Hell Hath No Fury Like an Employer Scorned: Proceeding Simultaneously in Tort & Contract Against a Faithless Servant

By Leo K. Barnes Jr.

In light of the unbridled fiduciary duty owed to an employer,[1] after an employee resigns to join a competitor an immediate investigation concerning the former employee's activities in the months preceding resignation is warranted. If the investigation confirms pre-resignation misconduct by the former employee (*i.e.*, the employee used the employer's time, facilities or resources in a disloyal manner such as preparing for the new venture, or the compiling and dissemination of the employer's confidential information), the employer may possess an opportunity to pursue a breach of fiduciary duty claim against the former employee premised upon the faithless servant doctrine.

Assume the former employee is subject to post-employment restrictive covenants (such as a covenant not to compete or solicit customers). Savvy counsel for an employer may elect to pursue simultaneously the contractual restrictive covenant claims (relating to post-resignation competition) coupled with the fiduciary duty claims (relating to the pre-resignation misconduct). After asserting the two claims, the employer will likely be met with a motion to dismiss, claiming that the parallel pursuit in contract and tort warrants dismissal as impermissibly duplicative. Indeed, it is well settled that claims of breach of fiduciary duty which merely duplicate contract claims should be dismissed. See, e.g., *William Kaufman Org., Ltd. v. Graham & James LLP*, 703 N.Y.S.2d 439, 442 (1st Dep't 2000); Morgan v. A.O. Smith Corp., 697 N.Y.S. 2d 152, 152 (2d Dep't 1999). One key factor in pursuing viable tort and contract claims simultaneously is distinguishing the damage elements of each claim so that there is no overlap in the analysis. For example, while the fiduciary duty claim may seek redress for misconduct during the period of employment and seek disgorgement of all compensation paid from day one of disloyalty, the breach of restrictive covenant claim may focus upon post-resignation improper use of confidential information coupled with lost profits on ill-gotten gains.

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In a December 2019 decision in the matter of *Advance 2000 Inc. v. Harwick*, 2019 WL 6725977, Western District of New York Judge William Skretny denied a FRCP 12(b)(6) motion to dismiss purportedly duplicative causes of action by an employer against former employees, permitting the plaintiff to proceed simultaneously in contract and tort.

According to the decision, Advance offers full-service information technology solutions to businesses, including private cloud computing, network design and implementation, integrated communications, and consulting. Plaintiff hired Harwick as a business development executive, and Defendants Brisgone and Franz as systems engineers. All three were subject to non-compete and non-disclosure obligations and were thereafter provided with confidential information. Plaintiff alleged that beginning on May 26, 2015, all three defendants accessed plaintiff's confidential information and delivered it to one of Advance's competitors and that, at some point, defendants prepared a business plan for Squidwire group — one of Advance's competitors — that contained information stolen from Advance, which Squidwire used to Advance's detriment. Advance also alleges that all three defendants "surreptitiously work[ed] for a competing business group, i.e., Squidwire and its affiliates."

Advance alleged that defendants breached their duty of loyalty to Advance when they took actions to benefit a competitor while still employed by Advance, and that defendants breached their noncompete and nondisclosure agreements when they worked for, and delivered confidential information to, Squidwire. Defendants each filed a FRCP 12(b)(6) motion to dismiss, arguing that Advance's claims for breach of fiduciary duty were duplicative of the breach of contract claims, an argument which the court characterized as "unavailing." More specifically, the court determined that dismissal of the tort cause of action for breach of fiduciary duty was not warranted, notwithstanding the existence of the breach of contract cause of action. Indeed, the court observed that certain employee misconduct may serve as the foundation for simultaneous contract and tort claims:

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But conduct constituting a breach of contract may be actionable in tort if "a legal duty independent of the contract itself has been violated." *Nostrum*, 2014 WL 4370695, at *13. This duty can arise from the contract or from another source. *Mandelblatt v. Devon Stores*, 521 N.Y.S. 2d 672, 676 (1st Dep't 1987) ("The same conduct which may constitute the breach of a contractual obligation may also constitute the breach of a duty arising out of the relationship created by contract but which is independent of the contract itself."); see also *Fraternity Fund Ltd. v. Beacon Hill Asset Mgmt. LLC.*, 376 F.Supp.2d 385, 408 (S.D.N.Y. 2005) ("Such a duty may be independent of a contract and yet emerge from a relationship of trust and confidence created by a contract, as in the case of a lawyer and client."); *La Barte v. Seneca Res. Corp.*, 285 A.D.2d 974, 976–77, 728 N.Y.S.2d 618 (2001) ("This legal duty must spring from circumstances extraneous to, and not constituting elements of, the contract, although it may be connected with and dependent upon the contract."); *Penrose*, 682 F. Supp. 2d at 214–15 (finding a claim for both breach of fiduciary duty and breach of contract where the plaintiff alleged both that the defendant used his knowledge and skills to compete against the plaintiff and that the defendant used confidential trade secret information in violation of the non-disclosure agreement to compete).

An employee's fiduciary duty to his employer arises from the employer-employee relationship, not necessarily out of any specific contractual provisions. See *Abraham Zion Corp. v. Lebow*, 593 F. Supp. 551, 569 (S.D.N.Y. 1984), aff'd, 761 F.2d 93 (2d Cir. 1985) ("It cannot be disputed, however, that an employee has a fiduciary duty that exists independent of any contract between the parties to refrain from such conduct in certain circumstances.") Defendants' fiduciary duties may have been broader than their obligations under Advance's noncompete and nondisclosure agreements, because an employee is "prohibited from acting in any manner inconsistent with his agency or trust and is at all times bound to exercise the utmost good faith and loyalty in the performance of his duties." Lamdin, 272 N.Y. at 138. Advance alleges that defendants Harwick and Brisgone worked against Advance's interests and assisted a competitor while employed by Advance. This conduct would violate their fiduciary duty of loyalty, which exists apart from any contractual obligations, and therefore suffices to state a claim separate from Advance's breach-of-contract claims. Nostrum, 2014 WL 4370695, at *13.

Inasmuch as the duty of loyalty arises from the law of agency, faithless servant claims are not strictly limited to traditional employer/employee relationships. Rather, a viable faithless servant claim is premised upon an analysis of the nature of the relationship, not simple formulaic recitations and titles. For example, courts recognize the existence of a fiduciary duty owed by an independent contractor (see *Shaw Creations Inc. v. Galleria Enterprises Inc.*, 918 N.Y.S.2d 400 (Sup. Ct. 2010) wherein the court denied a motion to dismiss a claim for breach of fiduciary duty premised upon an independent contractor agreement, because the agreement contained provisions similar to an employment agreement) and joint venturers (see *Gramercy Equities Corp. v. Dumont*, 72 N.Y.2d 560 (1988), quoting *Meinhard v. Salmon*, 249 N.Y. 458, 463–64 (1928) joint venturers "owe each other a duty of 'finest loyalty' and honesty)."

The recovery of compensation paid to a disloyal agent may serve to level the proverbial playing field when an employer is faced with unfair competition from a former employee. Indeed, although the former employee may have been planning to depart for months, the employer, oftentimes the last to know, is tasked with immediately engaging counsel to enforce its contractual rights, a costly and distracting proposition which must be pursued at the same time that the employer is trying to stem the potential loss of business to the former employee. The prospect of recovering faithless servant damages aids the employer's cause. Hell hath no fury like an employer scorned.

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1 The employee is precluded from "acting in any manner inconsistent with his agency or trust and is at all times bound to exercise the utmost good faith and loyalty in the performance of his duties". See *Lamdin v. Broadway Surface Adver. Corp.*, 272 N.Y. 133, 138 (1936) cited in *Western Elec. Co. v. Brenner*, 1 N.Y.2d 291, 296 (1977).