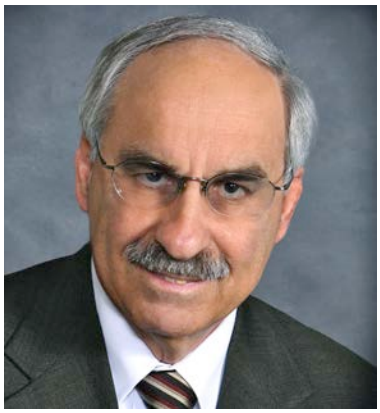
Breaking up is hard to do, but defaming the outgoing rep carries consequences



by Gerald M. Newman
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It was the author and journalist Helen Rowland who said, "Nowadays love is a matter of chance, matrimony a matter of money and divorce a matter of course."

More than once, rep-principal relationships have been compared to marriages. When the partners' interests are aligned and times are good, it is easy to seem happy and in love. When external pressures test the relationship, however, one party may quickly seek a divorce, and the scorned party often lashes out. Only one of these scenarios is worth writing about, of course.

The breakup

The lashing out of the moment involved Summit DNA, LLC, a New Hampshire-based medical consulting firm specializing in DNA testing. Summit signed a "Non-Exclusive Independent Sales Organization Agreement" with Proove Biosciences, Inc., a Southern California-based provider of proprietary genetic testing to physicians.

The parties' dispute recently played out in federal court in Baltimore, where Proove also maintains offices. After an initial year of Summit generating accounts for Proove in exchange for commissions, the payments stopped. Before Summit could respond to the non-payments, Proove also terminated its agreement, and accused Summit of violating the agreement's conflict of interest provision.

Summit promptly provided Proove with a notice of cure and asserted it was in full compliance with its agreement. Having safely restored the parties' agreement, but recognizing their irreconcilable differences, Summit proceeded to terminate, ratcheting up the dispute even more.

In response, Proove allegedly contacted a Summit customer with disparaging and false statements. Proove's president, Brian Meshkin, sent the following email.

"Additionally, it has come to our attention from multiple representatives of Summit Diagnostic that Summit has been marketing A1 Botech and Genomind genetic testing — which is an overt breach of our conflict of interest provision in Summit's contract with Proove.

"Thus, we have terminated our contract with Summit Diagnostics and are seeking legal action on related damages."

The aftermath

Immediately, Summit brought a nine-count complaint against both Proove and Meshkin individually. The more prominent charges alleged were "breach of contract" for failing to pay the commissions due and "defamation" for sending the above email falsely accusing Summit of breaching the parties' agreement.

Naturally, the defendants moved to dismiss. While a common defense strategy, motions to dismiss that seek to throw out a complaint as the first order of business generally face a high threshold. Courts are often reluctant to dismiss before a plaintiff has the opportunity to take discovery to help prove up the allegations.

The bickering, Part I: Breach of contract

Rather than make any effort to show it did pay the commissions due to Summit, defendants went on the offensive and argued that, by violating the agreement's conflict of interest provision, Summit cannot show it complied with a prerequisite to recovery, in legal terms, a "condition precedent." The operative conflict of interest terms in the agreement provided: "Summit shall not represent any individual or company directly or indirectly competing with Proove by offering same or similar services during the term of this agreement and in accordance with the 'Confidential Information, Trade Secrets and Competition' provision in the agreement."

As the court noted in ruling on the motion to dismiss, a condition precedent is defined in Maryland as a fact "which, unless excused, must exist or occur before a duty of immediate performance of a promise arises." In other words, defendants urged the court to rule that, by representing a competing company during the term of the agreement, Summit disqualified itself from suing for non-payment of commissions.

Looking at the conflict of interest provision, the court disagreed and found nothing suggesting it amounted to a condition precedent to recovery. Should Proove prove its assertion down the road, it might have available a defense to the complaint, but the language of the provision did not suggest it was a condition precedent to having to pay commissions. The motion to dismiss Summit's breach of contract claim was denied.

The bickering, Part II: Defamation

Among the elements a plaintiff alleging defamation in Maryland must plead, in order to withstand a motion to dismiss, are that the defendant made a statement to a third person that is both defamatory and false. "Defamatory"

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means a statement which tends to expose the plaintiff to "public scorn, hatred, contempt or ridicule," and which discourages others from having a good opinion of, or from associating with, the plaintiff.

Proove's motion asserted that its email, sent to a single Summit customer, did not subject it to public scorn, hatred, contempt or ridicule. Not surprisingly, the court quickly rejected this technical argument. The law recognizes that a corporation can be defamed by a statement that casts aspersions on its honesty, credit, efficiency, standing or prestige. The Meshkin email casting aspersions on Summit's business practices and honesty certainly qualified as defamatory.

Defendants also urged that the email was not false because Summit acknowledged working for two competing genetic testing companies. Such representation, they argued, plainly violated the conflict of interest provision's "shall not represent any individual or company directly or indirectly competing with Proove" language.

Summit, in turn, relied on other language from this same conflict of interest provision, contending the provision was only violated if, while representing a competing concern, it made improper use of the referenced "Confidential Information, Trade Secrets and Competition."

Summit noted this interpretation was consistent with the non-exclusive nature of the parties' "Non-Exclusive Independent Sales Organization Agreement," which always contemplated that Summit might represent competitors and only required that it preserve Proove's proprietary data.

The court essentially found both parties' positions reasonable, and it deemed the agreement ambiguous. In light of the conflicting interpretations, and because the case was at the early motion to dismiss stage, no determination could be made as to whether Summit violated the conflict of interest provision.

Therefore, the court could not decide if the emailed statements were false, and the defamation claim would survive the motion to dismiss.

The bickering, Part III: Individual liability

A related issue was the defendants' effort to defeat the defamation claim's extension to Meshkin individually and not just in his capacity as president of Proove. Ordinarily, officers of a corporation are not liable for torts committed by, or contractual obligations acquired by, the corporation. As the court noted, however, in Maryland, a corporate officer who "personally commits, inspires or participates" in a wrongful act, even though performed in the corporation's name, may be found personally liable.

By adequately pleading that Meshkin personally sent the subject email, Summit successfully exposed him to personal liability in the action. Keeping Meshkin in the case in his individual capacity, and not allowing him to use the corporation as a shield, was a highly effective move by Summit. The importance of having a director's personal assets on the line cannot be overstated for settlement considerations.

The upshot

Other (overreaching) claims attempted by Summit, including for tortious interference with business relationships, fraud and conversion, did not fare as well on the motion to dismiss, but the heart of the case against Proove and Meshkin survived. This meant that both would face the burden of discovery and of continued, potentially extensive litigation as Summit maintained its effort to recover the commissions due under the agreement and the damages caused by the defamatory email.

When a principal wrongfully withholds payment from its sales rep upon termination of a contract, instead of negotiating with the rep to arrive at an amiable separation, or otherwise acts against the rep's interests, various legal theories of relief may be available, and not all require the principal to lash out. It is the potential for such relief that should motivate fair treatment upon termination, and both reps and principals should be aware of its availability. ■