NO. COA14-185

NORTH CAROLINA COURT OF APPEALS

Filed: 5 August 2014

Beverage Systems of the Carolinas, LLC,

Plaintiff,

v.

Iredell County
No. 12 CVS 1519

Associated Beverage Repair, LLC, Ludine Dotoli and Cheryl Dotoli,

Defendants.

Appeal by plaintiff from order entered 3 October 2013 by Judge A. Robinson Hassell in Iredell County Superior Court. Heard in the Court of Appeals 20 May 2014.

Jones, Childers, McLurkin & Donaldson, PLLC, by Kevin C. Donaldson and Dennis W. Dorsey, for plaintiff-appellant.

Eisele, Ashburn, Greene & Chapman, PA, by Douglas G. Eisele, for defendants-appellees.

HUNTER, Robert C., Judge.

Plaintiff timely appeals from an order entered 3 October 2013 granting defendants' motion for summary judgment. After careful review, because the trial court had express authority to revise the restrictions of the non-compete agreement, we reverse the trial court's order and remand for the trial court to revise the geographic area covered by the non-compete to include those

areas necessary to reasonably protect plaintiff's business interests. Furthermore, since there is a genuine issue of material fact as to whether Ludine Dotoli violated the revised non-compete, we reverse the order granting summary judgment on the breach of contract claim and remand for trial. Finally, because plaintiff presented evidence showing a genuine issue of material fact for the remaining tort claims and request for injunctive relief, we reverse the order granting defendants' motion for summary judgment and remand for trial.

Background

The pertinent facts alleged in plaintiff's complaint are as follows: In 2009, Mark Gandino ("Gandino") created and organized Beverage Systems of the Carolinas, LLC, a company that supplies, installs, and services beverage products and beverage dispensing equipment in North Carolina ("plaintiff"). Beginning in 2008 and continuing through 2009, Gandino negotiated with Thomas and Kathleen Dotoli, the parents of defendant Ludine Dotoli ("Ludine")[1] (collectively, Thomas, Kathleen, and Ludine are referred to as "the Dotolis"), about the potential purchase of the business and assets of Imperial Unlimited Services, Inc.

[1] Throughout their pleadings and brief, plaintiff and defendants refer to Mr. Dotoli as "Ludine" even though it appears from his affidavit that his name is spelled "Loudine." For consistency, we use the same spelling as the parties in this opinion.

("Imperial") and Elegant Beverage Products, LLC ("Elegant") (collectively, Imperial and Elegant are referred to as "the businesses"). On or about 20 July 2009, plaintiff entered into an "Asset Purchase Agreement" (the "Agreement") with Elegant, Imperial, and the Dotolis. The Agreement provided for the sale of Imperial's and Elegant's assets, trade names, customer lists, accounts receivable, current customers and customer contracts, all equipment, and real property.

As part of the Agreement, Thomas, Kathleen, and Ludine agreed to execute a "Non-Competition Agreement" (the "non-compete"). Specifically, section 1 of the non-compete provided that:

> Subject to the provisions of Section 6 hereof, Seller and Shareholder shall not, from the effective date of the Asset Agreement in the states of North Carolina or South Carolina until the earlier of (i) October 1, 2014 (the "Non-Competition Period"), or (ii) such other period of time as may be the maximum permissible period of enforceability of this covenant (the "Termination Date"), without the prior written, consent of Purchaser, directly or indirectly, for himself or on behalf of or in conjunction with any person, partnership, corporation or other entity, compete, own, operate, control, or participate or engage in the ownership, management, operation or control of, or be connected with as an officer, employee, partner, director, shareholder, representative, consultant, independent contractor, guarantor, advisor

> or in any other manner or otherwise, directly or indirectly, have a financial interest in, a proprietorship, partnership, joint venture, association, firm, corporation or other business organization or enterprise that is engaged in the business of the Purchaser or any of its respective affiliates or subsidiaries on behalf of clients (the "Business").

The non-compete went on to say that:

> If, at the time of enforcement of any provisions of Sections 1, 3 or 4 hereof, a court holds that the restrictions stated herein are unreasonable under circumstances then existing, the parties hereto agree that the maximum period, scope or geographical area that are reasonable under such circumstances shall be substituted for the stated period, scope or area, and that the court shall be allowed to revise the restrictions contained in Sections 1, 3 and 4 hereof to cover the maximum period, scope and area permitted by law.

The Dotolis executed the non-compete at the closing on 30 September 2009. Plaintiff claimed that it collectively paid the Dotolis, Imperial, and Elegant $10,000 as consideration for the non-compete.

In March 2011, plaintiff learned that Ludine's wife Cheryl Dotoli ("Cheryl") had created defendant Associated Beverage Repair, LLC, ("Associated Beverage") (for purposes of this opinion, Associated Beverage, Ludine, and Cheryl are collectively referred to as "defendants") and that Ludine was

the manager of Associated Beverage. Moreover, plaintiff alleged that it found out that Ludine was soliciting business from plaintiff's existing customers, specifically PF Chang's and Bunn-O-Matic.

On 8 July 2013, plaintiff filed an amended complaint alleging the following causes of action: (1) breach of the non-compete against Ludine; (2) a request for preliminary and permanent injunctive relief against Ludine; (3) tortious interference with contract against all defendants; (4) unfair and deceptive practices against all defendants; (5) tortious interference with prospective economic advantage against all defendants; and (6) punitive damages. On 11 September 2013, defendants filed a motion for summary judgment as to all causes of action. In support of their motion, defendants filed an affidavit by Ludine claiming that "the deepest penetration by either Elegant or Imperial for the conduct of their business into South Carolina was Rock Hill . . . and to Spartanburg," and the "western-most penetration" included Gaffney. Furthermore, Ludine averred that in North Carolina, the furthest west the companies' business went was Morganton. The eastern-most penetration was to Wake County. Finally, Ludine denied contacting, communicating, or in any way inducing any prior

customers of Imperial or Elegance or present customers of plaintiff into switching their business to Associated Beverage.

The matter came on for hearing on 30 September 2013. On 3 October 2013, the trial court entered an order granting defendants' motion for summary judgment as to all claims. Plaintiff timely appealed.

Standard of Review

"Our standard of review of an appeal from summary judgment is de novo; such judgment is appropriate only when the record shows that there is no genuine issue as to any material fact and that any party is entitled to a judgment as a matter of law." *In re Will of Jones*, 362 N.C. 569, 573, 669 S.E.2d 572, 573 (2008) (internal citations omitted).

Arguments

I. The Non-Compete Agreement

Plaintiff first argues that the trial court erred in granting summary judgment on its breach of contract claim against Ludine. Specifically, plaintiff contends that the non-compete is valid as a matter of law and that there is an issue of material fact as to whether Ludine violated it. In the alternative, should the Court determine that the non-compete is unenforceable as to South Carolina, plaintiff argues that the

non-compete may still be enforced in North Carolina based on the "blue pencil doctrine." Because the trial court had express authority to revise the territorial restrictions of the non-compete pursuant to the terms of the agreement, we reverse the trial court's order granting summary judgment and remand this issue for the trial court to revise the geographic territories to include those areas reasonably necessary to protect plaintiff's business interests acquired by the purchase of Elegant and Imperial. Furthermore, there is a genuine issue of material fact as to whether Ludine violated the terms of the non-compete for the jury to resolve.

> It is the rule today that when one sells a trade or business and, as an incident of the sale, covenants not to engage in the same business in competition with the purchaser, the covenant is valid and enforceable (1) if it is reasonably necessary to protect the legitimate interest of the purchaser; (2) if it is reasonable with respect to both time and territory; and (3) if it does not interfere with the interest of the public.

Jewel Box Stores Corp. v. Morrow, 272 N.C. 659, 662-63, 158 S.E.2d 840, 843 (1968). Whether a covenant not to compete is reasonable is a matter of law to be decided by the court. *Id.* at 663, 158 S.E.2d at 843. "Greater latitude is generally allowed in these covenants given by the seller in connection

with the sale of a business than in covenants ancillary to an employment contract." *Seaboard Indus., Inc. v. Blair*, 10 N.C. App. 323, 333, 178 S.E.2d 781, 787 (1971). Here, only the first two elements need to be addressed since defendants did not argue before the trial court nor on appeal that the non-compete interfered with the interest of the public.

A. Legitimate Interest

"A covenant must be no wider in scope than is necessary to protect the business of the employer." *Hartman v. W.H. Odell & Associates, Inc.*, 117 N.C. App. 307, 316, 450 S.E.2d 912, 919 (1994) (internal quotation marks omitted).

Here, the scope of prohibited employment activities in the non-compete is reasonably necessary to protect plaintiff's business. In his affidavit, Ludine stated that he had not only been the creator and owner of Elegant, but he had also been the "principal technician" of Imperial. Thus, his employment activities for the businesses would have included both employee ones and activities related to management, operation, and control. The non-compete prohibits Ludine from competing, owning, managing, operating or controlling, or be connected to someone who has a financial interest in any business involved in the beverage dispensing or servicing industry. Thus, the non-

compete prohibits Ludine from engaging in employment activities he used to perform for Elegant and Imperial, and the scope of the non-compete reasonably protects a legitimate business interest of plaintiff.

B. Time and Territory Reasonableness

The non-compete restricted Ludine's activities for a five-year period following the sale of Elegant and Imperial. Although our Court has stated that "[a] five-year time restriction is the outer boundary which our courts have considered reasonable" and has noted that five-year restrictions "are not favored" in employment contracts, *Farr Assocs., Inc. v. Baskin*, 138 N.C. App. 276, 280, 530 S.E.2d 878, 881 (2000), "[i]n cases where the covenants not to compete accompanied the sale of a trade or business, time limitations of ten, fifteen and twenty years, as well as limitations for the life of one of the parties, have been upheld by the Supreme Court of North Carolina[,]" *Seaboard Indus.*, 10 N.C. App. at 335, 178 S.E.2d at 788. Furthermore, the five-year restriction was reasonable based on Imperial's past business presence in the industry. Imperial had been operating since 1999. In fact, plaintiff recognized how valuable Imperial's presence was in the beverage

dispensing industry and specifically purchased its "goodwill" for $100,000. Accordingly, the time restraint was reasonable.

With regard to the reasonableness of the territory, this Court has noted that

> to prove that a geographic restriction in a covenant not to compete is reasonable, an employer must first show where its customers are located and that the geographic scope of the covenant is necessary to maintain those customer relationships. A restriction as to territory is reasonable only to the extent it protects the legitimate interests of the employer in *maintaining* its customers. The employer must show that the territory embraced by the covenant is no greater than necessary to secure the protection of its business or good will.

Hartman, 117 N.C. App. at 312, 450 S.E.2d at 917 (internal citations omitted).

Here, the non-compete was limited to North and South Carolina. Ludine's affidavit stated that Imperial's and Elegant's combined business extended from Wake County to Morganton in North Carolina. In South Carolina, Ludine averred that their business only reached as deep as Rock Hill and Spartanburg and as far west as Gaffney. Consequently, the geographic area covered by the non-compete was not limited to places where Elegant and Imperial had former customers and included areas not necessary to maintain plaintiff's customer

relationships; thus, it was unreasonable.[2] Plaintiff requests that should the Court find that the geographic territory in the non-compete is overly broad, the Court should enforce the non-compete only as to North Carolina under the "blue pencil doctrine."

North Carolina has adopted the "strict blue pencil doctrine":

> When the language of a covenant not to compete is overly broad, North Carolina's "blue pencil" rule severely limits what the court may do to alter the covenant. A court at most may choose not to enforce a distinctly separable part of a covenant in order to render the provision reasonable. It may not otherwise revise or rewrite the covenant.

Hartman, 117 N.C. App. at 317, 450 S.E.2d at 920. Under this doctrine, the trial court may use its inherent power to enforce the reasonable, divisible provisions of the non-compete.

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[2]It should be noted that any area in which plaintiff itself had former or existing customers would also be reasonable to include in the non-compete. However, defendants contended in their motion for summary judgment that "[t]here is no pleading or proof that [plaintiff] operated anywhere in North Carolina or South Carolina prior to concluding purchase of the assets of Imperial and Elegant[.]" Plaintiff did not refute this nor did it provide any evidence in the record that it either had been operating in North or South Carolina prior to the acquisition or that it has existing customers it did not acquire from Imperial or Elegant. Therefore, for purposes of reasonableness, only former customers of Imperial and Elegant will determine the scope of the territory.

Welcome Wagon Int'l, Inc. v. Pender, 255 N.C. 244, 248, 120 S.E.2d 739, 742 (1961).

We agree with plaintiff that, under the "blue pencil doctrine," the trial court could have, but chose not to, strike the unreasonable territorial provisions of the non-compete. However, the trial court had authority to enforce the non-compete through paragraph six of the non-compete which specifically and expressly gave the trial court authority to "revise the restrictions . . . to cover the maximum period, scope and area permitted by law." In other words, the trial court's ability to revise the non-compete is not subject to the restrictions of the "blue pencil doctrine" which prohibits a trial court from revising unreasonable provisions in non-compete agreements. Instead, here, the parties included a specific provision in the non-compete—specifically, paragraph six—enabling the trial court to revise the non-compete. Given the fact that non-competes drafted based on the sale of a business are given more leniency than those drafted pursuant to an employment contract since the parties are in relatively equal bargaining positions, the trial court should not have held the entire non-compete unenforceable nor should the trial court's power to revise and enforce reasonable provisions of the non-

compete be limited under the "blue pencil doctrine." Instead, the trial court should have invoked its power under paragraph six and revised the non-compete to make it reasonable based on the evidence before it.

The facts of this case are distinguishable from those in which the trial court's authority to revise a non-compete is substantially limited by the "blue pencil doctrine" because those non-competes did not give the trial court express authority to revise the agreements. *See Hartman*, 117 N.C. App. at 318, 450 S.E.2d at 920 (ruling that the non-compete "could not be saved by 'blue penciling'"); *Manpower of Guilford Cnty., Inc. v. Hedgecock*, 42 N.C. App. 515, 523, 257 S.E.2d 109, 115 (1979) (noting that "th[e] Court cannot in the absence of clearly severable territorial divisions, enforce the restrictions only insofar as they are reasonable" under the "blue pencil doctrine"). In contrast, pursuant to the sale of a business, these parties, who were at arms-length with equal bargaining power, agreed to allow the trial court to revise the non-compete to make it reasonable, and the trial court should have done so. In sum, unlike previous cases, the parties here specifically contracted to give the court power to revise the

scope of the non-compete should part of it be determined to be unenforceable.

While this precise issue has not arisen in our Courts, i.e., the right of a trial court to revise the provisions of a non-compete based on the express language of the contract for the sale of a business, this Court has noted that similar language has appeared in a franchisor-franchisee contract in *Outdoor Lighting Perspectives Franchising, Inc. v. Harders*, __ N.C. App. __, 747 S.E.2d 256 (2013). In *Outdoor Lighting*, __ N.C. App. at __, 747 S.E.2d at 261, the franchise agreement between the parties gave the franchisor the right to reduce the scope of the non-compete, a right which the franchisor attempted to invoke. In looking at this particular provision, the Court noted that "it appears, given the language of the agreement, that [the franchisor] had the right to modify the non-competition provision in this manner and exercised this authority in an appropriate manner." *Id.* at __, 747 S.E.2d at 265, n.3. However, the Court was not required to "determine the effectiveness of [that] exercise in private 'blue penciling'" because the modified geographic scope was still unreasonable. *Id.* Although *Outdoor Lighting's* holding does not directly affect the outcome in this case, it indicates a willingness of

our Courts to recognize and enforce revised non-compete agreements when the parties contract for the right to revise a non-compete outside the employment context.

Finally, in recognizing the importance of allowing parties who agree that provisions of a non-compete may be revised in an effort to enforce them, we believe that this practice makes good business sense and better protects both a seller's and purchaser's interests in the sale of a business. It not only protects the business interests of the purchaser, which is a notable concern especially in cases where the seller, similar to Elegant and Imperial, has spent a substantial amount of time building up goodwill in a particular industry, but it also allows the seller to make more money than it would have had it just sold the assets of the business. This is especially true in North Carolina where our Supreme Court has been unwilling to adopt a more flexible approach to the "blue pencil doctrine," leaving the courts with few options to try to enforce non-competes in a rapidly changing economy.[3] In addition, potential buyers may be reluctant to buy a business not only if a seller

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[3] Judge Steelman highlighted this issue in his concurring opinion in *MJM Investigations, Inc. v. Sjostedt*, 205 N.C. App. 468, 698 S.E.2d 202, 2010 WL 2814531, *5 (No. COA09-596) (July 20, 2010) (unpublished), noting that: "The law of restrictive covenants should be re-evaluated by our Supreme Court in the context of changing economic conditions."

was unwilling to sign a non-compete but also if that non-compete could not be modified and enforced by the courts. As a final note, it is important to remember that, here, pursuant to the sale of Imperial and Elegant, Ludine agreed to sign the non-compete and was compensated for that agreement as well as getting, arguably, a higher price for the businesses' assets. Then, after allegedly violating the non-compete and being sued by plaintiff, he asked the courts to hold the negotiated-for non-compete invalid.

In support of its conclusion that the trial court could not have revised the non-compete despite the fact that paragraph six explicitly gave it the power to, the dissent notes that the language of paragraph six limits the trial court's authority to revise to that "permitted by law." Thus, according to the dissent, paragraph six "by its very terms makes the 'blue pencil' doctrine applicable." However, this interpretation of the language of paragraph six would construe the provision meaningless. By this logic, the parties would be giving the trial court authority to revise the agreement but, in the same sentence, restrict its power under the "blue pencil doctrine" which expressly prohibits any and all revisions by the trial court.