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# Navigating the Transition:
# What Executives Need to Know Before You Prepare to Leave

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Employees are shifting from one employer to the next at greater frequency than ever before, especially high level executives and entrepreneurs. Long gone are the days when an employee would spend her entire career with a single employer. Now, both executives and employers alike expect job-hopping during the course of business. With this trend increasing, executives and new entrepreneurs must understand their duties and obligations to their former employers before they prepare to transition to a new organization or start their own business, as the potential legal consequences are significant.

This article discusses the top concerns executives in Virginia[1] should consider before preparing to depart from their current employment. Specifically, this article discusses the following critical issues:

- Non-compete agreements and employment contracts.
- The duty of loyalty owed to an employer.
- Trade secrets and other proprietary concerns.
- Employer-client relations.
- The hiring employer's exposure to liability.

Armed with this knowledge, executives can avoid significant – and potentially devastating – legal consequences by smoothly transitioning from one employer to the next the correct way.

[1] While this article focuses on Virginia executives, much of the substance of the article may apply to executives and employees in other jurisdictions as well. Applicable state and local rules must be considered by executives and employees in other jurisdictions.

## I. What Does Your Agreement Say? Non-Competes and Other Contract Issues.

*Before* any executive decides to jump ship, she must refer to the terms of any employment agreement with her *current* employer. An employment agreement can create binding terms between the employer and executive. If the executive breaches one or more of those terms, the employer may seek to hold her liable in a breach of contract lawsuit.

The most common terms (and thus most heavily litigated) contained in this type of agreement include non-compete[2] and non-solicitation[3] terms, confidentiality and non-disclosure[4] clauses, and intellectual property rights[5] provisions. When an executive leaves for another company or a competing venture, an employer may file a breach of contract claim if it believes that the executive is impermissibly breaching a term of her employment agreement. If found liable for breaching the terms of her contract, a departing executive may find herself liable for substantial

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[2] A non-compete covenant is a promise by the employee not to work as a competitor to the employer after the employee's employment terminates. *E.g.*, "The Employee specifically agrees that for a period of 18 months after the Employee is no longer employed by the Company, the Employee will not engage, directly or indirectly, either as proprietor, stockholder, partner, officer, employee or otherwise, in the same or similar activities as were performed for the Company in any business within a 50 mile radius that distributes or sells products or provides services similar to those distributed, sold, or provided by the Company at any time during the two-year period preceding the Employee's termination of employment."

[3] A non-solicitation covenant is a promise by the employee not to attempt to solicit customers or employees of the employer after the employee's employment terminates. *E.g.*, "Employee agrees that for 18 months after Employee is no longer employed by the Company, Employee will not directly or indirectly solicit, agree to perform or perform services of any type that the Company can render ("Services") for any person or entity who paid or engaged the Company for Services, or who received the benefit of the Company's Services, or with whom Employee had any substantial dealing while employed by the Company. However, this restriction with respect to Services applies only to those Services rendered by Employee or an office or unit of the Company in which Employee worked or over which Employee had supervisory authority. This restriction also applies to assisting any employer or other third party."

[4] A non-disclosure clause is a promise by the employee not to disclose confidential information obtained in connection with her employment. *E.g.*, "Employee understands and acknowledges that the confidential information has been developed or obtained by the Company by the investment of significant time, effort and expense, and that the Confidential Information is a valuable, special and unique asset of the Company which provides the Company with a significant competitive advantage, and needs to be protected from improper disclosure. In consideration for the disclosure of the Confidential Information, Employee agrees that during employment and 3 years following termination of employment for any reason, Employee shall not directly or indirectly divulge or make use of any Confidential Information without prior written consent of the Company."

[5] An invention assignment clause is a representation by the employee that the employer owns all inventions or other work product created by the employee during the employee's employment. *E.g.*, "Employee hereby assigns and grants to the Company the sole and exclusive ownership of any and all inventions, information, reports, computer software or programs, writings, technical information or work product collected or develop by the Employee, alone or with others, during the term of the Employee's employment with the Company."

damages and attorneys' fees, and her new career opportunity destroyed or even blocked by a court order.

Often, when a breach of contract claim is filed against an executive, the issue of contract enforceability arises. Whether an employment agreement is enforceable is an issue of great importance and there is a substantial body of Virginia law dedicated purely to the issue of enforceability of employment agreements. Although this is not the primary focus of this article, a brief discussion of the issue is warranted.

Virginia case law closely scrutinizes enforceability of employment contract terms. Generally, restrictive covenants found in employment agreements are "not favored, will be strictly construed, and, in the event of an ambiguity, will be construed in favor of the employee."[6] Non-compete agreements are particularly scrutinized, as they can severely limit an employee's ability to earn a living. As such, it is the employer's burden to prove that a non-compete provision is enforceable, or no greater than necessary to protect a legitimate business interest.[7] Similarly, non-solicitation and confidentiality clauses are seen as restrictive covenants on trade and, likewise, are not favored by Virginia courts.[8]

Although courts disfavor such restrictive terms, employment agreements will be enforced against executives so long as the terms are reasonable in light of the circumstances and narrowly drawn.[9] Whether the restrictive covenants mentioned above are adjudged to be enforceable or not, the departing executive stands to lose if not cautious, either by paying damages after being found liable for breaching her employment agreement or by paying attorney's fees to defend such a suit.

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6 *Brainware, Inc. v. Mahan*, 808 F.Supp.2d 820, 825 (E.D.Va. 2011) (citing *Modern Env'ts, Inc. v. Stinnett*, 263 Va. 790, 795, 561 S.E.2d 694 (2002)).

7 *See Modern Envn'ts, Inc. v. Stinnett*, 263 Va. 491, 492, 561 S.E.2d 694, 695 (2002). In order to determine if the covenant not to compete is enforceable, courts consider a three-part test:

> [E]mployers must show that the non-compete clause (1) is narrowly drawn to protect the employer's legitimate business interest; (2) is not unduly burdensome on the employee's ability to earn a living; and (3) is not against public policy….[T]he analysis of these interrelated factors requires consideration of the restriction in terms of function, geographic scope, and duration.

*Lanmark Tech., Inc. v. Canales*, 454 F.Supp.2d 524, 528–29 (E.D.Va. 2006) (citing *Simmons v. Miller*, 261 Va. 561, 544 S.E.2d 666 (2001)).

8 *See Lasership Inc. v. Watson*, 79 Va. Cir. 205 (Fairfax Cty. 2009) (stating that non-compete, non-solicitation, and confidentiality provisions will be held to the same three-part test to determine enforceability); *see supra*, note 7.

9 *See Brainware*, 808 F.Supp.2d at 826.

In addition to the aforementioned contract terms, departing executives must also consider relevant employee handbook and policy provisions that may implicate other duties owed to the employer. While most employers do not intend for the employee policies to create binding terms like a contract, the company's policies are often a good indication as to the common law duties that are owed to the employer, such as the duty of loyalty and other statutory requirements discussed below.

Bottom line: In order to avoid a breach a contract suit, a departing executive needs to know and understand the terms of her employment agreement *before* leaving her current employer. If further inspection of these documents and provisions leaves the executive perplexed, contact an attorney for guidance.

## II. The Duty of Loyalty: Avoid Breaching Your Duty.

An executive (in fact, every employee) owes her employer the duty of loyalty.[10] The fiduciary duty of loyalty obligates executives to refrain from behaving in a manner contrary to her employer's interests while currently employed. The duty is assumed in every employment relationship and exists beyond the bounds of any employment agreement. As a result, all employees owe their employers the duty of loyalty at all times during the employment relationship. This includes the duty not to compete with her employer during her employment.[11]

Where an executive chooses to engage in business activity in direct competition with or against the interests of her employer while still employed, the executive has breached her duty of loyalty to her employer. This includes taking company property or assets, such as client lists or marketing plans. An executive should not copy company trade secrets, misuse confidential information, or solicit the employer's clients or co-workers prior to the termination of her employment.[12] That means that the executive cannot download documents from a work device or cloud onto a personal device or zip drive on her way out the door. Even if the documents or data being transferred from company property to personal property are *personal* documents, this can create the perception of impropriety, thus risking potential employer action against the executive. If an executive is concerned about appearing unethical when removing personal items from

[10] The duty of loyalty applies to *all* employees, even at-will employees. The duty of loyalty exists as a matter of law; it does not require a signed employment agreement or non-compete contract. The extent of the duty, however, may vary depending on the employee's level of responsibility and leadership within the organization.

[11] *Williams v. Dominion Tech. Partners, L.L.C.*, 265 Va. 280, 289, 576 S.E.2d 752, 757 (2003).

[12] *See Williams*, 265 Va. at 291, 576 S.E.2d at 758 (citing *Fedderman & Co., C.P.A., P.C. v. Langdon Associates, P.C.*, 260 Va. 35, 530 S.E.2d 668 (2000)).

employer property, the executive should consult Human Resources to help remove personal or permitted data off of work devices.

Conversely, it is not a breach of the duty of loyalty for an executive to begin mere preparation to compete with her former employer. For example, the planning and formation of a new organization that will directly compete with the former employer while the executive still employed is generally permitted. The executive should be wary not to use company time or property in her preparations to compete, as this may be seen as activity against the interest of her employer.[13] Whether an employee's pre-termination activity is mere preparation to compete or a breach of the duty of loyalty is a generally a fact-specific analysis made by courts on a case-by-case basis.[14] Where the executive's pre-termination activities are not "[exercised in] the utmost of good faith,"[15] or where the executive's pre-termination acts threaten to cripple the current employer's business (*e.g.* coordinated resignation *en masse*),[16] Virginia courts are likely to find that the executive breached her duty.

The importance of adhering to this duty cannot be overstated. An executive found liable for breaching this duty to a former employer risks losing all profits or benefits received as a result of the disloyal acts, even if the employer's losses are indirect. If found liable of breaching her duty, the executive may be responsible for compensatory and punitive damages.[17] Additionally, a finding of liability here may expose the executive to other theories of liability, including but not

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[13] Virginia courts have generally held that employees have no legitimate expectation of privacy when using company-issued equipment (especially when the employer maintains a clear policy to that effect), and thus, employers may search company equipment or email account, as well as messages sent from a company device. *See, e.g.*, *Hoofnagle v. Smyth-Wythe Airport Comm'n*, Case No. 1:15-CV-00008, 2016 WL 3014702 (W.D.Va, 2016).

[14] *See Fedderman & Co., C.P.A. v. Langan Associates, P.C.*, 260 Va. 35, 42, 530 S.E. 668, 672 (2000) ("We agree that, prior to resignation, these defendants were entitled to make arrangements to resign, including plans to compete with their employer, and that such conduct would not ordinarily result in liability for breach of fiduciary duty. However, the right to make such arrangements is not absolute. This right, based on a policy of free competition, must be balanced with the importance of the integrity and fairness attaching to the relationship between employer and employee or corporation and corporate director.").

[15] *Id.* at 43 (citing *Duane Jones Co. v. Burke*, 306 N.Y. 172, 117 N.E.2d 237 (1954)).

[16] *Id.* at 43 (citing *ABC Trans Nat'l Transport, Inc. v. Aeronautics Forwarders, Inc.*, 90 Ill. 186, 413 N.E.2d 1299 (finding that "the coordinated resignation of key management employees pursuant to their organized plan" resulted in the "crippling loss of half of the employer's business and major customers…was actionable breach of fiduciary duty").

[17] Additionally, employers in neighboring jurisdictions Maryland and District of Columbia may recover any compensation paid to a former employee during the period of breach under the "faithless servant" doctrine. Virginia does not apply this common law doctrine. *See Office of Strategic Services, Inc. v. Sadeghian*, No. 1:11-CV-195, 2015 WL 501958, *8 (E.D.Va. 2015).

limited to, statutory business conspiracy, interference with a business relationship or expectancy, trade secret misappropriation, discussed below.

Bottom line: An executive should be upfront and aboveboard in all of her dealings with her employer. Despite any friction between the employer and departing executive, the executive should create an exit strategy that does not implicate her duty of loyalty. The executive can do this by making sure that she does not take any company property or confidential information upon termination of her employment unless permitted, by taking care not to solicit clients or coworkers until after she has left her current employment,[18] and by steering clear of planning her next venture on company time or property. If relations with the current employer are good, the executive can even work with her soon-to-be former employer to create a plan that benefits both parties after termination.[19]

## III. Trade Secrets and Other Proprietary Information Issues.

As discussed above, a departing executive cannot take company property from her employer upon termination of employment unless the executive has been permitted to do so. This includes not only physical property, but also the employer's intellectual property, such as trade secrets. When a departing executive takes a trade secret without her former employer's permission, the executive is misappropriating that employer's property. Doing so exposes the executive to misappropriation of trade secret claims under both state and federal law.

Virginia law defines a "trade secret" as:

> information, including but not limited to, a formula, pattern, compilation, program, device, method, technique, or process that: (1) [d]erives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use, and (2) [i]s the subject of efforts that are reasonable under the circumstances to maintain its secrecy.[20]

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[18] A departing employee must pay attention to any employment agreement terms. If there is an agreement, the non-compete or non-solicitation terms of such an agreement may rule.

[19] *See, e.g.*, Geoff Williams, *Starting a Business—and Not a Legal Battle*, ENTREPRENEUR (Feb. 26, 2007), https://www.entrepreneur.com/article/175142 (discussing "how to quit your job, compete with your old boss and not get sued").

[20] Va. Code Ann. § 59.1-336. *E.g.*, computer algorithms, marketing strategies, manufacturing techniques, formulas or recipes, and client lists.

An executive who improperly "discloses or uses" trade secrets without her employer's express or implied consent may be found liable of trade secret misappropriation under the Virginia Uniform Trade Secrets Act ("VUTSA").[21] Further, an employer asserting a trade secret misappropriation claim need not prove competition between the employer and former executive to establish liability under the VUTSA.[22] The employer needs only prove that there was a trade secret and that it was misappropriated.[23]

Additionally, the newly enacted federal Defend Trade Secrets Act of 2016 ("DTSA") creates a private right of action to sue in federal district court for trade secret misappropriation. Similar to VUTSA, the DTSA defines "trade secret" expansively to include information of *all* types, so long as the owner of the trade secret takes reasonable measures to keep the information secret.[24] The DTSA does not preempt state law, thus affording aggrieved employers options as to where and how they would like to sue former executives. Penalties for misappropriation under state and federal law include injunctive relief, compensatory, and punitive damages. Additionally, attorney's fees may be awarded in cases where the misappropriation was made in bad faith.[25]

As mentioned above, in order for statutory protection to attach, a trade secret must be a *secret*, or generally not known to the public. The duty to take reasonable steps to maintain secrecy lies with the employer. If the employer fails to make reasonable efforts to maintain secrecy, *e.g.* the trade secret is posted to the Internet,[26] the employer risks losing trade secret status over the

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21 Va. Code Ann. § 59.1-336 *et seq*.

22 *See Collelo v. Geographic Services, Inc.*, 283 Va. 56, 71, 727 S.E.2d 55, 61 (2012).

23 *Id.*, 283 Va. at 68, 727 S.E. at 60.

24 *See* 18 U.S.C. § 1839(3).

25 The DTSA additionally allows for *ex parte* civil seizure in extraordinary circumstances. *See* 18 U.S.C. §1836(b)(2).

26 *See Religious Tech. Center v. Lerma*, 908 F.Supp. 1362, 1368 (E.D.Va. 1995) ("Once a trade secret is posted on the Internet, it is effectively part of the public domain, impossible to retrieve. Although the person who originally posted a trade secret on the Internet may be liable for trade secret misappropriation, the party who merely down loads Internet information cannot be liable for misappropriation because there is no misconduct involved in interacting with the Internet."). *See also, MicroStrategy Inc. v. Business Objects, S.A.*, 331 F.Supp.2d 396, 416 (E.D.Va. 2004) ("Simply because information is disclosed outside of a company does not result in the loss of trade secret status. The secrecy need not be absolute; the owner of a trade secret may, without losing protection, disclose it to a licensee, an employee, or a stranger, if the disclosure is made in confidence, express or implied. Furthermore, the requirement that the information not be generally known refers to the knowledge of other members of the relevant industry—the persons who can gain economic benefit from the secret. Finally, only reasonable efforts must be taken to maintain secrecy. Restricting access to information, implementing confidentiality agreements, and providing physical barriers to access are all reasonable efforts.").

information it seeks to protect. In such a case, an executive accused of misappropriating a trade secret will not be liable under either the VUTSA or DTSA. The departing executive, however, should not take this risk without guidance if it is unclear whether trade secret status still exists over the information or property she seeks to take.

There are other legal claims related to trade secret misappropriation that an employer can assert against a former executive, including statutory theft under the Virginia Computer Crimes Act and common law conversion. Under the Virginia Computer Crimes Act ("VCCA"), it is a crime "for any person, with malicious intent, to temporarily or permanently remove, halt, or otherwise disable any computer data, computer programs or computer software from a computer or computer network."[27] For example, accessing an employer's computer server room and altering the start-up sequence so that the server does not load properly is a violation under the VCCA if the executive or manager acts in bad faith.[28] The common law tort of conversion is the wrongful assumption or exercise of right of ownership over goods belonging to another in denial of or inconsistent with the owner's property rights.[29] If an executive takes or deprives her employer of use of its customer lists, not only could the executive be liable for trade secret misappropriation, but also conversion.[30]

Bottom line: Executives should not "take" first and ask for forgiveness later. Employers invest significant resources to develop and protect proprietary information. Departing executives who take documents and data without permission may be rewarded with a lawsuit. What is considered employer property may be unclear at times, but this is not an invitation for an executive to assume that any documents, data or information are free for the taking. Again, executives should review relevant employment agreement terms, consider the circumstances, and seek guidance for developing a safe exit strategy.

## IV. Employer-Client Relations.

One of the quickest ways to anger a former employer is to interfere with its book of business – this means clients. Mentioned above, if the former employer has an employment agreement with the departing executive, the employer may assert a breach of contract if the

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[27] Va. Code Ann. § 18.2-152.4.

[28] *See Tech Systems, Inc. v. Pyles*, No. 1:12–CV–374 (GBL/JFA), 2013 WL 4033650, *3 (E.D.Va. Aug. 6, 2013).

[29] *See Simmons v. Miller*, 261 Va. 561, 582, 544 S.E.2d 666, 679 (2001).

[30] *See id.*

executive impermissibly solicits the employer's clients in violation of the terms of the agreement. Even where there is no written agreement between former employer and executive, a departing executive still risks liability under tortious interference with a contract or business expectancy theory.

Tortious interference is a common law claim asserted when a party intentionally damages the plaintiff's – in this case former employer's – contractual or business relations. An employer may successfully bring a tortious interference claim against an ex-executive if the employer can show a valid contractual relationship, the former executive's knowledge of that relationship, the executive's intentional conduct inducing or causing the termination of that relationship, and resulting damage to the employer's contractual relationship.[31] Although not laboring under a non-compete agreement, an executive who actively seeks to recruit her former employer's clients to the executive's new competing venture, resulting in damage to the employer–client contractual relationship, may find herself the target of a tortious interference suit. In some cases, the employer may even be able to assert tortious interference with *prospective* economic advantage claim and seek damages for future lost profits, if the employer can prove that the ex-executive employed "improper methods" of interference, such as violations of statutes, regulations, or recognized common law rules.[32]

Bottom line: The mere fact that the departing executive does not have a non-compete or non-solicitation agreement with her employer does not absolve the executive of liability. For the same set of facts, not only could an executive be found liable under a tortious interference claim, she might also be found liable for breach of duty of loyalty or misappropriation of trade secrets. Further, under a tortious interference claim, the executive may be liable for punitive damages where her conduct is adjudged sufficiently egregious.

## V. Sharing Your Liability with Your New Employer.

There are additional issues to consider when an executive moves from one employer to a competitor. Though common, these situations not only inflict legal strain on the departing executive, but also on her new employer. Many of the abovementioned harms can be imputed in

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[31] *See Commerce Funding Corp. v. Worldwide Sec. Services Corp.*, 249 F.3d 204, 210 (4th Cir. 2001).

[32] *See id.* at 231—14 (citing *Duggin v. Adams*, 234 Va. 221, 360 S.E.2d 832 (1987) (discussing additional improper methods including "violence, threats or intimidation, bribery, unfounded litigation, fraud, misrepresentation or deceit, defamation, duress, undue influence, misuse of inside or confidential information, or breach of a fiduciary relationship"); *See, e.g.*, *Allen Realty Corp. v. Holbert*, 227 Va. 441, 318 S.E.2d 69 (1984) (Allegation that accountant hired to assist in plaintiff realty company's liquidation prevented plaintiff from entering into contract with prospective purchaser by intentionally failing to disclose purchaser's offer states prima facie cause of action for interference with prospective contract).

one form or another to the receiving employer if care is not taken. Two common risks to both receiving employers and executives are discussed below.

As discussed above, a company's trade secrets are protected from employee misappropriation under both state and federal trade secret misappropriation laws. Likewise, a hiring competitor may also be liable for improperly acquiring trade secrets or other confidential information through its new hires. Under the Virginia law, acquisition through improper means includes "acquisition through theft, bribery, misrepresentation, breach of a duty or inducement of a breach of a duty to maintain secrecy, or espionage through electronic means," among other methods.[33] So long as there is a trade secret that was misappropriated, as defined by statute, liability may be imputed to a hiring employer if its actions are deemed improper in the acquisition of the information. For example, if an ex-executive who now works for Employer A solicits trade secrets from employees currently with her former employer, Employer B, in violation of her employment agreement with Employer B, this could constitute a breach of contract and trade secret misappropriation. If acting within the scope of her employment with Employer A when improperly soliciting the confidential information, the executive's liability will be imputed to Employer A.[34]

Additionally, former employers may assert two types of civil conspiracy against former executives and their new employers: common law conspiracy and statutory conspiracy.[35] Common law conspiracy consists of "two or more persons combined to accomplish, by some concerted action, some criminal or unlawful purpose or some criminal or unlawful means."[36] In a civil action in this context, the unlawful purpose or means is the "damage caused by the acts committed in furtherance of the conspiracy."[37] Similarly, statutory conspiracy consists of "any two or more persons who combine, associate, agree, mutually undertake or concert together for the purpose of willfully and maliciously injuring another in [her] ... trade or business ... by any means whatever."[38] Liability under statutory conspiracy will result in treble damages *and* assignment of plaintiff's attorney's fees.[39] For example, where an executive and the hiring

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33 *MicroStrategy Inc. v. Business Objects, S.A.*, 331 F.Supp.2d 396, 416 (E.D.Va. 2004).

34 *See, e.g., id.* at 422.

35 Va. Code. Ann. §§ 18.2-499—500; *Commercial Businesses Systems, Inc. v. Bellsouth Services, Inc.*, 249 Va. 39, 453 S.E.2d 261 (1995).

36 *Commercial Businesses Systems*, 249 Va. at 48, 453 S.E.2d at 267.

37 *Id.*

38 Va. Code. Ann. § 18.2-499A.

39 Va. Code. Ann. § 18.2-500A.

 

employer act together in stealing current employer's clients or confidential information with the purpose of damaging the current employer's business, the executive and the hiring employer may be liable under either or both common law and statutory conspiracy.

Bottom line: Ultimately, it is the competing employer's duty to protect itself. An executive, however, who wishes to start, and keep, her new employment relationship on good terms should be forthcoming about any conflicts that she is bringing to the new business. Further, an executive should always seek independent counsel regarding issues of former employer relations should any conflicts of interest arise with the new employer.

## VI. Conclusion

Intimidating though they are, the laws in this arena are designed to promote fair competition between employers and executives. To transition from one employer to the next, an executive should take care to know and understand the terms of her employment agreement. Additionally, the executive must be aware that she owes her employer a duty of loyalty until the employment relationship is terminated, though some preparation to compete is generally permissible. An executive should not attempt to take documents, trade secrets, confidential proprietary information, or even clients without her soon-to-be former employer's permission. Finally, the executive should seek legal counsel before choosing to engage in acts that may infringe upon her former employer's rights. The departing executive should develop an exit plan that allows her to transition to the next venture without burning bridges with a former employer. With professionalism and honesty, an executive can navigate this transition smoothly. As with many business issues today, it is better to consult with legal counsel before preparing to leave, as opposed to having to call your attorney after you are served with a lawsuit.