

AINSLIE V. CANTOR FITZGERALD, L.P.

SUMMARY AUTHORED BY ANDREW A. BROWN

Consol. C.A. No. 9436-VCZ

Court of Chancery of the State of Delaware

January 4, 2023

Key Takeaway: *Delaware courts will not enforce unreasonable restrictive covenants in the employment context, and are hesitant to “blue pencil” such agreements to make them reasonable.*

In *Ainslie v. Cantor Fitzgerald, L.P.*, six former partners sued Cantor Fitzgerald (“Cantor”) to recoup payments withheld by Cantor, which Cantor refused to turn over to the partners because they allegedly breached restrictive covenants by engaging in competitive activity within a year of leaving Cantor. The former partners claimed the restrictive covenants were unreasonable restraints on trade. Cantor moved for summary judgment under Court of Chancery Rule 56, arguing that it does not need to pay anything to the breaching former partners. Vice Chancellor Morgan T. Zurn granted in part and denied in part both parties’ motions, finding that the restrictive covenants were unenforceable as an unreasonable restraint on trade, and that Cantor could not withhold payments from the former partners for purportedly breaching unenforceable covenants.

Companies’ noncompete and nonsolicit agreements are carefully reviewed by courts to ensure they are not unreasonable restraints of trade. Contracts are read as a whole, and courts may uphold forfeiture and non-penalty liquidated damages clauses in limited partnership contracts where agreed upon in unambiguous language, as statutorily permitted by Delaware’s Limited Partnership Act. Even still, the enforceability of such remedies depends on the enforceability of the underlying promise that was breached. An agreement is not *per se* enforceable based on the parties’ signing. Delaware courts will not generally enforce provisions requiring the breaching party to pay a preset amount “untethered” to the actual damages of the breach. If the restrictive device is a condition, the Court will make a public policy determination along with an evaluation for reasonableness in determining any restraint of trades enforceability.

Words and phrases such as “if,” “provided that,” and “on the condition that,” generally indicate the parties have created a condition precedent. Delaware courts will uphold such restrictive trade covenants

when they: (1) are reasonable in geographic scope and temporal duration, (2) advance a legitimate economic interest of the party seeking their enforcement, and (3) survive a balancing of the equities. The courts favor freedom of trade over freedom of contract and are hesitant to “blue pencil” such contracts to make them reasonable.

Cantor Fitzgerald’s former partners agreed to several interlocking provisions designed to restrict them from competing, soliciting clients or employees, or using confidential information for up to four years after the partner leaves. The Court first addressed whether the restrictive devices were damages or conditions. The Court reasoned since the provisions contained the verbiage “provided,” they were conditions precedent. Cantor’s obligation to pay the former partners was to be triggered so long as the partners had not engaged in any impermissible competitive activity. However, unenforceable restrictive covenants are inactionable breaches.

The Court determined that the partnership agreements did not provide Cantor with the ability to refuse paying the former partners because the conditions were unenforceable. The former partners’ payment was subject to two conditions (1) not breaching any partner obligation, and (2) not engaging in any competitive activity for up to four years. The Court deemed the former unenforceable for three reasons. First, the global restrictions for up to four years were unreasonable in geographic scope and temporal duration. Second, prohibition against competitive activities not only against Cantor, but also to any affiliated entities provided an unreasonable scope of protection to Cantor’s economic interests. This was further aggravated by the broad language providing that a breach is committed by conduct that “is or could be considered” a breach.¹ Third, the Court reasoned that the contracts were overbroad and risky for former partners to find any employment in the financial service field; It determined the restrictions did not survive the balancing of the equities. Accordingly, the no breach restrictive covenants are unenforceable.

The Court found the forfeiture-for-competition provisions to be unreasonable restraints of trade as well. After determining that the reasonableness standard shall apply, the Court deemed the provisions unenforceable for the same three reasons as outlined above: unreasonable geographic and temporal scope, no protection of a legitimate economic interest, and failure to survive the balancing of the equities. Cantor’s duty

¹ The former partners are considered to have breached the contract when Cantor unilaterally determines they have breached, even though a breach may not have occurred.

to pay the former partners, therefore cannot be conditioned on the ‘breach’ or competitive activity of the former partners.²

Vice Chancellor Zurn denied Cantor’s motion for summary judgment and granted in part the former partners motion, finding that all of the restrictive covenants were unenforceable as unreasonable restraints on trade, and that Cantor could not withhold payments owed to former partners for breaching unenforceable restrictive covenants.

² Ainslie is not entitled to his base amount (separate from the conditioned payment) because he failed to sign a release. The partnership agreement permits Cantor to request releases in connection with the payment of a withdrawing partner’s base amount.

