

EMPLOYMENT & IMMIGRATION LAW

Garden Leave Provisions

A growing trend in employment agreements

By Thomas B. Lewis and
Mark F. Kowal

American employers frequently use noncompetition agreements (noncompetes) as a means to protect and defend their business interests. Generally, a noncompete prohibits a departing employee from accepting competitive employment for a specified period of time. American courts usually enforce noncompetes only when they are reasonable and protect an employer's legitimate business interest. As many courts value free mobility of employees and open and fair competition, courts are commonly cautious when deciding the scope and/or enforceability of noncompetes. This uncertainty has created an environment where employers may be unable to sufficiently protect their interests against departing, well-trained, highly productive employees. A "garden leave provision" may effectively protect the legitimate interests of the business while not causing a financial hardship to the employee.

Garden leave was first developed by English businesses. In the employment context, garden leave, unlike a restrictive covenant, requires that the

Lewis is chair of Stark & Stark's employment group; Kowal is an associate in the group.

employee provide the employer with a specific notice period before terminating employment. (A garden leave can also be defined as requiring payment to the employee during the term of the noncompete thereby not allowing that employee to be employed in a competitive employment position during the specified time period.) Greg T. Lembrich, "Garden Leave: A Possible Solution to the Uncertain Enforceability of Restrictive Employment Covenants," *Colum. L. Rev.* 2291, 2292 (Dec. 1992). During this notice time, the employer normally does not have the employee work. Instead, the employee is paid salary and benefits, often with the expectation of not working for the employer resigned from. Since the employee remains employed, she can neither work for a competitor nor do anything else to harm or violate their duty of loyalty to the former employer.

Garden leave provisions offer many of the same benefits as traditional noncompete provisions. Garden leave will generally protect the employer from misappropriation of confidential proprietary information as well as direct competition created by the departing employee. Moreover, because the employee is still employed, she still owes a duty of loyalty to the employer. In addition, since the employee is no longer in the office, she will likely

be unable to access sensitive business information, and any information in the employee's possession often becomes out of date and of limited value when the employee resumes working for a new employer. Garden leave provisions, like traditional noncompete provisions, are driven by principles of contract, allowing employers the ability to seek injunctive relief and damages if an employee breaches the garden leave provision.

Garden Leave in New Jersey

In *Campbell Soup Co. v. Desatnick*, the U.S. District Court for the District of New Jersey favorably cited a safety net clause in a noncompetition agreement between Campbell Soup Company (Campbell) and Desatnick, one of its former employees. *Campbell Soup Co. v. Desatnick*, 58 F.Supp.2d 477 (D. N.J. 1999). Here, Desatnick sought a preliminary injunction enjoining Campbell from enforcing a 1997 noncompetition covenant preventing Desatnick from accepting employment with the Pillsbury Company (Pillsbury). Desatnick alleged that Campbell had no legitimate business interest in preventing him from joining Pillsbury as chief marketing officer. Desatnick believed he did not possess any proprietary secrets or confidential information that required protection.

The 1997 agreement contained a "safety net" provision. Under the safety net, if Desatnick was unable to find employment with a noncompetitor, Campbell would pay 100 percent

of his base monthly salary (including medical and dental benefits) beginning 90 days after his last day of employment at Campbell, and continuing for the 18-month duration of the noncompetition provision, or until Desatnick found a suitable position, if that happened sooner.

The court found the 1997 non-competition agreement reasonable and enforceable and that the agreement did not result in undue hardship to Desatnick that was disproportional to the interests Campbell was attempting to protect. Notably, the court found the safety net provision of the agreement reasonable because it cushioned the financial loss to Desatnick, and therefore, any intent by Campbell to impose punishment upon Desatnick was negated.

Garden Leave in American Courts

American employers have begun including garden leave provisions in the employment contracts of key employees. However, as garden leave is a relatively new phenomenon, there is limited case law addressing enforcement. In *Baxter International, Inc. v. Morris*, one of the first cases to examine the enforceability of a garden leave provision, the Eighth Circuit affirmed a district court ruling, refusing to stop a research scientist from working for a competitor even though his previous employer was willing to pay him during the duration of his one year noncompete agreement. The court held, "if [Morris' previous employer] paid Morris' salary for the year he would be forbidden to work by the covenant, Morris would suffer undue hardship." *Baxter International, Inc. v. Morris*, 976 F.2d 1189, 1197 (8th Cir. 1992).

Since *Baxter*, several cases involving garden leave have arisen in New York courts. These courts have upheld noncompetes with safety net clauses as well as noncompetes with provisions remarkably similar to traditional English garden leave provisions.

A New York court found the restrictive covenant reasonable "on condition that plaintiffs continue to receive their salaries for six months while not employed by a competitor." *Maltby v. Harlow Meyer Savage Inc.*, 633 N.Y.S.

2d 926, 930 (N.Y. Sup. Ct. 1995).

A New York court upheld a six-month restrictive covenant, placing significant reliance on the employee's full compensation of salary and payment of health and life insurance premiums. *Lumex Inc. v. Highsmith and Life Fitness*, 919 F. Supp. 624, 629-36 (E.D.N.Y. 1996)

The Second Circuit, applying New York law, upheld a six month noncompetition agreement that did not contain any post-employment payment provision. The court held the employer's provision of the employee-salesman's annual compensation of \$600,000, contingent upon the employee-salesman's agreement to abide by his contractual post-employment restrictions, was equivalent to the post-employment payments in *Maltby*, thereby alleviating the policy concern that noncompete provisions prevent a person from earning a livelihood. *Ticor Title Insurance Co. v. Cohen*, 173 F. 3d 63, 71 (2d Cir. 1999).

A New York court upheld a 30-day notice provision which was combined with the 90-day non-compete provision, holding that the safety-net payment provision made, "virtually nonexistent [the] concern that the former employee could lose his livelihood." *Natsource LLC v. Paribello*, 151 F. Supp. 2d 465, 472 (S.D.N.Y. 2001).

Finally, a New York court upheld a restrictive covenant containing a "sitting out" clause. The court granted the employer a five-month enforcement period of the restrictive covenant, holding that the risk to the former employee-executive of a loss of livelihood was mitigated by the continual payment of his salary. *Estee Lauder Co. Inc. v. Batra*, 430 F. Supp. 2d 158, 182 (S.D.N.Y. 2006).

Limitations to the Scope of Garden Leave

In *Bear, Stearns & Co., Inc. v. Sharon*, the U.S. District Court for the District of Massachusetts refused to issue a preliminary injunction to enforce a contractual provision requiring an employee to provide 90 days' notice of termination of employment. *Bear, Stearns & Co., Inc. v. Sharon*, 550 F.Supp. 2d 174 (D. Mass. 2008).

Here, Sharon resigned from Bear, Stearns (Bear Stearns) on March 17, 2008, and immediately accepted employment with Morgan Stanley. Bear Stearns alleged that: 1) the terms of Sharon's employment required that he give 90 days' prior written notice before resigning; 2) Sharon misappropriated Bear Stearns' confidential information; and 3) Sharon wrongfully induced employees (and clients) of Bear Stearns to leave and become employed by (or customers of) Morgan Stanley.

The court denied the request for preliminary injunction enjoining Sharon from being employed during the 90-day garden leave period for three reasons: Bear Stearns could not establish irreparable harm because its harm could be recompensed by money damages; the hardship to Bear Stearns of permitting Sharon to resume his employment with Morgan Stanley was outweighed by the risk to Sharon's "professional standing and the inability to advise his clients in times of economic turmoil"; and specific performance of the 90-day garden leave provision would require Sharon to continue an at-will employment relationship against his will.

The court distinguished garden leave from a noncompetition or nonsolicitation provision, holding that a different result might be warranted if the provision were a "simple restrictive covenant against competition or the solicitation of clients." Giving the garden leave provision full effect "would be to force Sharon to submit to Bear Stearns' whim regarding his employment activity in the near future."

Drafting Concerns for Employers

Court decisions can assist employers drafting garden leave provisions. However, many courts apply subjective standards to the enforcement of any restrictive provision. To protect long-term business interests, employers must recognize the practical, economic and legal implications of including garden leave provisions in employment contracts. Because Employers must pay the salary to their employees during the garden leave period, careful determination of the type of employee that necessitates

a garden leave provision, how many employee contracts will include a garden leave provision, and the likelihood of one or more employees being on garden leave at any one time, should be considered prior to including a garden leave provision in any employment contract.

Once an employer has decided which employees should be afforded garden leave, the garden leave provision should include the following:

1. A statement giving the employer the authority to place the employee on garden leave;
2. A statement that reserves the employer's right to exclude the employee from the workplace;
3. A statement prohibiting the employee from contacting clients and accessing or using the company's proprietary information;
4. Terms indicating what, if anything, the employee is required to do while on garden leave (noting however, the court's concern regarding involuntary servitude in *Sharon* — the less an employee on garden leave is required to do for their employer, the more likely the provision will be enforced); and
5. Terminology enjoining the employee from engaging in employment with any other employer for the duration of the garden leave.

A properly executed garden leave provision may safeguard an employer's proprietary information and allow the employer to effectively transition the business, thereby protecting the interests of the company. Employers would be wise to insure that garden leave provisions are specifically tailored to each employee, that they significantly limit the employee's responsibilities during leave and that they are reasonable in duration. Even if all factors are met, a garden leave provision will still be subject to an equitable, somewhat subjective, test by the court, concluding with whether the agreement is enforceable. ■