INTERNATIONAL BUSINESS MACHINES CORPORATION v. BAJOREK
191 F.3d 1033 (9th Cir. 1999)

KLEINFELD, Circuit Judge:

FACTS

IBM issued stock options to its executive employee, Dr. Bajorek, that were worth more than $900,000 when he exercised them. His option agreements included a promise that if he worked for a competitor within six months after he exercised his options, he would return any profits from the stock options. He left, and immediately went to work for a competitor. IBM therefore notified him that his stock options were cancelled.

Dr. Bajorek sued IBM in California for a declaratory judgment that he was in compliance with his agreements and that IBM was not entitled to cancel his stock options. IBM sued Dr. Bajorek in New York for breach of contract, on the theory that he broke his promise not to go to work for a competitor for six months. IBM's complaint also alleged fraudulent misrepresentation, on the theory that when Dr. Bajorek certified upon exercise of his stock options that he was in compliance, he knew full well that he did not intend to comply. Each case was filed in state court and removed to federal court. The stock option agreements said that disputes were to be resolved according to the law of New York.

The district court granted judgment on the pleadings for Bajorek. It addressed Bajorek's declaratory judgment action first and dismissed IBM's damages suit. The district court did not apply New York law, despite the parties' agreement to do so. Its theory was that application of New York law would violate strong California policies against restraining people from engaging in their lawful trade, and against employers collecting from employees wages they had already paid them. Those doctrines of California law, as the district court viewed them, made unenforceable the provision of the stock options requiring reimbursement if Dr. Bajorek went to work for a competitor within six months.

. . . IBM is a New York corporation with its principal place of business in New York. Bajorek worked for IBM for 25 years, mostly in California, but also for a few years in Minnesota and New York. IBM periodically issued various incentives in the nature of stock options to selected employees, including Bajorek, to induce them to remain with IBM. Dr. Bajorek's stock option agreements provided that, upon exercise, he would certify that he was in compliance with a cancellation clause, which prohibited him from working for a competitor, and that if he violated that clause during the six months after exercise, then he had to pay back to IBM his gains and payments from exercise of the options. Most importantly for this case, the stock options provided that the plan and all determinations made pursuant to it would be governed by the law of New York. Dr. Bajorek exercised his stock options, but went to work part-time for a competitor during his last week at IBM. He then went to work full time with the competitor as a senior executive immediately upon leaving IBM. IBM notified him that it was rescinding his stock options and demanded the money due upon cancellation, but Dr. Bajorek refused to pay it.

Dr. Bajorek made $928,538.74 from exercise of the stock options. IBM argues that he took almost a million dollars for not working for a competitor, yet did just that, so he has to pay the money back. Dr. Bajorek argues that under California law, an employer cannot take back the money it pays to employees, and cannot restrict an employee from going to work for a competitor, so he was not bound by these parts of the agreement. New York law does not have provisions like these. Thus the question is whether Dr. Bajorek is bound by his agreement to application of the law of New York.

ANALYSIS

. . . New York has a substantial relationship to the transaction and to the parties. IBM has its headquarters there. Bajorek chose to work for IBM. He voluntarily entered into contracts with IBM. The parties have a reasonable basis for choosing New York law, because IBM stock is nationally traded on the New York Stock Exchange, and this corporation headquartered in New York has an interest in having all its stock option agreements with employees in different places construed according to the same law. . . .

Bajorek . . . claims that IBM sought to prevent him from going to work within six months for Komag. If so, that would exclude him from one small

corner of the market but would not preclude him from engaging in his profession, trade or business. The covenant not to compete is limited to six months and to competitors. . . . Bajorek could have kept the money and gone to work for a competitor immediately upon quitting, had he elected to exercise his stock options six months before he quit. And he was free to work in his profession and in the same industry and keep the money, so long as he did not work for a competitor. And he could work for a competitor if he gave up what was paid in part for his promise not to.

It is one thing to tell a man that if he wants his pension, he cannot ever work in his trade again . . . and quite another to tell him that if he wants a million dollars from his stock options, he has to refrain from going to work for a competitor for six months.

III. The fraud claim.

The district court dismissed IBM's fraud claim on the pleadings. Thus the question is whether IBM could prove facts that would entitle it to relief under New York law for fraud. IBM pleaded that by signing his stock option form, Bajorek "implicitly made a material false representation to IBM that he would comply with the terms," and knew at that time that he would go to work for a competitor within six months in violation of the terms. He knew when he signed the forms that IBM would reasonably rely on his signature to sell him the stock, and that, had he disclosed the truth, that he knew he was going to violate the terms, IBM would not have sold him the stock pursuant to the option agreements.

The forms for exercising the stock option agreements said "I certify that I am in compliance with all terms and conditions ... including the rescission, conflict of interest, no compete, confidentiality and patent provisions." IBM did not plead that at the moment of exercise Bajorek was already working for a competitor, but only that he knew then that within six months he would do so, in violation of the agreement, and that he planned not to pay back the money he made from exercising the stock options.

Because the implied misrepresentation was of an intention, rather than a present fact, IBM's pleadings raise a question of whether signing the certification to collect the benefits of the stock option agreements, while intending to break the promises given in exchange for the stock, would constitute fraud under New York law.

New York's highest court has considered the question, "is a cause of action for fraud stated by alleging that a promisor, at the time of making certain representations, lacked any intention to perform them." Its answer was unequivocal. "A false statement of intention is sufficient to support an action for fraud, even where that statement relates to an agreement between the parties."

. . . IBM pleads that Bajorek "implicitly made a material false representation to IBM that he *would* comply." The exercise form also said that "I understand that failure to be in compliance will subject my profit . . . to be forfeited and repaid to IBM to the extent permitted by law and I agree to do so within ten days of notification." IBM's theory is that Bajorek, by signing with a present intention of not paying back the money, made a false statement of intention. . . .

Bajorek argues that his representation could not properly be treated as fraudulent, because the covenant he intended to breach was not enforceable under California law, so he did not intend to break any contractual provision that was not void as a matter of law. But the parties have not made us aware of any New York laws like the California provisions . . . that Bajorek claims made his agreement void. . . . [but] the two California statutes do not apply and Bajorek agreed to be bound by New York law. That would include New York law regarding fraud.

CONCLUSION

We vacate the judgments dismissing IBM's claims and granting judgment on the pleadings in favor of Bajorek. We remand for adjudication under New York law of IBM's complaint for damages for breach of contract (or Bajorek's complaint for a declaratory judgment that he did not breach) and IBM's complaint alleging fraudulent misrepresentation.

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