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PRACTICE GROUP
NEWSLETTER
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LITIGATION

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IN THIS NEWSLETTER:

Don't let the slower pace of summer keep you from staying up-to-speed on your current business practices, especially those that may help you minimize your risk of litigation. In this issue, we report on recent developments in the areas of employment, commercial and intellectual property law, along with some practical advice to help you avoid costly disputes.

"Our tradition is based on unparalleled client service, individual attention, adding value and a strategic approach to every situation."

EMPLOYMENT LAW:

DEFINING "SOLICITATION" IN RESTRICTIVE COVENANT AGREEMENTS

In *Bessemer Trust Company v. Branin*, the Court of Appeals held that an executive who sold his company and later joined a competitor could assist his new employer in a variety of ways to pitch his former clients without violating the law on non-solicitation. This is an important development for service-sector businesses and companies that acquire them.

Background

Francis S. Branin owned a company that provided financial advice to high net-worth individuals. He later sold his business to Bessemer and became an employee there. Branin ultimately left Bessemer to join Stein Roe, a rival financial advisory firm. Bessemer had not required him to sign a non-compete agreement, restrictive covenant, or agree to any post-employment restriction when Bessemer bought Branin's company, nor at any time afterward.

When Branin resigned from Bessemer, he did not inform his clients of his departure, nor did he approach them after he joined Stein Roe. Nevertheless, after Branin started working at Stein Roe, the largest client with whom he worked at Bessemer learned that Branin had left, and contacted him. The client requested a meeting with Stein Roe to decide whether his account should stay with Bessemer or follow Branin to Stein Roe. Branin arranged a meeting between the client and his new partners. Prior to this meeting, Branin assisted in developing the strategy for the meeting and provided information to his new partners about the client's needs and preferences. Branin also attended the client meeting alongside his new partners, although his role, according to the court, was limited to providing factual information in answer to the client's questions. The client ultimately decided to move his business from Bessemer to Stein Roe, and Bessemer filed a lawsuit against Branin for breach of the purchase agreement and breach of his duty of loyalty to Bessemer.

Decision

The court found that Branin's actions were not unlawful in the absence of a written restrictive covenant, and noted that a seller of a business does have several obligations to an acquirer that extend beyond the seller's employment with the acquirer. First, a seller has a common-law duty not to disparage the purchaser of the business. Second, the seller cannot explain to clients why he believes his new employer's products or services are superior to those of his prior employer, which had acquired his company. Third, a seller has an implied duty not to solicit his former clients, whose accounts were part to the goodwill he sold.

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DEFINING "SOLICITATION" IN RESTRICTIVE COVENANT AGREEMENTS *>> continued from page 1*

New York courts may not sustain improper solicitation claims unless an employer can prove that a seller and former employee actively solicited former clients.

The court analyzed Branin's actions and held that he did not "solicit" a client to join Stein Roe. The court reasoned that the client sought out Branin, and Branin's role in the meeting with the client was limited to answering the client's factual inquiries. The court further explained that although a seller of a business shall not actively solicit former clients, clients are free to choose with whom they do business. Furthermore, a seller may answer the factual inquiries from a former client, as long as the responses do not go beyond the scope of the specific information sought by the client. Because Branin had not crossed any of these lines, his actions were deemed not to have violated his duties to Bessemer.

Although the court found that Branin's actions did not constitute a solicitation, it is undeniable that his actions played a role in persuading the client to move his account from Bessemer to Stein Roe. Stein Roe would not have performed nearly as well at the client meeting without the assistance of Branin, who had intimate knowledge of the client's needs and preferences. Furthermore, although Branin's role at the meeting was limited to responding to factual inquiries, the mere presence of Branin – who had known and worked with the client for many years – surely had an influence on the client.

>> The Bottom Line

This case illustrates how easy it is for a seller and a former employee's actions to fall outside the common-law limitations on the seller's ability to solicit his clients once he joins a new firm. In both the sale-of-business and non-sale contexts, New York courts may not sustain improper solicitation claims unless an employer can prove that a seller and former employee actively solicited former clients.

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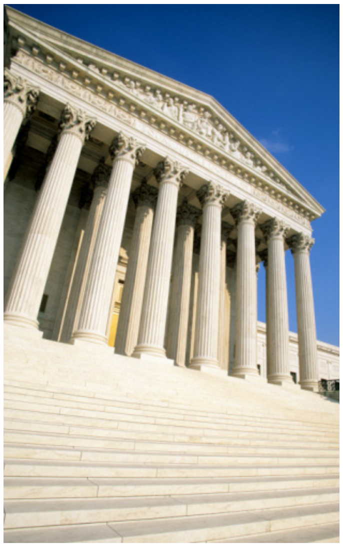
COMMERCIAL LAW:

GOING IT ALONE: AGREEING TO WAIVE THE RIGHT TO BRING A CLASS ACTION



Courts generally favor contract clauses calling for arbitration of disputes relating to the contract. This principle was reinforced by a recent U.S. Supreme Court case, *AT&T Mobility v. Concepcion,* which addressed class action waivers in arbitration agreements.

Vincent and Liza Concepcion entered into a cellular telephone contract with AT&T, which contained a provision providing for arbitration of all disputes between them. In addition, the provision required that any claims be brought on an individual, rather than a classwide, basis. AT&T provided the Concepcions with free phones, but charged them sales tax on the phones' retail value. The Concepcions attempted to bring a class action against AT&T under consumer protection statutes, and AT&T sought individual arbitration pursuant to the parties' contract.

The lower court held the contract's arbitration clause was unjust because AT&T had not shown that arbitration on an individual basis adequately substituted for class actions. The Ninth Circuit agreed. Both courts relied on a California case, referred to as *Discover Bank*, which established a "rule" in California that said that most collective arbitration waivers in consumer contracts are unjust.

Reversing the Ninth Circuit, the U.S. Supreme Court relied on the principle that "arbitration is a matter of contract." The Supreme Court also emphasized that the overarching purpose of the Federal Arbitration Act (FAA), the statute that provides for the resolution of disputes through arbitration, is "to ensure the enforcement of arbitration agreements according to their terms..." The Supreme Court concluded that California's *Discover Bank* rule unlawfully interferes with the fundamental attributes of arbitration and the purpose of the FAA. According to the Supreme Court, this is because the rule effectively allows a contracting party to get around its agreement to arbitrate individually and instead demand classwide arbitration – a procedure that is more formal, costly and complex than individual arbitration.

>> The Bottom Line

The implications of this decision are uncertain but likely far-reaching. Notably, it calls into question, if not overrules, a number of other court decisions striking down class action waivers. What is clear is the Supreme Court's general deference to the terms of arbitration agreements in contracts.

Companies drafting contracts that wish to avoid class actions should consider including provisions calling for individual arbitration of disputes and waiving class action litigation. On the flip side, consumers signing agreements should look for any clauses doing away with their right to bring a class action against the other party so that consumers understand their rights in the face of a dispute.

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COMPANIES DRAFTING CONTRACTS THAT WISH TO AVOID CLASS ACTIONS SHOULD CONSIDER INCLUDING PROVISIONS CALLING FOR INDIVIDUAL ARBITRATION OF DISPUTES AND WAIVING CLASS ACTION LITIGATION.

INTELLECTUAL PROPERTY LAW:

AN ALARMING RISE IN PATENT INFRINGEMENT CLAIMS

Companies involved in the online marketing of goods and services need to be aware of the risk of business method and software patent claims.

There has been an alarming rise in patent infringement claims asserted against advertisers, their marketing agencies, and related service providers, partly due to the increasing number of business method and software patents being issued.

Business method patents cover new ways of conducting business, and can be worded so broadly as to arguably cover a wide array of e-commerce business practices. Additionally, older business method and software patents are being bought and used by those who believe that they can extract money from companies whose activities are potentially covered by the patents they purchase. Many advertisers and their agencies have been recently hit with claims for such common online technologies as the use of drop-down menus, geo-location of retail stores, tools that allow users to manipulate their photos to make humorous videos of themselves, and the use of product placements in online ads.

Patents differ in many ways from other types of intellectual property. These differences are why companies involved in the online marketing of goods and services need to be aware of the risk of business method and software patent claims. In the past, service agreements between advertisers, their agencies and other service providers, as well as the subcontracts between the agencies and service providers, typically lumped patents in with trademarks, copyrights, rights of publicity and trade secrets. With the proliferation of business method and software patent claims being asserted for commonly used marketing techniques, this approach needs to be reconsidered. This is because patents, both legally and practically, have some unique qualities when compared to other intellectual property:

- patent infringement is a “strict liability” tort, meaning no bad faith or copying is necessary to assert a claim.
- patents are not easily searchable.
- patent rights are long-lasting, while technology is fast-changing.
- patent risk is not realistically insurable.

Therefore, the real question is not necessarily whether a patent might cover certain technology, but rather, whether someone will use it offensively to seek a license fee and/or litigate. Given these concerns, a company needs to consider carefully whether, or to what extent, it will agree to take on patent infringement responsibility for their marketing efforts where other parties are involved in the creation of the marketing materials.

>> The Bottom Line

Until adequate legislation alleviates some of these burdens, the risk of having to defend a business method and/or software patent claim is a reality of today’s e-commerce world. Patent infringement is no longer a risk limited to the technology and life sciences industries, and acknowledging patents as a unique form of intellectual property is the first step towards developing practices and procedures to reduce potential liability from patent claims.

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The case further illustrates the importance of specific contractual provisions with sellers who have client relationships and who remain employees of the acquired firm. These contractual provisions should:

- be prepared in connection with the sale, and should prohibit the seller from either soliciting or servicing, either directly or indirectly, the clients of his former firm.
- define "solicitation" more broadly by contract than *Bessemer* based upon the implied duty under the common law.

A properly drafted contractual provision might have allowed Bessemer to win in this case.

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