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NOTES

Giving the Green Light to Silicon Alley Employees: No-Compete Agreements between Internet Companies and Employees under New York Law

Dan Messeloff*

INTRODUCTION

Once upon a time, in a small neighborhood in London, there lived a baker named Mr. Reynolds. One day, a man named Mr. Mitchel approached Mr. Reynolds and offered to rent Mr. Reynolds' bakery from him. Mr. Reynolds agreed to rent the bakery to Mr. Mitchel for five years, and promised not to work as a baker in the area during that time, so as not to take customers away from Mr. Mitchel. If Mr. Reynolds broke the contract and opened a bakery nearby, he would have to pay Mr. Mitchel fifty pounds. Shortly after Mr. Mitchel began running the bakery, Mr. Reynolds did indeed open another bakery in the area. Mr. Mitchel sued Mr. Reynolds for fifty pounds, arguing that Mr. Reynolds had broken their agreement. Mr. Reynolds claimed in response that the contract was illegal, since he had been trained to be a baker, and the law should not prevent him from working as one.¹

Continuing the story, the judge found that the contract between Mr. Mitchel and Mr. Reynolds was in fact valid. "Where a contract for restraint of trade appears to be made upon a good and adequate consideration so as to make it a proper and useful contract, it is good," wrote Judge Macclesfield.² "[V]olenti no fit injuria, a man may, upon a valuable consideration, by his own consent, and for his own profit, give over his trade; and part with it

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¹ See *Mitchel v. Reynolds*, 24 Eng. Rep. 347 (Q. B. 1711).

² *Id.* at 349.

to another in a particular place.”³ Because of the agreement he had signed with Mr. Mitchel, and because he received money in exchange for the use of his bakery, Mr. Reynolds had to comply with the contract.⁴ Since he broke the agreement, Mr. Reynolds had to pay the fifty pounds.⁵

In his opinion, Judge Macclesfield discussed similar contracts, ones made in employment agreements (as opposed to business transactions, such as in Mr. Mitchel’s case).⁶ While the court had upheld the contract between Mr. Mitchel and Mr. Reynolds, it stated that it would not necessarily do so if it had been made between an employer and an employee.⁷ Such restraints, commonly referred to as no-compete agreements,⁸ are subject to “great abuses” by employers, who are “perpetually labouring for exclusive advantage in trade, and to reduce it into as few hands as possible.”⁹ More specifically, the court seemed wary of those employers “who are apt to give their apprentices much vexation on this account, and to use many indirect practices to procure such bonds from them,” to protect themselves from competition when their employees “set up for themselves.”¹⁰ In this light, the court held that, while the agreement binding Mr. Reynolds was valid, “[i]n all restraints of trade, where nothing more appears, the law presumes them bad;” only “if the circumstances are set forth, that presumption is excluded, and the Court is to judge of those circumstances accordingly; and if upon them it appears to be a just and honest contract, it ought to be maintained.”¹¹

Within the tale of Mr. Mitchel and Mr. Reynolds lie the common law origins of restrictive covenants and the modern no-compete agreement. A no-compete agreement, normally contained within a general employment contract, states that the employee shall not work for a competitor or, similar to the agreement between Mr. Reynolds and Mr. Mitchel, shall not set up a competitive business

³ *Id.*

⁴ *See id.* at 352.

⁵ *See id.*

⁶ *See id.* at 350.

⁷ *See id.* at 352.

⁸ “No-compete agreements” have also been referred to as noncompete agreements, noncompetition agreements, and agreements not to compete.

⁹ *Mitchel*, 24 Eng. Rep. at 350.

¹⁰ *Id.* at 352.

¹¹ *Id.*

for a specified period of time in a specified geographical area.¹² Balancing the competing interests of employers and employees, modern courts have deliberated the same factors and concerns as were expressed in *Mitchel*.¹³ Indeed, the case offers one of the first applications of the “rule of reason” to restraints of trade, even if it was at a time when competition beyond a local scale such as a neighborhood was inconceivable.¹⁴ One commentator has suggested that, “[w]ith *Mitchel*, the essential theory of employment covenants was largely completed,”¹⁵ while another said that “[t]here is very little in the modern approach to the problem for which a basis cannot be found in Macclesfield’s opinion.”¹⁶ Thus, if only in terms of the judicial consideration of no-compete agreements, little has changed since 1711. Little, that is, until now.

In several recent cases in New York involving the enforcement of restrictive covenants by Internet companies, the criteria previously used for determining the validity of a no-compete agreement, together with a more detailed version of the rule of reason established in *Mitchel*, have been questioned.¹⁷ The rapid rate of progress and technological development on the Internet has prompted courts to reevaluate the appropriate duration of no-compete agreements; a twelve-month period, for example, normally considered to be a reasonable term for a no-compete agreement in traditional industries, is an “eternity” online.¹⁸ Similarly, because the Internet has no territorial boundaries, any purely geographic restrictions would be “all-or-nothing:”¹⁹ under the traditional requirements, the “geographical area” of the Internet

¹² Harlan M. Blake, *Employee Agreements Not to Compete*, 73 HARV. L. REV. 625, 626 (1960).

¹³ *Id.* at 627.

¹⁴ *Id.* at 630.

¹⁵ Mark Glick, et al., *Post-Employment Covenants in Utah: A Unified Framework Using Law and Economics*, available at http://www.econ.utah.edu/les/PostEmp_Glick.htm.

¹⁶ Blake, *supra* note 12, at 630-31.

¹⁷ See *Earthweb v. Schlack*, 71 F. Supp. 2d 299 (S.D.N.Y. 1999); *DoubleClick v. Henderson*, 1997 WL 731413 (N.Y. Sup. Ct., Nov. 7, 1997).

¹⁸ *Earthweb*, 71 F. Supp. 2d, at 316.

¹⁹ Blake has argued that the decline in significance to the courts of geographic boundaries with respect to no-compete agreements has been gradual. See Blake, *supra* note 12, at 675. (quoting “Thus, in the modern cases the ‘time’ dimension remains critical, but the ‘activity’ restraint is, in many cases, replacing the ‘area’ restraint. Restraints mainly concerned with protecting confidential information are likely to be inadequate if they contain any geographic limitation; markets and competition are increasingly national, even international, in scope.”).

(in the words of Judge Macclesfield) would demand that an employee be restricted from working for any company doing business on the Internet. Alternatively, because of the staggering growth of e-commerce and the proliferation of businesses going online, and thus the severe burden upon an employee prevented from working for another Internet company, it is possible that such an employee could not be restricted from working for any Internet company at all.²⁰ This Hobson's choice risks inequity for both employees and employers.

In response to this problem, courts – and legislatures – both in New York and around the country have been called upon to delineate what, if any, temporal, territorial, or other boundaries might exist online.²¹ Ultimately, courts are likely to continue to apply an analysis similar to that which they have always used in determining whether no-compete agreements are enforceable.²² In one narrow respect, therefore, these recent cases illustrate the judicial distaste, if only heightened, for no-compete agreements. Whether in the “brick and mortar” world or online; the Internet context may necessitate only slightly different outcomes than might occur within traditional industries.²³ In broader terms,

²⁰ See *Earthweb*, 71 F. Supp. 2d, at 306 (referring to comparisons between some Internet companies as “ephemeral”).

²¹ Some states have elected to address the issue through their respective legislatures, others through the judiciary. Therefore, different jurisdictions weigh the competing interests inherent in no-compete agreements differently. California, for example, takes a very restrictive approach. See CAL. BUS. & PROF. CODE, 16600-01 (1997). “Only where the interest sought to be protected would be recognized by the law of unfair competition, e.g., trade secrets or other proprietary rights, would a covenant not to compete be allowed and only to the extent necessary to protect these special interests;” Benjamin Aaron and Matthew Finkin, *The Duty of Loyalty: The Law of Employee Loyalty in the United States*, 20 COMP. LAB. L. & POL’Y J. 321 (1999); see, e.g., *Hollingsworth Solderless Terminal Co. v. Turley*, 622 F.2d 1324 (9th Cir. 1980). South Dakota, on the other hand, has made a broad legislative provision for covenants not to compete. See S.D. CODIFIED LAWS § 53-9-11 (Michie 1990). Under South Dakota law, so long as the statutory conditions are met, no examination of the “reasonableness” of the covenant is required for employees who voluntarily quit or are discharged for cause. The generally prevailing view, however, is that a covenant not to compete will be enforced if it is supported by consideration, is justified by a legitimate interest of the employer, and is reasonable in the restrictions it imposes on what the employee may do, where (or for whom) and for how long in light of the employer’s interest, the employee’s interest, and the public interest. See Aaron, *Duty of Loyalty*, 20 COMP. LAB. L. & POL’Y J. at 325. For a complete analysis of the jurisdictional holdings of each of the fifty states, consult COVENANTS NOT TO COMPETE: A STATE-BY-STATE SURVEY (Brian Malsberger, ed.) (2nd ed. 1996 and 1998 Cumulative Supplement).

²² See, e.g., *Earthweb*, 71 F. Supp. 2d at 316.

²³ *Id.* at 313, 316.

however, these cases promote the growing notion that the Internet warrants a modification, if not a complete reassessment, of not just employment law or business law, but of traditional legal principles as a whole. Part I of this Note reviews the judicial treatment of no-compete agreements historically, from common law through the current New York law. Part II analyzes *Earthweb v. Schlack*,²⁴ a federal case decided in the Southern District of New York involving a no-compete agreement between an Internet company and one of its employees. Part III of this Note speculates as to the applicability of *Earthweb*, both specifically with respect to no-compete agreements and employment law, and generally with respect to the effect the unique characteristics of the Internet will have on other cases and on law as a whole.

I. A SOCIO-ECONOMIC AND LEGAL HISTORY OF NO-COMPETE AGREEMENTS

Traditionally, as originally discussed in *Mitchel v. Reynolds*, no-compete agreements represented a meeting of two contrasting policies: the protection of “the uninhibited flow of services, talent, and ideas,” as manifested by employee mobility and which resulted in the ability of employees to serve society, and, on the other hand, the recognized right of employers to secure the legitimate fruits of their toil and money.²⁵ The law pertaining to restrictive covenants has been influenced by many diverse factors, including the Black Death, which decimated the European population, and thus the European work force, in the 14th century, and the rise of craft guilds in the 15th and 16th centuries.²⁶ As a result of the Black Death in 1348 and the resultant reduced labor supply, each employee became critical to the continued operation of society.²⁷ To maintain the proper functioning of society, courts were compelled to secure for every “master” or “journeyman” the ability to pursue his trade without restriction.²⁸

²⁴ *See id.*

²⁵ *See* Reed, *Roberts Assoc. v. John J. Strauman*, 40 N.Y.2d 303, 308 (1976).

²⁶ *See* MALSBERGER, *supra* note 21, at 155-57.

²⁷ *See id.*

²⁸ *See id.*

A. Restrictive Covenants at Common Law

From the earliest reported cases, courts have leaned towards protection of the rights of the employee. Indeed, the first known case of a restraint of trade occurred in 1414, centuries before even *Mitchel*, by which point “old and settled law” had been established in the matter.²⁹ In *The Dyer’s Case*,³⁰ a dyer had covenanted not to practice his trade in London for two years. Writing for the court, Mr. Justice Hull found that the agreement was against public policy, against common law, and against the common good: “*per Dieu, si le plaintiff fuit icy, il irra al prison, tanque il ust fait fyne au Roye*” (“by God, if the plaintiff was here, he should go to prison till he had paid a fine to the King”).³¹ From this case two fundamental common-law principles emerged: (1) all available skilled labor had to be kept in the public domain, and (2) an individual had a right to earn a livelihood.³²

Other cases have produced more illuminating analyses, if not more indignant outcries, for the general judicial reluctance to enforce no-compete agreements.³³ At common law, each individual was held to possess a valuable commodity, or at least a potentially valuable commodity, in his ability to apply a learned skill for the common benefit of society; to hinder the application of this skill was to undermine the interests of society, not to mention jeopardize the livelihood and subsistence of the bound party and his family.³⁴ “[T]he law abhors idleness, the mother of all evils . . . and especially in young men, who ought in their youth (which is their seed time) to learn lawful sciences and trades, which are profitable to the commonwealth, and whereof they might reap the fruit in old age.”³⁵ At common law, restrictive covenants such as no-compete agreements were interpreted as a restraint upon the potential for society as a whole. “[I]t is contrary to public policy and inimical to the best interests of men and the welfare of society, that any one should bind himself generally not to engage in a

²⁹ *The Dyer’s Case*, Y.B. Mich. 2 Hen. 5, fol. 5, pl. 26 (1414).

³⁰ *Id.*

³¹ *Id.*

³² See MALSBERGER, *supra* note 21, at 157.

³³ See generally David L. Gregory, *Courts in New York Will Enforce Non-Compete Clauses In Contracts Only If They Are Carefully Contoured*, 72 N.Y. ST. B.J. 27 (2000).

³⁴ See James Kerr, *Contracts In Restraint of Trade*, 22 AMER. L. REV. 873 (1888).

³⁵ *Case of Tailors of Ipswich*, 77 Eng. Rep. 1218, 1219 (K.B. 1614).

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legitimate profession, or carry on his lawful trade or business.”³⁶ Due to the existing social and economic circumstances, from the earliest decisions on record, no-compete agreements were viewed with judicial disfavor.³⁷

Nevertheless, in spite of the harm no-compete agreements posed to both individuals and to society at large, there were certain undeniable, indispensable benefits arising from restrictive covenants. “Self-protection is the first law of nature and of nations, and paramount to all others,” one early commentator noted.³⁸ Indeed, when properly constructed, no-compete agreements prevent industry from undermining itself:

A merchant or manufacturer would soon find a rival in every one of his servants if he could not prevent them from using to his prejudice the knowledge they acquired in his employ. Engagements of this sort between masters and servants are not injurious restraints of trade, but securities necessary for those who engage it. The effect of such contracts is to encourage rather than cramp the employment of capital in trade and the promotion of industry.³⁹

Without the enforcement of no-compete agreements, businesses would be unable to afford the stimulation of research and improved business methods, nor could they achieve the freedom of communication necessary for a company to operate efficiently.⁴⁰ A company has a legitimate interest against unfair practices by an employee or another company that might lure the employee in order to gain an unfair advantage over the original employer.⁴¹ A company has a natural right to defend itself against “deliberate surreptitious commercial piracy,” and to “safeguard[] that which has made [the] business successful.”⁴²

³⁶ Kerr, *supra* note 34, at 857-76 (emphasis omitted).

³⁷ See generally Tracy L. Staid, *The Enforceability of Noncompetition Agreements When Employment Is At-Will: Reformulating The Analysis*, 2 EMPLOYEE RTS. & EMPLOYMENT POLY’ J. 95 (1995).

³⁸ Kerr, *supra* note 34, at 874.

³⁹ *Homer v. Ashford*, 3 Bing. 322, 327 (1825).

⁴⁰ See Blake, *supra* note 12, at 627.

⁴¹ Joseph Bachelder III, *Restrictive Covenants: ‘BDO Seidman’ Case*, N.Y. L.J., Aug. 30, 1999 at 3.

⁴² *Reed Roberts Assoc. v. John J. Strauman*, 40 N.Y.2d 303, 308 (1976).

Other significant socio-economic bases for restrictive covenants justify their appeal to and frequent use by employers. In a service-driven economy, for example, the ability of an employer to protect its investment in human resources, customer relationships, and confidential business information – the focal elements of a valid no-compete agreement – is critical to ensuring the company's continued economic viability.⁴³ No-compete agreements protect the employer's interests in such investments by preventing former employees from entering into competitive employment and otherwise eroding the former employer's market share.⁴⁴ These restraints safeguard interests not protected by trade secret, patent, or copyright statutes, and serve to enhance those protections by supplying contractual remedies to which an employer might not otherwise be entitled.⁴⁵ "The growth in use of such covenants also represents a sound response to increased levels of employee mobility, the globalization of product markets, and rapid advances in technology."⁴⁶ With the comfort and security of no-compete agreements, employers can be more confident that valuable information imparted to their employees will not be used against them later in a competitive endeavor.⁴⁷

Historically, until the end of the nineteenth century, both English and American courts regarded *Mitchel* as the seminal authority in cases involving restrictive covenants and no-compete agreements.⁴⁸ As the respective societies became more capitalistic, however, their courts began adopting more flexible requirements – the central concern became whether the contract at issue was fair and reasonable, not whether the transaction involved actual consideration, as necessary under strict contract law.⁴⁹ With the twentieth century and the peak of the Industrial Revolution came a wider variety of jobs and a wider range of circumstances surrounding employment. Unprecedented mergers and industrial growth led to fierce rivalries between competing companies, each of which might have been both limited to and protected previously by local markets.⁵⁰ Indeed, the Industrial Revolution

⁴³ See MALSBERGER, *supra* note 21, at ix.

⁴⁴ *See id.*

⁴⁵ *See id.*

⁴⁶ *See id.*

⁴⁷ *See id.* at ix-x.

⁴⁸ *See* Blake, *supra* note 12, at 630-631.

⁴⁹ *See* Glick, et al., *supra* note 15.

⁵⁰ Blake, *supra* note 12, at 638.

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foreshadowed the current “Internet Revolution,” in terms of “new” employer-employee relationships and the balance of rights contained therein:

Men had become more mobile geographically; to leave one’s town no longer involved the economic risks and actual physical dangers of an earlier period. Local roots were less strong; hostility to strangers less of a factor. On the other hand, operations were larger, personal relationships between master and servant were less important and the employee was more completely dependent on his vocation for his livelihood than ever before.⁵¹

With the sweeping changes in employment trends caused by the Industrial Revolution, the appropriateness of certain elements of the rule of reason test formulated in *Mitchel* demanded reconsideration in light of the varied cases which were beginning to emerge.⁵² With changes to technology came changes to industry and to the economy, which in the nineteenth century warranted shifts in the balance of power within the employer-employee relationship.⁵³ The Industrial Revolution thus posed the first real challenge to the judicial attitude towards no-compete agreements.

Instead of protecting employers from expanding markets and increasingly encroaching competitors, however, the Industrial Revolution led American courts to place even more emphasis on protecting employees and even less on technical contract terms.⁵⁴ The earliest cases in New York involving restrictive covenants declared that restraints which covered the entire state were invalid without any consideration at all as to the circumstances in which the agreement was made.⁵⁵ The courts premised their respective holdings in their “regard for the interests of the public in unmonopolized, untrammelled commerce, trade, and the arts, and in having as many possible industrious citizens engaged in contributing their quota to the aggregate productions of the

⁵¹ *Id.* at 638-39.

⁵² *See id.* at 637-39.

⁵³ *See id.*

⁵⁴ *See id.* at 639-40.

⁵⁵ *See Lawrence v. Kidder*, 10 Barb. 641 (N.Y. Sup. Ct. 1851); *Dunlop v. Gregory*, 10 N.Y. 241 (1851).

community.”⁵⁶ Any agreement that prevented an individual from engaging in practicing his occupation within the boundaries of the entire state “exact[ed] more territory from the obligor than [was] essential to the protection of the obligee,” and was held uniformly invalid.⁵⁷

In the first case involving a restrictive covenant before the United States Supreme Court, however, the Court found that a consistent rule as to the appropriate geographic boundaries for restrictive covenants was not so clear.⁵⁸ In *Oregon Steam v. Winsor*,⁵⁹ a navigation company sold a steamship to another company, on the condition that the purchasing company not use the ship in California waters for ten years.⁶⁰ *Oregon Steam* involved a business transaction similar to *Mitchel*, and the terms of the transaction were similarly upheld.⁶¹ The Supreme Court echoed the English rule of reason test, establishing it as the legal standard for the enforcement of no-compete agreements in the United States.⁶² Justice Bradley, writing for the Court, reiterated Macclesfield’s holding, that “[i]n order that it may not be unreasonable, the restraint imposed must not be larger than is required for the necessary protection of the party with whom the contract is made.”⁶³ The restraint at issue was found to be necessary to protect the former company from interference with its own business⁶⁴ – it did not unreasonably restrict the interests of the purchasing company, nor did it “deprive the country of any industrial agency.”⁶⁵ The restraint “involved no transfer of residence or allegiance on the part of the vendee in order to pursue its employment, nor any cessation or diminution of its business whatever.”⁶⁶ The agreement was presumed to be beneficial to both parties to the contract, and was therefore upheld.⁶⁷

⁵⁶ See *Lawrence*, 10 Barb. at 641.

⁵⁷ See *id.*

⁵⁸ See *Oregon Steam Navigation Co. v. Winsor*, 87 U.S. 64, 67-68 (1873).

⁵⁹ See *id.*

⁶⁰ *Id.* at 65.

⁶¹ *Id.* at 65, 71-72; see also *Mitchel v. Reynolds*, 24 Eng. Rep. 347 (Q.B. 1711).

⁶² *Oregon Steam*, 87 U.S. at 66-67.

⁶³ *Id.*

⁶⁴ *Id.* at 71-72.

⁶⁵ *Id.* at 69.

⁶⁶ *Id.*

⁶⁷ *Id.*

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While the rule of reason survived from England to the United States, Justice Bradley noted in the *Oregon Steam* decision that certain considerations with respect to no-compete agreements were indeed different in the United States than they had been in England. The rigid rule in terms of state boundaries as interpreted by New York courts was held to be erroneous, as the unique territory comprising the United States made the application of the rule of reason far more difficult than an understanding of it:⁶⁸

In this country especially, where State lines interpose such a slight barrier to social and business intercourse, it is often difficult to decide whether a contract not to exercise a particular trade in a particular State is, or is not, the rule. It has generally been held to be so, on the ground that it would compel a man thus bound to transfer his residence and allegiance to another State in order to pursue his avocation . . . This country is substantially one country, especially in all matters of trade and business.⁶⁹

So long as a restrictive covenant contained specific territorial boundaries, and did not include the country as a whole, the Court would refuse to construe the contract as void.⁷⁰ In contrast to New York's earlier holding, state boundaries alone were no obstacle to the conduct of business, and therefore, to restrict a company from engaging in business within an entire state was not necessarily unreasonable.⁷¹ Nevertheless, "[t]he point of difficulty in these cases is to determine what is a reasonable distance within which the prohibitory stipulation may lawfully have effect."⁷² Thus, in the Supreme Court's first opportunity to address no-compete agreements, it confessed that a functional determination on the matter of reasonable geographic boundaries for such contract could be quite complex.⁷³

The first major case in New York to follow *Oregon Steam* yet again found guidance in *Mitchel*. Similar to both *Mitchel* and

⁶⁸ *Oregon Steam Navigation Co.*, 87 U.S. at 67.

⁶⁹ *Id.*

⁷⁰ *Id.* at 67-69.

⁷¹ *Id.*

⁷² *Id.* at 68.

⁷³ *Id.*

Oregon Steam, in *Diamond Match v. Roeber*,⁷⁴ the New York Court of Appeals upheld the agreement specifically at issue, a restrictive covenant prohibiting the purchaser's right to manufacture matches throughout the United States, "except for Nevada and Montana."⁷⁵ "We are unwilling to say that the doctrine as to what is a general restraint of trade depends upon state lines, and we cannot say that the exception of Nevada and Montana was colorable merely."⁷⁶ In spite of the curious restriction, the purchaser had entered the agreement willingly and supported by good consideration, "presumably because he considered it for his advantage to make the sale."⁷⁷ With that understanding, the court refused to invalidate what it perceived the contracting parties had considered to be a reasonable agreement.⁷⁸

Nevertheless, the court cautioned against excessive enforcement of no-compete agreements between employers and employees, alluding to both the rule of reason and recalling the "mischief[s]" that arose from such restraints.⁷⁹ The court identified damage from such covenants "(1) to the party, by the loss, by the obligor, of his livelihood and the subsistence of his family; and (2) to the public, by depriving it of a useful member and by enabling corporations to gain control of the trade of the Kingdom."⁸⁰ The court expanded even further the judicial sensitivity towards employees that began with *Mitchel* and had been developed by the Supreme Court in *Oregon Steam*, citing geographic, technological, and perhaps most importantly, socio-economic changes:

Steam and electricity have, for the purposes of trade and commerce, almost annihilated distance, and the whole world is now a mart for the distribution of the products of industry. The great diffusion of wealth and the restless activity of mankind striving to better their condition has greatly enlarged the field of human enterprise and created a vast number of new industries, which give scope to ingenuity and employment for capital and labor. The laws no

⁷⁴ 106 N.Y. 473 (1887).

⁷⁵ *Id.* at 478.

⁷⁶ *Id.* at 485.

⁷⁷ *Id.*

⁷⁸ *Id.*

⁷⁹ *Mitchel*, 24 Eng. Rep. at 357-48.

⁸⁰ *Diamond Match*, 106 N.Y. at 481.

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longer favor the granting of exclusive privileges, and, to a great extent, business corporations are practically partnerships and may be organized by any persons who desire to unite their capital or skill in business, leaving a free field to all others who desire for the same or similar purposes to clothe themselves with a corporate character.⁸¹

For the blossoming New York economy, and that of the United States, to achieve its full potential, no-compete agreements had no choice but to bow to public policy and the greater interests of society, as nineteenth-century America could not afford to be “trammled by unnecessary restrictions.”⁸²

B. Establishing a Modern Standard Under New York Law

In 1932, the Restatement of Contracts proposed a uniform test for the enforceability of restrictive covenants.⁸³ The original Restatement stated that such a restraint would be held reasonable only if “it (1) is no greater than is required for the protection of the employer, (2) does not impose undue hardship on the employee, and (3) is not injurious to the public.”⁸⁴ The original version was adopted, largely intact, by the Restatement (Second) of Contracts in 1979, which stated:

- (1) A promise to refrain from competition that imposes a restraint that is ancillary to an otherwise valid transaction or relationship is unreasonably in restraint of trade if;
 - (a) the restraint is greater than is needed to protect the promisee’s legitimate interest, or

⁸¹ *Id.* The language in *Diamond Match* suggests that the Internet, or more specifically, the potential for sweeping and comprehensive growth which the Internet carries, might not be as novel to American society or to the American judiciary as some proponents contend.

⁸² *Id.* at 482.

⁸³ RESTATEMENT OF CONTRACTS § 515 (1932).

⁸⁴ This is an adaptation of the Restatement’s more general formulation to postemployment restraints, typical of those found in cases. *See* Blake, *supra* note 12, at 648-49 and n.79.

(b) the promisee's need is outweighed by the hardship to the promisor and the likely injury to the public.⁸⁵

A restraint would be reasonable only if it was no greater than that required for the protection of the employer, does not impose undue hardship on the employee, and is not injurious to the public.⁸⁶ The Restatement version was adopted in part under New York law by the Court of Appeals in *Reed Roberts Associates, Inc. v. Strauman*,⁸⁷ in which the court established the modern guideline under New York law for the enforceability of no-compete agreements.

In *Reed Roberts*, the plaintiff-employer sought to prevent a former employee from competing against it and soliciting its customers.⁸⁸ In its decision, the court first discussed restrictive covenants as a whole, following the pattern of *Mitchel*, *Oregon Steam*, and *Diamond Match*.⁸⁹ The court held that, under New York law, covenants restricting competition were only enforceable "to the extent that they satisfy the overriding requirement of reasonableness," a standard which varied with the circumstances in which the covenant was issued.⁹⁰ Thus, where a business was sold, restrictive covenants would be upheld more strictly with respect to time, scope and extent.⁹¹ In such cases, the anticompetitive measures were "designed to protect the goodwill integral to the business from usurpation by the former owner while at the same time allowing an owner to profit from the goodwill which he may have spent years creating."⁹² It was this "goodwill" that had been protected by the court in *Mitchel* over 350 years earlier.

In discussing no-compete agreements between employers and employees, the court in *Reed Roberts* followed the precedent established in *Mitchel*, one in which a "stricter" standard of reasonableness, one even more sympathetic towards employees,

⁸⁵ RESTATEMENT (SECOND) OF CONTRACTS §187 (1979).

⁸⁶ For a complete discussion of the differences between the two Restatements, see Milton Handler and Daniel Lazaroff, *Restraint of Trade and the Restatement (Second) of Contracts*, 57 N.Y.U. L. REV. 669 (1982).

⁸⁷ 40 N.Y.2d 303 (1976).

⁸⁸ *Id.* at 305-06.

⁸⁹ *Id.*

⁹⁰ *Id.* at 307-08.

⁹¹ *Id.*

⁹² *Id.*

would be used.⁹³ The “undoubted judicial disfavor” towards no-compete agreements was justified by “powerful considerations of public policy which militate against sanctioning the loss of a man’s livelihood.”⁹⁴ The view of at the time was that the economy of New York and in the United States resulted directly from “the uninhibited flow of services, talent and ideas,” and that no contract should bind an employee to prevent him from “apply[ing] to his own best advantage” the valuable skills obtained through previous employment.⁹⁵

Echoing the Restatement, the court in *Reed Roberts* held that “a restrictive covenant will only be subject to specific enforcement to the extent that it is reasonable in time and area, necessary to protect the employer’s legitimate interests, not harmful to the general public and not unreasonably burdensome to the employee.”⁹⁶ To temper its deference to a free and unfettered market, the court recognized the “legitimate” rights and interests of employers in securing the confidentiality of employees through no-compete agreements.⁹⁷ These interests included protection from “the disclosure or use of trade secrets or confidential customer information,” such as customer lists, each of which amounts to “deliberate surreptitious commercial piracy.”⁹⁸ Where the employee’s knowledge did not qualify for protection as a trade secret, however, and where there was no evidence of a breach of the employer’s trust, the court found no reason “to inhibit the employee’s ability to realize his potential both professionally and financially by availing himself of opportunity.”⁹⁹ The test as formulated in *Reed Roberts* has become the modern standard under New York law.¹⁰⁰

In a more recent case, *BDO Seidman v. Hirshberg*,¹⁰¹ the New York Court of Appeals applied the traditional test to no-compete agreements between “professionals,” in this case, accountants.¹⁰²

⁹³ *Reed Roberts*, 40 N.Y.2d at 307-08.

⁹⁴ *Id.* (citations omitted).

⁹⁵ *Id.*

⁹⁶ *Id.*

⁹⁷ *Id.* at 308.

⁹⁸ *Id.*

⁹⁹ *Reed Roberts*, 40 N.Y.2d at 309.

¹⁰⁰ *Id.*

¹⁰¹ 93 N.Y.2d 382 (1999).

¹⁰² *Id.* at 389-90.

In *BDO Seidman*, the court reiterated the “modern, prevailing common-law standard” for the enforceability of no-compete agreements as established in *Reed Roberts*: A no-compete agreement will be enforced to the extent that it is reasonable in time and area, necessary to protect the employer’s legitimate interests, not harmful to the general public, and not unreasonably burdensome to the employee.¹⁰³ The court ruled, however, that a legitimate employer interest included protection from “exploiting or appropriating the goodwill of a client or customer, which had been created and maintained at the employer’s expense, to the employer’s competitive detriment.”¹⁰⁴ In addition to trade secrets and customer lists, the court in *BDO Seidman* held that a company’s investment in customer relationships and in goodwill warranted protection as well. The goodwill which had previously been protected only in sale of business contracts was recognized as a legitimate employer interest to be protected in no-compete agreements between employers and employees. Furthermore, while *Reed Roberts* was the general test to be applied, employers were entitled to special protection against “professionals,” former employees who expose the employer “to special harm because of the unique nature of the employee’s services.”¹⁰⁵ This factor emerged as the “unique or extraordinary services” exception to the traditional enforcement of no-compete agreements. The burden of proof in the enforcement of a no-compete agreement now shifted in part: Under *BDO Seidman*, an employer must show that the employee threatened the interests of the employer, or alternatively, that the employee possessed “unique or extraordinary” skills or services, the use of which for a new employer would alone undermine the former employer’s interests.¹⁰⁶

In sum, under New York law, a no-compete agreement will generally be enforced if it is (1) reasonably limited in terms of scope and duration, and (2) narrowly tailored to the employer’s legitimate interests, which include protection of its trade secrets or other confidential information, or if the employee’s services are “unique or extraordinary.”¹⁰⁷ This formulation allows for “fair and reasonable counterbalancing provisions” on behalf of both the

¹⁰³ *Id.* at 388-89.

¹⁰⁴ *Id.* at 389.

¹⁰⁵ *See Lumex v. Highsmith*, 919 F. Supp. 624, 628 (E.D.N.Y. 1996).

¹⁰⁶ *Id.* at 628; *see also BDO Seidman*, 93 N.Y.2d at 389.

¹⁰⁷ *BDO Seidman*, 93 N.Y.2d at 389.

employer and the employee.¹⁰⁸ The threshold issues are therefore twofold: First, whether the no-compete agreement is reasonable as to “duration, territory and scope of proscribed activity,” and second, whether the agreement serves a “legitimate” purpose – i.e., something other than preventing talented employees from going to work for a competitor.¹⁰⁹ Only if a no-compete agreement comports with these terms will it be enforced under New York law.

II. NO-COMPETE AGREEMENTS AND THE INTERNET: *EARTHWEB V. SCHLACK*

“Turn on, tune in, interface:” A fitting motto for the twenty-first century and the Internet Revolution.¹¹⁰ According to recent studies, there were approximately 332.7 million Internet users as of June, 2000,¹¹¹ with more than 18 million new users every month,¹¹² and a projected 700 million users expected by the end of 2001.¹¹³ “E-commerce,” business transactions taking place over the Internet, is expected to reach \$1.1 trillion by 2002.¹¹⁴ In a mere twenty years, the Internet has transformed itself from a government and university research project into the ultimate “hangout for the masses.”¹¹⁵ One example of the Internet’s influence is the \$165 billion merger between America Online and Time Warner. The transaction was widely recognized as the absorption of the latter, the nation’s largest media and entertainment company with \$15 billion in sales in 1999, by the former, the nation’s largest Internet company, whose stock shares have increased over 59,000 percent since it went public in March, 1992.¹¹⁶ The New York Times called the deal “the first (though hardly the last) consummated marriage between new media and old;”¹¹⁷ whereas the Wall Street

¹⁰⁸ *Lumex*, 919 F. Supp., at 636.

¹⁰⁹ *Id.*

¹¹⁰ Gina Maranto, *Tune In, Turn On, Interface*, N.Y. TIMES, June 5, 1994, Sec. 7, at 38.

¹¹¹ Masaaki Suzuki, *Analysis: IT Infrastructure Needed to Bridge Digital Divide*, THE DAILY YOMIURI, July 26, 2000 at 12. (citing report of NUA, a company that specializes in publishing worldwide statistics).

¹¹² CES Notebook, COMMUNICATIONS DAILY, Jan. 11, 1999.

¹¹³ Agence France-Presse, *U.N. Fears Divisive Impact of the Internet*, N.Y. TIMES, June 29, 2000 at A16.

¹¹⁴ CES Notebook, *supra* note 112.

¹¹⁵ Maranto, *supra* note 110.

¹¹⁶ *Id.*

¹¹⁷ Frank Rich, *Two 21st Century Foxes Elope*, N.Y. TIMES, Jan. 15, 2000 at A17.

Journal called it “the death of old media.”¹¹⁸ Like Time Warner, traditional companies around the globe have found themselves facing an ultimatum: “[A]dapt to the new rules, or risk being left aside.”¹¹⁹ By the time it is complete, the Internet Revolution is expected to have an unparalleled influence on the world, requiring only two or three decades to achieve far more than the Industrial Revolution accomplished in two or three centuries.¹²⁰

With respect to no-compete agreements, because the Internet has had – and will continue to have – such a tremendous impact on the economy as a whole and on specific companies individually, it has also had an enormous impact on employment trends and employee mobility.¹²¹ Coupled with, or perhaps a result of, the robust American and global economy it helped to cultivate, the Internet has fostered a general mentality of employee mobility. According to one analyst, “[p]eople who try new opportunities aren’t necessarily seen as job hoppers anymore, but rather as risk takers.”¹²² Typical employees in Silicon Valley, for example, will have worked in 10 different jobs by the time they are 45 years old.¹²³ In the United States, the expected increase in information-science-related jobs is 118 percent by 2006, while the number of graduates planning to go into information science is expected to increase by only 4 percent.¹²⁴ Employees in certain Internet-related industries have thus become “more akin to rock stars than to regular employees,” as they are highly sought-after and therefore have significant leverage in the employer-employee relationship.¹²⁵ “Intellectual capital is becoming the battleground between budding entrepreneurs and organisations. The pendulum has swung towards the creators, many of whom want to own the intellectual rights to their work, but that’s being fiercely resisted by organisations of intergalactic value, which want control over the

¹¹⁸ *Id.*

¹¹⁹ Alex Berenson and Bill Carter, *When Everything New Becomes Dizzily Newer*, N. Y. TIMES, Jan. 11, 2000 at C1.

¹²⁰ CES Notebook, *supra* note 112.

¹²¹ *Id.*

¹²² Richard Ream, *Changing Jobs? It's a Changing Market*, INFORMATION TODAY, Feb. 1, 2000 at 18.

¹²³ *Id.*

¹²⁴ *Id.*

¹²⁵ Margaret Coles, *IT Stars Use Courts to Cast Off Chains*, SUNDAY TIMES (London), Dec. 5 1999.

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ideas.”¹²⁶ As a result, no-compete agreements are becoming an area of increasing concern for Internet companies engaged in this struggle, since, particularly with the recent market decline, “you’re going to see a lot of employers start to try enforcing those noncompetes.”¹²⁷

A. *Earthweb v. Schlack: The Southern District Goes Online*

In light of recent trends in both the economy and employee mobility, Mark Schlack is not exceptional. It is precisely because Mark Schlack is not exceptional that the issue of no-compete agreements on the Internet, contracts between Internet companies and their employees, is so critical to the Internet Revolution.¹²⁸

Mark Schlack had worked in the publishing industry for sixteen years before joining an Internet company called Earthweb.¹²⁹ Earthweb provided online products and services to information technology (IT) professionals through a number of websites containing articles and other training materials, periodicals, books, downloads, and other resources tailored to IT professionals.¹³⁰ Schlack was responsible for the editorial content of all of Earthweb’s websites, and was given the title of Vice President, Worldwide Content.¹³¹ Schlack was one of ten vice presidents within the company, in addition to two senior vice presidents, an executive vice president, and the chief executive officer.¹³² Schlack began his employment with Earthweb in October 1998.¹³³

When Schlack began working at Earthweb, he signed an employment agreement containing several sections, one of which was a no-compete agreement. The first section of the contract

¹²⁶ *Id.*

¹²⁷ John Shyer and Blair Connelly, *Dot-Com Noncompete Agreements Enforceable?*, N.Y. L.J., Sept. 18, 2000 at S5 (citation omitted).

¹²⁸ See Ronald Gilson, *The Legal Infrastructure of High Technology Industrial Districts: Silicon Valley, Route 128 and Covenants Not to Compete*, 74 N.Y.U. L. REV. 575 (suggesting that “[p]ostemployment covenants not to compete have the potential to restrict seriously the movement of employees between existing firms and to start-ups and, hence, to restrict seriously employee-transmitted knowledge spillovers”).

¹²⁹ *Earthweb v. Schlack*, 71 F. Supp. 2d 299, 303 (S.D.N.Y. 1999).

¹³⁰ *Id.* at 302-03.

¹³¹ *Id.* at 303.

¹³² *Id.*

¹³³ *Id.*

stated that Schlack's employment was "at will,"¹³⁴ meaning that the relationship "may be severed at any time by either party without cause."¹³⁵ The third section contained an "encyclopedic" definition of "inventions," which was incorporated into the subsequent section concerning non-disclosure of proprietary information.¹³⁶ Under the fourth section, Schlack was prohibited, both during and after his term of employment, from disclosing or using any "Confidential Information," unless requested to do so.¹³⁷ Under Earthweb's definition, such information included:

[A]ll proprietary information, technical data, trade secrets, and know-how, including, without limitation, research, product plans, customer lists, markets, software, developments, inventions, discoveries, processes, formulas, algorithms, technology, designs, drawings, marketing and other plans, business strategies and financial data and information, including but not limited to Inventions, whether or not market as 'Confidential.'¹³⁸

In spite of what might have been a genuine attempt at protecting information it had hoped to keep confidential, Earthweb's definition of "Confidential Information" restricted Schlack from utilizing far more than mere confidential information.

¹³⁴ *Id.* at 306.

¹³⁵ BLACK'S LEGAL DICTIONARY 525 (7th ed. 1999).

¹³⁶ *Earthweb*, 71 F. Supp. 2d at 306-07. Section Three defined "Inventions" as:

[A]ll ideas, potential marketing and sales relationships, inventions, copyrightable expression, research, plans for products or services, business development strategies, marketing plans, computer software (including, without limitation, source code), computer program, original works of authorship, characters, know-how, trade secrets, information, data, developments, discoveries, improvements, modifications, technology, algorithms and designs, whether or not subject to patent or copyright protection, made, conceived, expressed, developed, or actually or constructively reduced to practice by [Schlack] solely or jointly with others during the terms of [Schlack's] employment with Earthweb, which refer to, are suggested by, or result from any work which [Schlack] may do during his . . . employment, or from any information obtained from Earthweb or any affiliate of Earthweb, such that said information is obtained in the performance of duties related to employment at Earthweb.

Id.

¹³⁷ *Id.* at 307.

¹³⁸ *Id.*

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The fifth section of Schlack's employment agreement contained a no-compete agreement, or a "Limited Agreement Not to Compete."¹³⁹ Schlack could not "directly or indirectly" work in any capacity "for any person or entity that directly competes with Earthweb" for a period of twelve months.¹⁴⁰ A "directly competing entity" included:

(i) an on-line service for Information Professionals whose primary business is to provide Information Technology Professionals with a directory of third party technology, software, and/or developer resources; and/or an online reference library, and/or

(ii) an on-line store, the primary purpose of which is to sell or distribute third party software or products used for Internet site or software development.¹⁴¹

Under the terms and conditions of this employment agreement, containing fourteen sections over five pages, Mark Schlack began his employment with Earthweb.

On Sept. 22, 1999, after less than a year with Earthweb, Schlack left to join ITworld.com, a website owned and operated by International Data Group, Inc. (IDG), which was scheduled to launch in January, 2000.¹⁴² According to Earthweb, IDG is the world's leading provider of IT print-based information with over \$1 billion in annual revenues, mainly through its publication of

¹³⁹ *Id.*

¹⁴⁰ *Id.*

¹⁴¹ *Id.*

¹⁴² Under New York law, a trade secret is determined through consideration of the following:

- (1) the extent to which the information is know outside of the business;
- (2) the extent to which it is known by employees and others involved in the business;
- (3) the extent of measures taken by the business to guard the secrecy of the information;
- (4) the value of the information to the business and its competitors;
- (5) the amount of effort or money expended by the business in developing the information, [and]
- (6) the ease or difficulty with which the information could be properly acquired or duplicated by others.

Earthweb, 71 F. Supp. 2d at 314 (citation omitted).

more than 280 monthly periodicals.¹⁴³ IDG planned to consolidate four of its on-line IT publications, along with three other wholly-owned websites, into a single website, ITworld.com, which would be available to IT professionals for news, opinions and product information.¹⁴⁴ In contrast to Earthweb's focus on products and services of third parties, ITworld.com would rely on its own internal staff of more than 275 journalists.¹⁴⁵ Shortly after Schlack tendered his resignation, however, Earthweb sought a preliminary injunction in federal court to prevent Schlack from "disclosing or revealing Earthweb's trade secrets to IDG or any third parties."¹⁴⁶

In order to enforce its no-compete agreement through a preliminary injunction, Earthweb had to establish "(1) irreparable harm or injury, and (2) either (a) a likelihood of success on the merits or (b) sufficiently serious questions going to the merits to make them a fair ground for litigation and a balance of hardships tipping decidedly in [Earthweb's] favor."¹⁴⁷ In New York, irreparable harm may be demonstrated by a showing of misappropriation of trade secrets by an employee. "A trade secret, once lost, is lost forever; its loss cannot be measured in money damages."¹⁴⁸ Alternatively, Earthweb could show irreparable harm through the "inevitable disclosure" of trade secrets by the employee, normally used when an employee will join a company in direct competition with the original employer, and the employee possesses highly confidential or technical knowledge.¹⁴⁹ The theory behind the doctrine of inevitable disclosure is akin to "a coach, one of whose players has left, playbook in hand, to join the opposing team before the big game."¹⁵⁰ Similar to restrictive covenants, however, the doctrine of inevitable disclosure is generally frowned upon by the judiciary, except under the most exceptional circumstances.¹⁵¹ Therefore, if Schlack did not misappropriate any of Earthweb's trade secrets, any injunctive relief for Earthweb against Schlack would have to be found within the no-compete agreement contained in Schlack's employment

¹⁴³ *Id.* at 303.

¹⁴⁴ *Id.* at 306.

¹⁴⁵ *Id.*

¹⁴⁶ *Id.* at 302.

¹⁴⁷ *Earthweb*, 71 F. Supp. 2d at 308.

¹⁴⁸ *Id.* (citation omitted).

¹⁴⁹ *Id.* at 309.

¹⁵⁰ *Id.* (citation omitted).

¹⁵¹ *Id.* at 310.

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agreement.¹⁵²

In its preliminary analysis of the employment contract between Earthweb and Schlack, the court found various terms problematic, several of which resembled the “mischiefs” condemned in *Mitchel*.¹⁵³ First, the employment offered by Earthweb to Schlack was “at will,” which meant that Earthweb could terminate Schlack without cause and with no penalty for doing so, and yet it made no provision for any severance payment to Schlack.¹⁵⁴ Earthweb had even reserved the unilateral right to modify the terms of its agreement with Schlack.¹⁵⁵ Before considering the details of the no-compete agreement specifically, the court indicated that the contract which Earthweb had offered to Schlack seemed “onerous[ly]” overbroad, and tended to inhibit fair competition rather than protect the confidential information it feared Schlack might disclose.¹⁵⁶ The court concluded that, collectively, under the terms of his employment contract, Schlack seemed not so much employed by Earthweb as he was “indenture[d]” to it.¹⁵⁷

To justify the strict terms within the employment contract it had extended to Schlack, Earthweb argued that Schlack had been exposed to certain trade secrets while with the company, and that such terms were necessary and legitimate for Earthweb’s protection.¹⁵⁸ Schlack contested the extent to which he had access to any trade secrets, as well as his value to the company and the potential harm to Earthweb caused by his departure.¹⁵⁹ Earthweb argued that Schlack was “one of its most important officers,” and that, without the enforcement of its no-compete agreement, he would divulge important trade secrets.¹⁶⁰ Schlack asserted that Earthweb had inflated the nature of his position with the company, and that his position with IDG was sufficiently different that he would have no occasion to disclose anything he might have learned from his position with Earthweb.¹⁶¹ The two parties also disputed

¹⁵² *Id.*

¹⁵³ *See Mitchel*, 24 Eng. Rep. at 348.

¹⁵⁴ *Earthweb*, 71 F. Supp. 2d at 311.

¹⁵⁵ *Id.*

¹⁵⁶ *Id.*

¹⁵⁷ *Id.*

¹⁵⁸ *See id.* at 307-08.

¹⁵⁹ *Id.*

¹⁶⁰ *Earthweb*, 71 F. Supp. 2d at 303.

¹⁶¹ *Id.*

the extent to which Schlack had exposure to Earthweb's confidential information or trade secrets, namely, the company's strategic content planning and Schlack's technical knowledge of Earthweb's operations.¹⁶²

With respect to strategic planning, Earthweb alleged that Schlack knew "the specific target audience for each website, how Earthweb aggregated content on those websites to reach the targeted audience, and how Earthweb may intend to improve the content and delivery of particular websites."¹⁶³ Schlack responded that, while he did have significant involvement in Earthweb's editorial development, he had little if any interaction with senior management, and therefore knew little about any overall business goals.¹⁶⁴ Schlack also asserted that any incidental information he might have known about Earthweb's strategic planning would soon be obsolete, as the company's websites were constantly changing.¹⁶⁵ The only other confidential information at issue was Schlack's technical knowledge of Earthweb's operations. While Schlack had no access to Earthweb's source codes or configuration files, Schlack was allegedly aware of Earthweb's "trial and error process" in implementing the services of outside consultants. Earthweb feared that Schlack would use this knowledge to Earthweb's detriment by solving similar technical problems at ITworld.com thereby allowing ITworld.com to avoid the mistakes and pitfalls that had befallen Earthweb.¹⁶⁶ In all, Earthweb alleged that Schlack's knowledge, in aggregate, constituted confidential information which deserved protection as a trade secret, and that he should be enjoined from working for any competing Internet company.¹⁶⁷

The court determined that, as is likely at most Internet start-ups and other small companies, Mark Schlack did have access to information concerning a wide range of matters, some sensitive and confidential and some not.¹⁶⁸ Schlack did work in collaboration with other employees on matters relating to

¹⁶² *Id.*

¹⁶³ *Id.* at 304.

¹⁶⁴ *Id.* at 305.

¹⁶⁵ *Id.*

¹⁶⁶ *Earthweb*, 71 F. Supp. 2d at 305.

¹⁶⁷ *Id.* at 307-08.

¹⁶⁸ *Id.*

Earthweb's technology, marketing and advertising.¹⁶⁹ Although not directly responsible for such areas, Schlack's decisions relating to Earthweb's editorial content directly impacted these aspects of Earthweb's business, and it was unsurprising that Schlack's input was in fact regarded by Earthweb as "essential."¹⁷⁰ Nevertheless, the court doubted whether Schlack's level of input permitted him access to the type of information traditionally afforded trade secret protection.¹⁷¹ Schlack had not been involved in developing or planning Earthweb's business strategies or goals, nor did he have access to financial reports or information, categories of information normally considered confidential and deserving of protection.¹⁷² Furthermore, the court found that, given the "fluid and ever-expanding world of the Internet,"¹⁷³ any claims of confidentiality with respect to strategic planning were dubious, as such information was immediately and instantaneously revealed to the public upon a website's launch.¹⁷⁴

In its analysis of Schlack's duties to Earthweb, the court found that while the nature of Schlack's position did in fact offer him a broad perspective over Earthweb's day-to-day operations, in many important respects, his access to highly confidential information was limited.¹⁷⁵ Schlack's only contact with what the court might have considered confidential information in such cases – "advertiser list[s], source codes, or configuration files" – was incidental.¹⁷⁶ His editorial responsibilities did not place him within the "requisite proximity" to trade secret information, nor did it warrant restricting Schlack from pursuing employment with another Internet company such as ITworld.com.¹⁷⁷

Earthweb also pressed the position that, under the doctrine of "inevitable disclosure," Schlack might "unintentionally" reveal his knowledge of the company's trade secrets.¹⁷⁸ Under this principle, "a person in possession of trade secrets, when working on a similar

¹⁶⁹ *Id.* at 315.

¹⁷⁰ *Id.* at 305.

¹⁷¹ *Id.* at 316.

¹⁷² *Earthweb*, 71 F. Supp. 2d at 305.

¹⁷³ *Id.* at 302.

¹⁷⁴ *Id.* at 315.

¹⁷⁵ *Id.*

¹⁷⁶ *Id.*

¹⁷⁷ *Id.* at 316.

¹⁷⁸ *Earthweb*, 71 F. Supp. 2d at 316.

project, may ‘inevitably disclose’ the proprietary information and techniques of which he is in possession.”¹⁷⁹ Earthweb raised as an example *Lumex Inc. v. Highsmith*,¹⁸⁰ a case in which the district court found a risk of inevitable disclosure based on both the employee’s access to highly sensitive information, and that the industry in question, the health fitness industry, was a “‘copy cat’ or cloning industry.”¹⁸¹ Nevertheless, the court in *Earthweb* understood the company’s proposed application of the inevitable disclosure doctrine as “an implied-in-fact restrictive covenant,” which, like express restrictive covenants, ran counter to public policy.¹⁸² “[I]n its purest form, the inevitable disclosure doctrine treads an exceedingly narrow path through judicially disfavored territory.”¹⁸³ Because of the “onerous” terms of Schlack’s employment agreement, the court refused to expand the terms of the agreement even further on Earthweb’s behalf. “Earthweb [cannot] make an end-run around the agreement by asserting the doctrine of inevitable disclosure as an independent basis for relief.”¹⁸⁴ If Earthweb was entitled to a preliminary injunction barring Schlack from working for another Internet company, such relief would have to be found within the restrictive covenant it drafted, namely, the no-compete agreement.

The court then examined the specific no-compete agreement contained within Schlack’s employment contract with Earthweb.¹⁸⁵ Because Schlack was restricted through the terms of the agreement from working for a company whose “primary business” directly competed with Earthweb, the construal of ITworld.com’s purpose would contribute significantly to whether the agreement would be enforced. The company said that ITworld.com would be in direct competition with Earthweb, based on Earthweb’s interpretation of ITworld.com’s “‘mission’ memorandum,” and its analysis of the websites that IDG had hired Schlack to integrate.¹⁸⁶ Alternatively, Schlack argued that the “limited” no-compete agreement did not apply to ITworld.com, because that company’s “primary business”

¹⁷⁹ *Id.* (quoting *Delphine Software Intern. v. Electronic Arts, Inc.*, 1999 WL 627413, *3 (S.D.N.Y. Aug. 18, 1999)).

¹⁸⁰ 919 F. Supp. 624 (E.D.N.Y. 1996).

¹⁸¹ *Id.* at 629.

¹⁸² *Earthweb*, 71 F. Supp. 2d at 310.

¹⁸³ *Id.*

¹⁸⁴ *Id.* at 311.

¹⁸⁵ *Id.*

¹⁸⁶ *Id.* at 306.

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was neither “a directory of third party technology,” an “online reference library,” nor an “online store,” similar to Earthweb.¹⁸⁷ Instead, ITworld.com’s primary focus would be to publish news, analysis, and product information generated by its own editorial staff.¹⁸⁸ Furthermore, although both Earthweb and ITworld.com targeted IT professionals, Schlack argued that Earthweb’s products and services were aimed at programmers and technicians, while ITworld.com targeted upper-level executives, such as technology managers and chief information officers.¹⁸⁹ Earthweb countered that, as an Internet start-up company, ITworld.com’s “primary business” could change in the interim months preceding its launch, at which point it would be possible for ITworld.com to “directly compete” with Earthweb.¹⁹⁰ The unique capacity with which an Internet company could change its “primary business,” however, worked to Earthweb’s detriment: In order to obtain the preliminary injunction it sought, the court reiterated that Earthweb had to demonstrate that it would suffer irreparable harm “now,” and not at some point in the future.¹⁹¹

Towards that end, the court found that any comparison between Earthweb and ITworld.com, or between many Internet companies for that matter, might ultimately prove to be “ephemeral.”¹⁹² In consideration of the Internet Revolution, the court confessed its difficulty in assessing the characteristics of ITworld.com, “an embryonic business entity that will compete in a nascent industry which is evolving and re-inventing itself with breathtaking speed.”¹⁹³ Supported by Earthweb’s plans for “constant chang[e]” to its own websites, the court could not discern ITworld.com’s purpose from its “‘mission’ memorandum,” calling it a “visionary outline” and nothing the court could grasp to “transform . . . the idea of [ITworld.com] into a perceptible reality.”¹⁹⁴ Because any Internet company is likely to begin with nothing more than ITworld.com’s “architecture, content, and marketing strategy,” the court could not reach the determination that such an entity would

¹⁸⁷ *Id.* at 312.

¹⁸⁸ *Earthweb*, 71 F. Supp. 2d at 312.

¹⁸⁹ *Id.*

¹⁹⁰ *Id.*

¹⁹¹ *Id.*

¹⁹² *Id.* at 306.

¹⁹³ *Id.* at 312.

¹⁹⁴ *Earthweb*, 71 F. Supp. 2d at 312.

“directly compete” with Earthweb.¹⁹⁵

In reaching his conclusion, Judge Pauley relied in part upon another case, *DoubleClick v. Henderson*,¹⁹⁶ for guidance in dealing with restrictive covenants between employers and employees on the Internet. Ironically, the district court in *DoubleClick* declined to address the enforceability of the specific no-compete agreement involved in that case.¹⁹⁷ Nevertheless, the *DoubleClick* decision does shed light on the use of restrictive covenants, such as no-compete agreements, by Internet companies.

The defendants in *DoubleClick* were two senior executives for an Internet advertising company, with access to the company’s business plan, revenue projections, plans for future projects, pricing and product strategies, and other various databases with information concerning DoubleClick’s clients, among other confidential information.¹⁹⁸ The defendants had misappropriated trade secrets and other confidential information in their “surreptitious . . . plot . . .” to form their own company in direct competition with their former employer.¹⁹⁹

Nevertheless, in spite of the defendants’ conduct, the court still recognized the employees’ legitimate interest in applying their experience to future employment.²⁰⁰ The court found that the plaintiff’s proposed injunction, which sought to restrict the defendants for “a period of at least twelve months from launching a competitive business or from working for a direct competitor of DoubleClick, would prevent [defendants] [from] working for such a company if it engaged in Internet advertising even as a marginal

¹⁹⁵ *Id.*

¹⁹⁶ 1997 WL 731413 (N.Y. Sup. Nov. 7, 1997).

¹⁹⁷ In *DoubleClick*, there was “substantial evidence” that defendants had misappropriated their employer’s trade secret information. “Even in the absence of a contract restriction, a former employer is not entitled to solicit customers by fraudulent means, the use of trade secrets, or confidential information.” *Id.* at *4 n.2. In *Earthweb*, Earthweb made no allegation of misappropriation of trade secrets, only that Schlack would disclose what he had learned while with the company.

¹⁹⁸ To illustrate the degree to which the information was intended to be kept confidential, some of the misappropriated documents, such as “summaries of operations, revenue and expense analyses, [and] analytical summaries of financial indicators,” were distributed to DoubleClick’s top managers at the beginning of Board of Directors meetings, and then collected at the end so that they would remain confidential. *Id.* at *2.

¹⁹⁹ *Earthweb*, 71 F. Supp. 2d at 309.

²⁰⁰ *DoubleClick*, 1997 WL 731413 at *8.

part of its business.”²⁰¹ Instead, the court ruled that the defendants should not be restricted from working for companies that engaged in advertising in any media, including the Internet, so long as they did not contribute specifically to that company’s Internet advertising projects.²⁰²

In addition to limiting the scope of positions from which the defendants were restricted, the court in *DoubleClick* also found fault with the duration of the injunction sought by the employer, particularly in consideration of the unique characteristics of the Internet industry.²⁰³ In this respect, the *DoubleClick* decision was the first to raise this matter, and for that reason the case may be highly instructive in other cases involving Internet companies, such as *Earthweb*. “Given the speed with which the Internet advertising industry apparently changes, defendants’ knowledge of DoubleClick’s operations will likely lose value to such a degree that the purpose of a preliminary injunction will have evaporated before the year is up.”²⁰⁴ Previously, courts had enforced

²⁰¹ *Id.*

²⁰² *Id.*

²⁰³ *Id.*

²⁰⁴ *DoubleClick*, 1997 WL 731413 at *8. In place of DoubleClick’s suggested injunction of twelve months, the court issued an injunction which was to expire six months from the date of the opinion, at which point, upon a showing of good cause, DoubleClick could move to extend the injunction. The court also formulated the injunction so as to confine those businesses found to be “in direct competition” with DoubleClick:

It is hereby ORDERED that, Defendants are enjoined, for a period of six months from the date of this opinion, from launching any company, or taking employment with any company, which competes with DoubleClick, where defendants’ job description(s) or functions at said company or companies include providing any advice or information concerning any aspect of advertising on the Internet. A company shall be presumed to compete with DoubleClick if it provides advertising software, advertising services, or a mix of advertising software and advertising services, to any entity seeking to advertise on the Internet, or to any website seeking advertisers. Nothing herein shall be construed to prevent defendants from working for any employer that competes with DoubleClick, so long as defendants’ job description(s) or functions with such employer do not include providing advice or information concerning any aspect of advertising on the Internet. Defendants are also enjoined, for a period of six months from the date of this opinion, from providing any advice or information concerning any aspect of advertising on the Internet to any third parties who 1) work for defendants’ employer(s), or 2) provide or promise to provide any of the defendants with valuable consideration for the advice or information, or 3) share or promise to share any financial interest with any of the defendants.

Id.

restrictive covenants originally drafted to be in effect for six months, while there had been other cases in which a court had determined that a proposed year-long agreement was too burdensome. Nevertheless, the court in *DoubleClick* provides the first declaration that, within an entire industry, agreements preventing an employee from reentering the market for a single year were uniformly unfair. In certain key aspects, the Internet industry and other industries doing business on the Internet operated differently from more traditional industries, and *DoubleClick* advanced the notion that the Internet merited certain distinct considerations as well.

Thus, following the decision in *DoubleClick*, Judge Pauley concluded that, due to the particular nature of the Internet industry, the no-compete agreement offered by Earthweb to Schlack would “fail to pass muster” even if Schlack’s position at ITworld.com fell within the provision’s narrow parameters.²⁰⁵ Stating that under New York law, a no-compete agreement must be reasonable in terms of its scope and duration,²⁰⁶ Pauley reiterated the “powerful considerations of public policy which militate against sanctioning the loss of a man’s livelihood” and the employer’s entitlement “to protection from unfair or illegal conduct that causes economic injury.”²⁰⁷ With respect to the duration of the restriction, however, the court ruled that a one-year restriction was an excessive period to keep an employee from reentering the Internet workforce, “given the dynamic nature of this industry, its lack of geographical borders, and Schlack’s former cutting-edge position.”²⁰⁸ Citing *DoubleClick*, the court stated that a one-year restriction was generally excessive within the Internet industry, “given the speed with which the . . . industry changes.”²⁰⁹ Still, the court did not follow *DoubleClick* completely, as it declined to “blue pencil” Earthweb’s no-compete agreement to make it reasonable, opting instead to disregard it completely. “[R]etroactive alterations distort the terms of the employment relationship.”²¹⁰ Because the employment agreement as a whole overreached on Earthweb’s behalf, the court decided that it would act on Schlack’s behalf, and

²⁰⁵ *Earthweb*, 71 F. Supp. 2d at 313.

²⁰⁶ *Id.*

²⁰⁷ *Id.*

²⁰⁸ *Id.*

²⁰⁹ *Id.*

²¹⁰ *Id.* at 311.

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decline to enforce the agreement's terms.²¹¹ In perhaps its most vivid claim, the court concluded its discussion by declaring that "in the Internet environment, a one-year hiatus from the workforce is several generations, if not an eternity."²¹² Since the enforcement of such a restriction in the Internet industry would be unreasonable, the court refused to grant the preliminary injunction.²¹³ Schlack was free to join ITworld.com.

III. LESSONS TO LEARN FROM EARTHWEB V. SCHLACK

In response to the *Earthweb* decision, several employment lawyers began to suggest means by which lawyers and counsel for Internet companies should draft employment contracts and no-compete agreements which would comport with the "new" requirements and thereby avoid the problems unearthed in *Earthweb*.²¹⁴ "The holding in *Earthweb* that twelve months was too long a restrictive period grabbed the attention of employment lawyers and in-house counsel, who for years had been advising companies that twelve months was a reasonable duration for a noncompete," said one commentator. "Such advice may still hold true in traditional industries, but perhaps not when the client is a high-technology company."²¹⁵ Practically speaking, it is increasingly important after *Earthweb* that no-compete agreements be even more specifically tailored to the needs of the employer and the responsibilities of the employee in order to deserve judicial enforcement. While *Earthweb* is not the first case to stress this point, it certainly raises the bar as to how specific agreements must be. "Because most high-tech companies are in a state of continual flux, it is often difficult to anticipate the areas in which companies will be competing just one year – or even months – ahead of time," said another employment attorney. If the definitions of key employment terms aren't considered thoroughly, companies run

²¹¹ *Earthweb*, 71 F. Supp. 2d at 313.

²¹² *Id.* at 316.

²¹³ *Id.*

²¹⁴ See, e.g., Beverly Garofalo and Mitchell Fishberg, *Noncompete Agreements*, NAT'L L.J., Jan. 17, 2000 at B7; Jonathan Jacobson, *Court Ruling May Herald Next Step In Evolution of Restraint of Trade Law*, N.Y. L.J., Dec. 20, 1999 at 1; Victoria Cundiff, *Untangling Earthweb: A Fresh Look at Non-Competes and the Inevitability Doctrine*, PATENTS, COPYRIGHTS, TRADEMARKS AND LITERARY PROPERTY COURSE HANDBOOK SERIES, P.L.I., Feb. 2000.

²¹⁵ Garofalo et al., *supra* note 214.

the risk of drafting their agreements too narrowly or too broadly.²¹⁶ At the very least, Earthweb demonstrates that standardized, one-size-fits-all, “boilerplate” no-compete agreements are useless.²¹⁷

Another practical consideration to be gleaned from *Earthweb* is that, similar to targeting specific responsibilities or information, employers should use no-compete agreements more selectively. Although Schlack was a senior executive with the company, the court found Earthweb’s no-compete agreement to have been applied almost indiscriminately, as Schlack had minimal, if any, access to much of the information Earthweb was prohibiting him from using. “Only those employees with actual access to proprietary company information should be required to sign them; employees who are required to sign noncompetes may take them more seriously, knowing that they were among a select group.”²¹⁸ Alternatively, “[a] court may question the legitimacy of the employer’s purported protectible business interest if every clerk and secretary has signed off on the same boilerplate covenant.”²¹⁹ As in *Earthweb*, many technology companies require most employees to sign such agreements, since employees may indeed be exposed to confidential information at any given time during the term of their employment. Still, such a practice may ultimately prove to be counterproductive, and an employer interested in the safest means of security might find the effort to be largely unenforceable. In general, after *Earthweb*, “[t]he fate of the thousands of one-year noncompetes already in existence remains to be seen.”²²⁰

While certain specific concerns raised by both the *Earthweb* decision and by the practitioners are indeed significant with respect to employment law, several assertions promoted within the *Earthweb* decision, coupled with *DoubleClick*, raise the broader issue of conventional law as it relates and is applied to the Internet, and to activity which takes place online. In *Earthweb*, Judge Pauley found certain significant factors inapplicable, criteria normally relied upon under the application of New York law to traditional industry. Even in its nascence, the Internet has proven

²¹⁶ *Id.*

²¹⁷ *Id.*

²¹⁸ *Id.*

²¹⁹ *Id.*

²²⁰ *Id.*

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itself to be the source of many legal problems and an ample target for criticism from judges and lawyers alike. Judicial vexation with the Internet is widespread, even if judges are simultaneously awestruck, as the explosion in Internet use creates an explosion of lawsuits involving the Internet. In a recent domain-name dispute case also decided in the Southern District of New York, the court expressed its concern over the “knotty,” novel issues raised generally by disputes occurring over the Internet:

Do these online collisions pose new, unique difficulties to the law? To what extent do the distinct dimensions of the World Wide Web challenge the established concepts and methods developed to resolve legal conflicts arising from other media? Do the familiar approaches suffice to accommodate analysis of unaccustomed aspects of the new disputes?²²¹

The Internet has been called “a mass medium of communication and commerce . . . [and] an incubator of lawsuits,”²²² and “a legal chimera,” which “bedevils the litigator” through its “dissonant union of intellectual property and free speech.”²²³ Transactions taking place over the Internet, and the complications that arise, have even been compared to sex: “Although it is usually easy for two willing partners to complete a ‘transaction,’ the surrounding legal, cultural, and societal issues are dauntingly complex. Nor is there much specialized guidance for electronic merchants beyond informal ‘netiquette.’”²²⁴ As rapidly as the legal system attempts to apply traditional legal principles to the Internet, the Internet eludes the law, evolving at an uncontrollable rate, and the disparity is as evident as a cavernous hole between where the law is and where it needs to be.

To say that the Internet presents the legal establishment with very difficult problems is self-evident; to say precisely how the legal establishment should confront the Internet is in itself difficult and problematic. Nonetheless, if this Note does not, as it cannot,

²²¹ *Bigstar Entertainment, Inc. v. Next Big Star, Inc.*, 105 F. Supp. 2d 185, 189 (S.D.N.Y. 2000).

²²² *Id.*

²²³ Ryan Lambrecht, *Trade Secrets and the Internet: What Remedies Exist for Disclosure in the Information Age?* 18 REV. LITIG. 317 (1999).

²²⁴ *Id.*

propose a legal approach to the Internet, it is clear from indications both within and without the legal world that strict application of conventional legal principles to the Internet will not work since the Internet defies convention. Many of the rapidly-growing variety of cases involving the Internet raise knotty issues, some of them novel, yet whether these disputes pose unique difficulties to the law, or simply raise a twenty-first century challenge to it, remains to be seen. As one court propounded recently, “[t]o what extent do the distinct dimensions of the World Wide Web challenge the established concepts and methods developed to resolve legal conflicts arising from other media? Do the familiar approaches suffice to accommodate analysis of unaccustomed aspects of the new disputes?”²²⁵ More often than not, litigators rely on conventional wisdom to solve their problems, a strategy which may not work, “given the Internet’s defiance of convention and wisdom alike.”²²⁶

The history of restrictive covenants and no-compete agreements illustrates the notion that, as a result of socioeconomic and technological advances, what was once unreasonable is now reasonable. Modern society, and the Internet industry as a whole, seems to have reached a point where, conversely, what was once reasonable is now unreasonable. In addition to *Earthweb* and employment law, the issue of jurisdiction over the Internet, only the most preliminary judicial concern, also helps to illustrate the ways in which the Internet has confronted traditional law. Modern courts have found themselves struggling to articulate new standards, apply existing precedent, and educate themselves about the technical contours of the World Wide Web.²²⁷ The tremendous potential for growth and revenue “has begun to test the limits and underlying legitimacy of territorial concepts of personal jurisdiction.”²²⁸ Evoking Judge Pauley’s discussion of the Internet in *Earthweb*, another court found that, unlike federal districts, states or other fields, the Internet “has no territorial boundaries . . . [N]ot only is there perhaps ‘no there there,’ the

²²⁵ *Bigstar*, 105 F. Supp. 2d at 189.

²²⁶ Garofalo, *supra* note 214.

²²⁷ See generally Richard Rochlin, *Cyberspace, International Shoe, and the Changing Context for Personal Jurisdiction*, 32 CONN. L. REV. 653 (2000).

²²⁸ Kevin Fitzmaurice & Renu Mody, *International Shoe Meets the World Wide Web: Whither Personal Jurisdiction in the Age of the Internet?*, 71 FLA. B. J. 22 (1997).

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‘there’ is everywhere.”²²⁹ The Internet has no territorially-based boundaries; the speed and cost of message transmission on the Internet “is almost entirely independent of physical location.”²³⁰ The Internet puts significant pressure on jurisdictional analysis because “electronics enable a person to achieve a presence in all fifty states (or even the entire world) almost immediately from anywhere there might be a modem hookup.”²³¹ Again, it is important to realize that jurisdiction is only the most preliminary of concerns, if one of the more interesting and abstract, raised by the Internet.

In sum, *Earthweb* provides “a small glimpse of the future.”²³² As businesses and consumers adopt new technologies for concluding age-old transactions, they seek comfort in existing legal frameworks to determine their rights and obligations. The new technologies challenge traditional legal concepts, especially in a borderless legal environment where in many instances it remains unclear whose laws apply.²³³ In this “Brave New Economy,” one thing is certain: As dot-coms grow up and the Internet comes of age, the array of legal issues faced by on-line companies will grow ever more complex and numerous.²³⁴ At this early point in the Internet Revolution, it is accurate, if simplistic, to say that the most powerful tool in the dot-com arsenal is an understanding of the Internet, and of the technological and social changes it has unleashed, in order to navigate, litigate, and legislate the legal world of the Internet safely.²³⁵

IV. CONCLUSION

From its earliest common law origins, the judicial attitude towards no-compete agreements has been sensitive to the needs and vulnerabilities of employees. In one sense, *Earthweb*

²²⁹ *Blumenthal v. Drudge*, 992 F. Supp. 44, 48 (D.D.C. 1998) (citation omitted).

²³⁰ Christopher Cameron & Kevin Johnson, *Death of a Salesman? Forum Shopping and Outcome Determination Under International Shoe*, 28 U.C. DAVIS L. REV. 769, 785, n.57 (1995) (citation omitted).

²³¹ Karin Mika & Aaron Reber, *Internet Jurisdictional Issues: Fundamental Fairness in a Virtual World*, 30 CREIGHTON L. REV. 1169 (1997).

²³² Garofalo, *supra* note 214.

²³³ Daniela Ivascanu, *Legal Issues in Electronic Commerce in the Western Hemisphere*, 17 ARIZ. J. INTL. COMP. LAW 219 (2000).

²³⁴ Garofalo, *supra* note 214.

²³⁵ *Id.*

represents only the next step along that path, a case which is marginally different, if at all, from those cases which emerged during the past several hundred years, long before the Internet, but well after the Industrial Revolution and its resultant social and legal changes. From a slightly different angle, however, *Earthweb* simultaneously represents a new wave of cases emerging from an entirely new and unprecedented medium, one which has already produced social, political and cultural revolutions of its own. William Gibson, the science-fiction author and founder of the “cyberpunk generation” who was also responsible for coining the term “cyberspace,” said of the Internet,

The Web is new, and our response to it has not yet hardened. That is a large part of its appeal. It is something half-formed. Larval. It is not what it was six months ago; in another six months it will be something else again. It was not planned; it simply happened, is happening. It is happening the way cities happened. It is a city.²³⁶

The Internet is indeed a city, if not a world, of its own, colonizing the “brick and mortar” world at a unprecedented rate. The Internet is leading the world into the twenty-first century, and it will not stop for the American legal system. Courts must recognize that the Internet is unique, and that, increasingly, it must be dealt with as unique.

²³⁶ William Gibson, *The Net Is a Waste of Time*, N.Y. TIMES, July 14, 1996 at Sec. 6, p. 31.