COMMERCIAL LAW

IDC Defense UPDATE

DECEMBER 2013
VOL. 14 NO. 3

A publication generated by the **Illinois Association of Defense Trial Counsel** Commercial Law Committee

For this issue of the newsletter, the Commercial Law Committee asked three John Marshall Law School students to write articles. They are Sarah Flohr, Kathleen Ihlenfeld, and Marcus Morrow, each of them 3L students. Here is their work product.

Court Refuses to Enforce Restrictive Covenants

by Marcus R. Morrow

The Illinois Appellate Court recently held in *Fifield v. Premier Dealer Services, Inc.*, 2013 IL App (1st) 120327, non-solicitation and noncompetition provisions in an employment contract constituted "postemployment restrictive covenants" and the postemployment restrictive covenants were not supported by adequate consideration. *Fifield v. Premier Dealer Services, Inc.,* 2013 IL App (1st) 120327 (2013). The plaintiff former insurance agent was employed by defendant insurance company and in late October 2009 was required to sign an "Employment Confidentiality and Inventions Agreement" ("the Agreement") which included non-solicitation and noncompetition provisions. The agreement stated in pertinent part:

> "Employee [plaintiff] agrees that for a period of two (2) years from the date Employee's [plaintiff] employment terminates for any reason, Employee [plaintiff] will not, directly or indirectly, within any of the 50 states of the United States, for the purposes of providing products or services in competition with the Company [defendant] (i) solicit any customers, dealers, agents, reinsurers, PARCs, and/or producers to cease their relationship with the Company [defendant] * * * or (ii) interfere with or damage any relationship **381 *940 between the Company [defendant] and customers, dealers, agents, reinsurers, PARCs, and/or producers * * * or (iii) * * * accept business of any former customers, dealers, agents, reinsurers, PARCs, and/or producers with whom the Company [defendant] had a business relationship within the previous twelve (12) months prior to Employee's [plaintiff] termination."

Before signing the agreement, plaintiff employee negotiated with defendant employer and the parties agreed to add to the agreement a provision, which stated that the non-solicitation and noncompetition provisions would not apply if plaintiff was terminated without cause during the first year of his employment.

On October 30, 2009 plaintiff signed the offer and began his employment with defendant, however, on February 12, 2010, plaintiff resigned from his position with defendant. Shortly thereafter, plaintiff began working for a competing insurance firm.

■ *Continued on next page*

On the inside

On March 5, 2010, plaintiff filed a complaint for declaratory relief pursuant to section 2-701 of the Illinois Code of Civil Procedure (735 ILCS 5/2-701 (West 2010)) and requested that the trial court declare that plaintiff at no time had access to confidential and proprietary information while employed with defendant. The plaintiff also claimed that certain provisions of the Agreement were invalid and unenforceable, apparently because the restrictive covenants were not supported by adequate consideration because he resigned less than two years after signing the Agreement. After defendant filed responsive motions and the trial court heard oral argument, the trial court entered an order, which granted plaintiff employee motion for declaratory relief. The order stated, "The non-solicitation and non-interference provisions found within [the Agreement] are unenforceable as a matter of law for lack of adequate consideration."

On appeal, the defendant argued that the trial court erred in granting plaintiff's motion for declaratory relief. Specifically, defendant employer argued that unlike in other Illinois cases relied upon by plaintiff, plaintiff was not employed when he was asked to sign the Agreement. Thus, defendant asserted that it gave plaintiff ample consideration in the form of employment itself in exchange for the promise to abide by the non-solicitation and noncompetition provisions because plaintiff was able to avoid unemployment by accepting defendant's offer. Additionally defendant argued that although the non-solicitation and noncompetition agreement are restrictive covenants, they are not postemployment restrictive covenants because plaintiff signed the agreement before he became an employee.

The appellate court found that in order for a restrictive covenant to be valid and enforceable, the terms of the covenant must be reasonable. However, before even considering whether a restrictive covenant is reasonable, the court must make two determinations: (1) whether the restrictive covenant is ancillary to a valid contract; and (2) whether the restrictive covenant is supported by adequate consideration.

The appellate court found that in order for a restrictive covenant to be valid and enforceable, the terms of the covenant must be reasonable. *Cambridge Engineering, Inc. v. Mercury Partners 90 BI, Inc.,* 378 Ill. App. 3d 437 (2007). However, before even considering whether a restrictive covenant is reasonable, the court must make two determinations: (1) whether the restrictive covenant is ancillary to a valid contract; and (2) whether the restrictive covenant is supported by adequate consideration. *Lawrence & Allen, Inc. v. Cambridge Human Resource Group, Inc*., 292 Ill. App. 3d 131, 137, 226 Ill. Dec. 331, 685 N.E.2d 434 (1997).

In *Brown & Brown, Inc. v. Mudron*, the court stated, "continued employment for a substantial period of time beyond the threat of discharge is sufficient consideration to support a restrictive covenant in an employment agreement." *Brown & Brown, Inc. v. Mudron*, 379 Ill. App. 3d 724, 728 (2008). Illinois courts analyze the adequacy of consideration in the context of postemployment restrictive covenants because it has been recognized that a promise of continued employment may be an illusory benefit where the employment is at-will. *Id*. Generally, Illinois courts have held that continued employment for two years or more constitutes adequate consideration. *Id.* at 728–29, 320 Ill. Dec. 293, 887 N.E.2d 437. The restrictive covenant will not be enforced unless there is adequate consideration given. *Id.*

■ *Continued on next page*

In support of their argument, plaintiff argued that *Brown* was dispositive of the issues in this case. Defendant argued that the holding in *Brown* was not applicable to this case because, unlike the defendant in *Brown*, plaintiff was not employed by defendant when he signed the agreement. The Appellate court agreed with the plaintiff and pointed out, in *Bires v. WalTom, LLC*, 662 F.Supp.2d 1019, 1030 (2009), the United States District Court for the Northern District of Illinois explicitly rejected the argument that *Brown* only applies to situations where an employer amends an existing employment relationship to incorporate a restrictive covenant.

The Appellate court also disagreed with defendant's argument that the non-solicitation and noncompetition provisions in the agreement were not postemployment restrictive covenants. Illinois courts have treated restrictive covenants signed by individuals in situations similar to plaintiffs as postemployment restrictive covenants. See *Lifetec, Inc. v. Edwards*, 377 Ill. App. 3d 260, 263, (2007). In this case, the non-solicitation and noncompetition provisions in the agreement restricted plaintiff's ability to seek further employment after his employment with defendant ended. Therefore, the Appellate court found that the non-solicitation and noncompetition provisions in the agreement were postemployment restrictive covenants and for the foregoing reasons, affirmed the trial court's judgment in the plaintiff employee's favor.

Court Dismisses Fraud Claims against Franchisor

by Kathleen M. Ihlenfeld

In *Avon Hardware Company v. Ace Hardware Corporation*, 2013 Il App(1st) 130750, two franchisees alleged various claims of common law and statutory fraud against a franchisor. In this case, a franchisor developed a concept store plan called "Vision 21" to compete with "Big Box" retailers. Each franchisee entered into a franchising agreement to operate one of the franchisor's "Vision 21" stores. However, both stores eventually failed and the franchisees attribute this failure to the fraudulent negotiations that they believe the franchisor engaged in.

During their negotiations, each franchisee was given a "pro forma" document, which contained a forecast of sales and cash flow. The franchisor also provided each franchisee with a Uniform Franchising Offering Circular ("UFOC"), which contained historical data detailing the performance of its stores. In their Complaint, the franchisees allege that the franchisor used these documents to entice them into opening a "Vision 21" store even though the numbers were false and misleading.

In response, however, the franchisor contended that the franchisees' claims were baseless because each of these documents contained clauses cautioning franchisees from relying on such numbers. For example, the "pro forma" document warned franchisees that its numbers were merely estimates and should not actually be relied on. Similarly, the UFOC explained that such results should not be considered as the actual or potential results that a franchisee will achieve. The franchisor also contended that the franchisees could not pursue their claims because both signed franchising agreements that contained a clause warranting that the franchisees did not rely on any sales or profit information when entering into their agreements.

■ *Continued on next page*

Ultimately, the circuit court agreed with the franchisor and granted the franchisor's motion to dismiss. To reach its decision, the circuit court applied the "bespeaks caution" doctrine, which states that allegations of misrepresentation may be rendered immaterial if cautionary language sufficiently and specifically addresses the numbers contained in the presented materials. The court found that both documents sufficiently warned the franchisees.

On appeal, the appellate court reached a similar conclusion. Regarding the "pro forma" document, the appellate court explained that future projections are statements of opinion. Therefore, the court held that since "the basis for a fraud or misrepresentation claim must be a statement of fact," the statements in these documents are not actionable.

To reach its decision, the circuit court applied the "bespeaks caution" doctrine, which states that allegations of misrepresentation may be rendered immaterial if cautionary language sufficiently and specifically addresses the numbers contained in the presented materials. The court found that both documents sufficiently warned the franchisees.

With regard to the UFOC document, the appellate court dismissed the franchisees' claims because they failed to establish two necessary elements in support of their fraud or misrepresentation claims. First, the court found that the franchisees failed to establish that the document contained any false statements of material fact. The appellate court explained that despite the franchisees complaints, the franchisor was forthcoming with its historical information. The court noted that the UFOC clearly stated that not all stores reported their financial information, and therefore, its data only encompassed information for 37-41% of its stores. The court also noted that the franchisor properly included information detailing the number of stores that closed in the last three years. Thus, the court held that the franchisor neither made false statements of material fact nor concealed material information.

Second, the court found that the franchisees failed to establish that they reasonably relied on the information that the UFOC document contained. The court explained that not only did the franchisor represent that these numbers only represented a small portion of its stores, but also that the cautionary language these documents contained rendered any reliance by the franchisee unreasonable. Accordingly, the court concluded that since the franchisees failed to establish the necessary elements of their fraud claims, the circuit court properly dismissed the franchisees claims.

Court Upholds Forum Selection Clause

by Sarah Flohr

In *Brandt v. MillerCoors, LLC*, 2013 IL App (1st) 120431, William Brandt, Jr., as assignee for the benefit of creditors of Entec International NA, LLC, a professional parts procurement and management services company ("plaintiff"), brought breach of contract, fraudulent scheme, unjust enrichment, and commercial disparagement claims against MillerCoors, LLC ("defendant"). The trial court granted defendant's motion to dismiss based on the forum selection clause of the parties' agreement. The appellate court affirmed the trial court's dismissal of plaintiff's complaint. First, the court held that plaintiff failed to show that enforcement of the clause would be so inconvenient that plaintiff, for all practical purposes, would be deprived of its day in court if it were required to litigate an allegedly fraudulently induced contract in another jurisdiction. Second, the court found plaintiff's argument, that the clause was part of defendant's fraudulent scheme, insufficient to render it unenforceable.

On March 1, 2010, plaintiff and defendant, two companies headquartered in Illinois, entered into a contract under which plaintiff would supply defendant's Georgia, North Carolina, Virginia, and Ohio breweries with parts procurement and other services, including sending two agents from its headquarters to support each of the four breweries. Defendant's administration of the agreement primarily took place in Colorado, Wisconsin, and North Carolina. The agreement entered into by the two parties was one of defendant's standard contracts. The parties did not discuss or negotiate the Clause requiring that, "[a]ny litigation or enforcement of an arbitration award must be brought in District Court, Jefferson County, State of Colorado or the U.S. District Court for the District of Colorado," and that "[e]ach party consents to personal and subject matter jurisdiction and venue in such courts and waives the right to change venue."

> Illinois courts have held that a contract's forum selection clause is *prima facie* valid and should be honored unless the opposing party demonstrates that enforcement "will be so gravely difficult and inconvenient that [the opposing party] will for all practical purposes be deprived of [its] day in court."

After plaintiff commenced performance under the agreement, defendant began receiving complaints about plaintiff's services. In December 2010, defendant cancelled the parties' agreement. Plaintiff subsequently filed a complaint on March 30, 2011, in Illinois, despite the agreement's express provisions requiring all claims to be

■ *Continued on next page*

filed in Colorado. Defendant moved to dismiss plaintiff's complaint based on the Clause in the parties' agreement, which the trial court granted in January 2012.

On appeal, plaintiff first argued that it should be allowed to bring a cause of action in Illinois despite the express language in the parties' agreement. Illinois courts have held that a contract's forum selection clause is *prima facie* valid and should be honored unless the opposing party demonstrates that enforcement "will be so gravely difficult and inconvenient that [the opposing party] will for all practical purposes be deprived of [its] day in court." Quoting *Calanca v D & S Manufacturing Co.*, 157 Ill. App. 3d 85, 87-88 (1st Dist. 1987). Illinois courts generally consider the following factors when determining if such a clause is unreasonable: (1) the law governing the formation and construction of the contract; (2) residency of the parties; (3) location of the execution and performance of the contract; (4) location of the parties and witnesses; (5) the inconvenience to the parties of any particular location; and (6) whether the parties bargained for the clause.

The court reasoned that the only factor favoring Illinois as a forum was that both parties were headquartered in Illinois. However, plaintiff failed to show that litigation in Colorado would be so inconvenient that it would have "no real opportunity to litigate the issues in a fair manner," and that "enforcement of the clause [would be] tantamount to depriving the plaintiff access to the courts." Quoting *Dace Int'l, Inc. v. Apple Computer, Inc.*, 275 Ill. App. 3d 234, 239 (1st Dist. 1995). Therefore, the court held that plaintiff failed to meet its burden under *Calanca*.

Next, plaintiff argued that the court should not enforce the Clause because it did not have the opportunity to negotiate its language before signing the agreement. However, Illinois courts have consistently held they "will not simply 'release a sophisticated corporate entity from the consequences of its bargain.'" Quoting *Dace*, 275 Ill. App. 3d at 240. The court reasoned that plaintiff was a "sophisticated corporate entity that engaged in lengthy negotiations before entering into the agreement at issue," and "[t]he clause was not hidden or difficult to find within the contract." Therefore, plaintiff's argument that defendant was in a superior bargaining position relative to plaintiff had no merit. Additionally, there was "no indication that [plaintiff] was unaware of the clause when it signed the contract or began performance pursuant to the contract." Thus, plaintiff had the ability to forgo the parties' agreement and pursue opportunities with companies other than defendant.

Finally, plaintiff argued that the defendant fraudulently induced it to enter into the contract containing the clause. However, Illinois courts have held that, "[i]n order to invalidate a clause on the ground of fraud or overreaching, the fraud alleged must be specific to the forum selection clause itself." *IFC Credit Corp. v. Rieker Shoe Corp.*, 378 Ill. App. 3d 77, 93 (1st Dist. 2007). The clause was part of defendant's standard contract. Therefore, the court reasoned that any party entering into a valid contract with defendant would also have to agree that Colorado is the forum of choice. Furthermore, plaintiff did not argue *how* the choice of Colorado as the forum would represent fraud on the part of defendant. Therefore, the court held that the clause contained in the agreement was valid and the trial court properly dismissed plaintiff's complaint.

Marcus Rockwell Morrow is a Beazley Health Law Fellow and 3L at Loyola University Chicago School of Law. Mr. Morrow has been a law clerk with *Querrey & Harrow* since summer 2012 and has worked on a variety of matters including construction, estate, medical malpractice, insurance coverage and personal liability defense. He is a native of Los Angeles and received his B.A. in Economics from the University of California, Berkeley.

Kathleen M. Ihlenfeld is a third year law student at The John Marshall Law School. Currently, she serves as the Managing Editor for *The John Marshall Law Review*. She has also been involved in several other organizations, including the Latino Law Student Association, Phi Delta Phi, and the Academic Enhancement Program. Her anticipated graduation date is May 2014. Originally from San Diego, California, Ms. Ihlenfeld obtained her undergraduate degree from the University of Wisconsin-Madison.

Sarah Flohr is a third-year law student at The John Marshall Law School in Chicago and currently serves as a Lead Articles Editor for *The John Marshall Law Review*. She will be graduating in May 2014. Ms. Flohr wrote the third article in this publication while clerking at *Querrey & Harrow* this past fall as part of the firm's *Construction Law Quarterly* newsletter.

The Illinois Association of Defense Trial Counsel (IDC) is the premier association of attorneys in Illinois who devote a substantial portion their practice to the representation of business, corporate, insurance, professional, and other individual defendants in civil litigation. For more information on the IDC, visit us on the web at **www.iadtc.org**.

This publication was generated by the **IDC Commercial Law Committee – Bruce H. Schoumacher**, *Querrey & Harrow, Ltd.,* Chicago, Chair, and **John J. O'Malley**, *Seyfarth Shaw, LLP,* Chicago, Vice Chair.

Illinois Association of Defense Trial Counsel, PO Box 588, Rochester, IL 62563-0588, 217-498-2649, **idc@iadtc.org**