration clause in the contract.

- The contract between the employer and employee may be able to emphasize as well as to define the duty of loyalty, for example, by spelling out the confidential nature of the employee's position.
- Similarly, the contract may be able to state the fiduciary nature of the employment relationship and thus help to create a fiduciary relationship between the employer and employee.
- The employer should use confidentiality and non-disclosure agreements to enhance contractual and trade secret protection of confidential information as well as to define the parameters of the duty of loyalty.
- Customer lists and contact information and other confidential and sensitive information, such as price lists, should be clearly designated as valuable confidential and proprietary information and then reasonable measures should be instituted to maintain the secrecy of such information so as to take advantage of trade secret law protection.
- The employer also should use non-solicitation and non-piracy agreements to contractually prevent the employee from contacting clients and customers of the employer and to further define the duty of loyalty.
- The employer also should use covenant-not-to-compete agreements to prevent the employee from unreasonably competing against the employer.
- The aforementioned contractual agreements should also specifically and explicitly cover social media and Internet communications and competition.
- The employer should use "works-for-hire" provisions within written employment agreements to set expectations with their workforce that all intellectual property developed by employees or independent contractors belongs exclusively to the employer.
- The aforementioned contractual provisions are particularly important in contracts with higher level employees who typically would have access to confidential information.
- If the duty of loyalty is violated by the employee misappropriating confidential information which rises to the level of a trade secret then the employer should utilize the remedies-civil and criminal-under the Uniform Trade Secret Act.

**Employees**

- The employee must be keenly aware of the fundamental premise of the loyalty duty, that is, to conduct the employer's business in the best interests of the employer and not the employee's own interest.
- The employee legally may explore other employment opportunities, even with competitors of the employer, while working for the employer.
- The employee is free to leave his or her employer's employment and start a separate and competing business so long as the former employee neither violates any contractual restrictions, such as confidentiality/non-disclosure agreements and/or covenants-not-to-compete, misappropriates trade secrets, nor wrongfully interferes with the former employer's business.

- The employee legally may prepare for a business, even a competing business, while in the employer's employ but the employee cannot divert the employer's customers or clients or co-workers or otherwise harm the employer.
- The employee must check if he or she is bound by any contractual provisions, for example, non-disclosure and confidentiality agreements, non-solicitation or non-piracy agreements or if there is potential for liability pursuant to trade secret law.
- The employee should inform his or her current employer of the intent to leave the firm and start a new and independent business, particularly if the new business will be competing against the employer's business or otherwise conflicting with the employer's business.
- Since the breach of the duty of loyalty may be construed in some jurisdictions as a breach of the fiduciary duty, Grebe (2002) advises that "certain classes of employees who decide to leave their jobs to compete with their employers must carefully evaluate whether they are subject to the stricter brand of fiduciary loyalty."
- The employee must be aware that this area of the law is not precise; moreover, it is an area that is very state- and fact-specific. As such, Grebe (2002) advises that "the employee should proceed with caution through this ever-gray area of the law."
- Patience is also counselled; that is, the employee should wait until he or she terminates employment with the current employer before starting a new competing business or working for a competitor of the former employer (Grebe, 2002).
- The employee may attempt to explicitly "contract out" of the duty of loyalty as is allowable, for example, under Delaware law (Rauterberg, 2017).
- Finally, since this area of the law is not precise, state- and fact-based and requires the application of general principles and criteria to particular cases the employee is strongly advised to seek legal counsel before contemplating competing against his or her current employer.

## SUMMARY

Similar to the norms of most well-intentioned and law-abiding people, the law in the United States values protects and promotes entrepreneurship, innovation, creativity, free markets and competition. The law also values individual rights, including the personal right and economic right to start a business or work for another business, even businesses in competition with one's former employer. Free markets and competition, moreover, are good for the economy and the consumer. Yet markets and competition must be open, honest and fair; and an employer is entitled to faithful and fair service by its employees. The common law duty of loyalty in the employment relationship is one legal mechanism to ensure fair competition and faithful service. This duty is violated when an employee directly competes against his or her current employer or acts adversely to the interests of his or her current employer. However, the employee can make plans to work for another employer or to embark on an entrepreneurial venture, even if in competition with his or her current employer, so long as the employee does not commit any disloyal, unethical or unfair acts. Accordingly, the courts on a case-by-case and state-by-state basis attempt to "draw the line" between permissible competition and disloyal actions. In this article, we have sought to state, explicate and illustrate key legal principles of the common law duty of loyalty, discuss their implications for employees and employers and to provide suitable recommendations to both parties to the employment relationship.

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