LEGAL ADVISOR

A PilieroMazza Update for Federal Contractors and Commercial Businesses

Litigation

AVOIDING PITFALLS WITH RESTRICTIVE COVENANTS IN EMPLOYMENT CONTRACTS

By Brian Wilbourn

A restrictive covenant is an agreement between an employer and an employee that imposes professional restrictions on the employee after the employment relationship ends. Restrictive covenants take various forms, but commonly involve restrictions on the type of business the former employee may engage in (non-competition agreements), restrictions on contacts with the company's customers or employees (non-solicitation agreements) or restrictions on the use of information obtained during the course of employment (confidentiality or non-disclosure agreements).

While these types of agreements have become common place in employment contracts, they should not be viewed as "one-size-fits-all" provisions. The legality of restrictive covenants is one of the most heavily litigated issues in employment contracts and courts are often reluctant to enforce what are perceived to be overly burdensome restrictions on a former employee's right to earn a living. Litigating the validity of restrictive covenants can be costly and, moreover, where the restriction is found to be unenforceable, companies can be left without recourse to protect valuable business interests. Accordingly, restrictive covenants must be crafted with careful consideration to the company's industry, the nature of employment relationship, and the type of the legitimate business interests to be protected. While the circumstances of each case are different, set forth below are general considerations that should be taken into account to ensure that restrictive covenants are effective in protecting a company's business interests.

1. Tailor the restrictive covenant for individual employees

Every restrictive covenant should be drafted with specific consideration to the company's industry, how the company operates, and, most importantly, the relationship between the employer and the individual employee. Based on this information, restrictive covenants can be drafted to specifically and accurately identify the types of legitimate business interests to be protected. The types of business interests that are typically protected by restrictive covenants include customer contacts, business knowhow, training/investment in employees, and customer relations and goodwill. By tailoring each agreement to the specific duties and responsibilities of the employee, employers increase the likelihood that the restrictive covenant will be found reasonable and enforced in a meaningful way.

2. Strictly and carefully limit the restrictive covenant

While the natural inclination of both employers and attorneys alike is to craft provisions as broadly as possible so as to offer maximum protection to the employer, this impulse must be resisted. Courts are often reluctant to enforce restrictive covenants and provisions that go beyond what is necessary to protect an employer's legitimate business interests are commonly struck down. Most notably (and as most employers are probably aware), restrictive covenants must be reasonably limited in both duration and geographic scope. Accordingly, a non-compete that restricts a regional sales person from competing with the employer on a world-

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wide basis, or a non-compete that restricts a former employee for a period of fifteen years, both likely present obvious cases of over-reaching and unenforceable restrictive covenants.

Other potentially over-reaching provisions, however, are less obvious. For example, suppose a non-competition provision purported to restrict a former employee from engaging in a business that offers "predominantly similar types of products and/or services" for a period of one year and throughout a limited thirty mile radius. This seemingly narrow restrictive covenant would be subject to attack in some jurisdictions because the phrase "predominantly similar types of products and/or services" is not specific enough in identifying the types of work that the former employee is prohibited from performing during the non-competition period.

Similarly, consider a non-solicitation of employees provision which provides that for a period of six months after termination of the employment relationship, a former employee will not solicit for employment any person "who was an employee of the Company within one (1) year prior to Employee's date of termination." On its face, this provision seems narrowly drafted. Assume, however, that "Employee A" started employment with the Company on June 1, 2013, was fired for cause on September 1, 2013, and opened a pizza parlor on September 15, 2013. Also assume that "Employee B" retired from the Company on May 1, 2013. Even though Employees A and B never worked at the Company at the same time, and had never even met, Employee A could not hire Employee B to work at the pizza parlor (a completely un-related and non-competitive business) without violating the above non-solicitation provision. In certain jurisdictions, such a provision could be found unenforceable, in its entirety, because it goes beyond what is necessary to protect legitimate business interests.

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For these reasons, it is important to carefully review the language and potential effect of restrictive covenants to ensure that the covenants are tailored to protect the company's legitimate business interests, without needlessly and unintentionally restricting other post-employment activities of former employees.

3. Understand the applicable law

While the examples above identify potentially problematic restrictive covenants, it is important to recognize that the enforceability of restrictive covenants depends not only on the particular circumstances of the employment relationship, but also, in large part, on the applicable state laws. The standards for enforcement of restrictive covenants vary from state to state. In crafting restrictive covenants, it is therefore critical to understand: (i) what state's law will apply in determining the enforceability of the restrictive covenant; and (ii) how the courts of that state determine the enforceability of restrictive covenants. One of the most effective ways to ensure the enforceability of restrictive covenants is for a company (or its attorneys) to review cases from the applicable jurisdiction and craft the agreements in a manner that is consistent with restrictive covenants that have been previously reviewed and approved by the courts.

As noted above, there are a variety of factors that should be considered in drafting restrictive covenants and there is no "one-size-fits-all" approach. However, by (i) tailoring restrictive covenants based on the responsibilities of individual employees; (ii) strictly and carefully limiting the restrictions put in place; and (iii) understanding the applicable law, employers can go a long way towards protecting their business interests through meaningful and enforceable post-employment restrictions. ❐

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WHAT IS ENOUGH CONSIDERATION OF SMALL BUSINESS INTERESTS? – GAO DENIES PROTESTS AGAINST GSA CONSOLIDATION OF SMALL BUSINESS CONTRACTS

By Katie Flood

In a recent decision by the U.S. Government Accountability Office (GAO), the U.S. General Services Administration (GSA) prevailed upon its argument that the government-wide provision of office supply items in the Office Supplies Third Generation (OS3) procurement did not improperly consolidate smaller contracts. In *American Toner & Ink, et al.*, B-409528.7 *et al.* (June 2014), the GSA argued that targeted consideration of the potential impact on small businesses was sufficient, and that the consolidation would result in substantial benefits to the government. Despite the receipt of input from the SBA, which argued that the consideration given by the GSA to the economic consequences in store for small businesses if consolidation occurred was not sufficient, the GAO determined that GSA complied with statutory requirements to consider the consolidation's potential economic effect on small businesses.

The protesters—American Toner and Ink, KPaul Properties, LLC., Dolphin Blue, Inc., and Capital Shredder Corp.—argued that the GSA's plan to consolidate numerous existing contracts for office supply items into a small pool of strategically sourced, multiple award contracts would harm small businesses.

The protesters—American Toner and Ink, KPaul Properties, LLC., Dolphin Blue, Inc., and Capital Shredder Corp.—argued that the GSA's plan to consolidate numerous existing contracts for office supply items into a small pool of strategically sourced, multiple award contracts would harm small businesses. GSA undisputedly had a statutory duty to examine these impacts on small businesses before it proceeded with the planned consolidation. Specifically, Section 1331 of the Small Business Jobs Act of 2010, Pub. L. 111-240 (Jobs Act), sets forth limitations on contract consolidation. Before consolidating contracts, agencies must conduct sufficient market research, assess and analyze the impact such a contract could have on small businesses, and ensure there are sufficient opportunities for small businesses. Moreover, the agency must make a determination that the consolidation is both necessary and justified, and may do so only if the benefits of the acquisition strategy substantially exceed the benefits of each of the possible alternative contracting approaches identified by the agency.

GSA argued that OS3 was a "follow on" contracting vehicle to a prior version of the program (OS2), and therefore did not constitute a consolidation of contract requirements subject to the provisions of the Jobs Act. In addition, GSA argued that it is "contrary to law" to provide an economic analysis of the consequences on small businesses on a consolidated contract. The SBA disagreed with this construction, arguing that the plain language of the statute states that consolidation of contracts occurs when an agency combines two or more requirements of the agency for goods or services that have been provided to or performed for the agency under two or more separate contracts lower in cost than the total cost of the contract for which the offers are solicited. Here, the SBA argued that GSA combined several of the office supplies requirements of GSA and numerous other agencies, and that these functions were performed on other contracts undeniably lower in cost than the estimated $1.25 billion of the OS3 procurement. SBA also argued that there was no reason to distinguish follow-on contracts from other types of consolidated contracts under the Jobs Act. Further, SBA posited that some type of data analysis of the potential impact by OS3 on the government's small businesses suppliers should have been performed.

Ultimately, the GAO disagreed with the SBA's analysis of the Jobs Act's requirements. In denying the protests, the GAO held that the consolidation analysis performed by the GSA was sufficient. The GSA conducted market research, identified alternate contract approaches that would involve less consolidation, and set out its views on the negative impact the consolidation strategy would have on small businesses, ultimately concluding that the benefits to be gained through OS3 outweighed the potential negative impact to small business concerns. Moreover, GSA expected that 23 of the 24 OS3 contracts to be awarded would be awarded to small businesses. The GAO held that the Jobs Act did not require "a more detailed or quantified cost-benefit

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analysis to justify the agency's solicitation approach" as argued by the SBA and the protesters. The GAO found that GSA met all of the Jobs Act's requirements, and therefore denied the protests.

The GAO has now specifically found that agencies need not perform quantified cost-benefit or economic impact analysis when analyzing procurement data in the decision to consolidate contracts.

The GAO's decision in *American Toner & Ink* is potentially troubling for the small business community, as there may be a negative impact on small businesses in relation to future procurements that consolidate smaller contracts into a larger vehicle like the OS3 contract. The GAO has now specifically found that agencies need not perform quantified cost-benefit or economic impact analysis when analyzing procurement data in the decision to consolidate contracts. Instead of bolstering the Jobs Act protections for small businesses against the very real trend towards consolidating contract into larger government-wide vehicles, the GAO instead found that agencies may perfunctorily check the various requirements before reaching a general determination that the benefits of consolidation outweigh the potential negative impacts on small business concerns. Hopefully, Congress will pay attention to the implementation of this policy on the ground, and will revise the Jobs Act to give the required consolidation analysis more teeth. ❒

About the Author: Katie Flood, an associate with PilieroMazza, practices in the areas of government contracts, small business administration programs, and litigation. Ms. Flood counsels clients in a broad range of government contracting matters, as well as Administrative Procedure Act actions and complex civil litigation in federal forums. She can be reached at kflood@pilieromazza.com.

Small Business

SBA PROPOSES NEW REGULATIONS WHICH PERMIT ADVISORY SMALL BUSINESS SIZE DECISIONS

By Patick Rothwell

As many small businesses are aware, the Jobs Act and its implementing regulations have imposed new penalties on small businesses for misrepresentation of size status. The seemingly broad scope of these penalties has been a source of ongoing concern to many because SBA's size regulations regarding affiliation are often not well understood by small businesses. This is, in part, because SBA's affiliation rules are both complicated and often difficult to apply on a fact-specific basis. Moreover, many small businesses have encountered difficulties in properly calculating their average annual receipts (or employees), along with their affiliates. In short, it is possible for a firm to honestly and mistakenly certify itself as a small business, and then, at least theoretically, face the prospect of additional penalties, some of which could be quite draconian for an honest mistake (suspension and debarment, loss of 8(a) eligibility, civil and criminal penalties, and so forth).

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In order to mitigate the potential for such harshness, the National Defense Authorization Act of 2013 created an exemption to (or "safe harbor" from) such penalties for misrepresen4.4tation of size where the concern making the misrepresentation acted in good faith reliance on a written "small business status advisory opinion" (advisory opinion) from a Small Business Development Center (SBDC) or a Procurement Technical Assistance Center (PTAC). An SBDC is a center which offers one-stop assistance to individuals and small businesses by

providing a wide variety of information and guidance in central and easily-accessible branch locations. There are SBDCs in each state and the District of Columbia. A PTAC provides assistance to businesses pursuing and performing under government contracts, including contracts with the Department of Defense, other federal agencies, state and local governments, and with government prime contractors. PTACs are also located throughout the country and are a part of the Procurement Technical Assistance Program, which is administered by the Defense Logistics Agency.

On June 25, 2014, SBA issued proposed regulations implementing this new safe harbor provision. According to the proposed regulations, a concern that receives an advisory opinion may rely on that opinion for purposes of responding to federal procurements, such as submitting bids or proposals, from the date it is issued unless and until it is rejected by SBA.

The process by which an SBDC or PTAC will issue such an advisory opinion is not specified in the proposed regulation. Should an SBDC or PTAC issue an advisory opinion, it is required to submit the advisory opinion to SBA's Associate General Counsel for the Office of Procurement Law for review, along with documentation (including a written statement from the principal of the concern) in support of the opinion. SBA will then decide, within 10 business days of receipt, whether to accept or reject the advisory opinion. Or, SBA could request a formal size determination of the concern.

The advantages to these advisory opinions are self evident. If a concern receives an advisory opinion indicating it is small under the applicable size standard, it can avoid fraud or misrepresentation penalties for an inaccurate size certification in connection with submitting a bid or proposal. Thus, such an advisory opinion has the potential to be an invaluable form of protection from liability. Under the current size protest regulations, a small business contractor cannot test its strategy for remaining below applicable size standards without first being subject to a size protest and a size determination proceeding after it has already self-certified as small in response to a procurement. Thus, the advisory opinion would be a more proactive way for a concern to determine at an early stage that it is below a particular size standard.

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On the other hand, it is possible that the utility of these new regulations will be limited. Importantly, no SDBC or PTAC is required to issue any advisory opinions, and there is no funding for issuing such opinions as of yet. Thus, it remains to be seen how many such entities will actually provide this service. Furthermore, it is not clear what level of evidence of size would satisfy an SDBC or PTAC initially, and, upon review, SBA. For instance, would SBA require a firm to submit information that would otherwise be required in a formal size determination proceeding, such information that would be requested in a Form 355? If that will be the case, then seeking an advisory opinion could be an expensive, cumbersome process. And, it appears the regulations do not contemplate the advisory opinion having any impact on a size protest. Thus, a contractor would not be able to use an advisory opinion as a complete defense to a size protest. Finally, there is no timeline for an SDBC or PTAC to issue advisory opinions. Thus, it is conceivable that, in many circumstances, an advisory opinion might not be received by the concern until after the deadline for responding to a particular procurement has passed.

In sum, while it remains to be seen how this new safe harbor from penalties arising from a misrepresentation of size will be utilized, it is, nevertheless, a tool that may well be useful for apparently small businesses to protect themselves from penalties should they later be unexpectedly determined to be other than small. Comments on this proposed regulation are due on or before August 25, 2014. Small businesses should consider submitting comments in response to these proposed regulations. Such comments could include suggesting to SBA that these advisory opinions should be used as a safe harbor from additional effects of an adverse size determination beyond penalties for misrepresentation. ❐

About the Author: Patrick Rothwell, an associate with PilieroMazza, practices primarily in government contracts and litigation. Mr. Rothwell advises clients in a variety of government contract matters, including size protests before the SBA and bid protests before the GAO and the United States Court of Federal Claims. He can be reached at prothwell@pilieromazza.com.

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Attorney in the Spotlight

ALEXANDER O. LEVINE

Our Attorney in the Spotlight, Alex Levine, is an associate working in the Government Contracts and Litigation Groups at PilieroMazza. Alex counsels clients in a variety of government contract matters and advises on regulatory compliance, debarment and suspensions, government investigations, and general litigation matters.

Alex's life-long interest in learning, thinking and debating seems a natural for a legal career but it was not until shadowing for a day, his older brother who practices labor law, that Alex realized how intellectually exciting and stimulating the legal profession can be. And now he puts his intellectual curiosity and problem solving to work on a day to day basis for the firm's clients.

Not surprising for an attorney, Alex's favorite aspect of his work is winning – taking on cases, working with people, and getting a good result; this makes all the hard work and strategy development rewarding for him. He has found a good fit at PilieroMazza where he is able to handle cases from the initial interview with a client through the final outcome, something that is not always possible in larger law firms.

Born in Connecticut, Alex came to Washington, DC to attend Georgetown University for his undergraduate degree; after completing his law degree at Columbia Law School, he returned to the DC area and now calls Arlington, VA home. A Georgetown Hoyas fan first and foremost, Alex also follows the Washington Redskins and the Washington Nationals. And then too, there's Fantasy Football. With that said, it's safe to say, Alex enjoys sports.

Parents of a young family, Alex and his wife, Julie, spend much of their free time exploring the D.C. area and attending cultural and sporting events with the kids. Once a year they even manage to combine the two when they attend "Opera in the Infield," a simulcast of the Washington National Opera shown at the Washington National Ball Park.

To learn more about Alex and how he can help with your company's government contracting and litigation needs, visit his attorney page at www.pilieromazza.com or contact him at alevine@pilieromazza.com.