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GET BACK PAY AS PAY BACK

By *Eliyahu S. Scheiman*

In a recent decision, *Kaye v. Rosefelde*, 223 N.J. 218 (2015), the New Jersey Supreme Court clarified the availability of a significant, but underutilized, weapon in an employer's arsenal, holding that, for a breach of loyalty, an employer may be entitled to the return of an employee's compensation even *without proof* of economic damages.

Kaye is more helpful for its holding than its facts, which are not easily replicable. The defendant was an attorney and employee of a timeshare business. The trial court found that he had engaged in serious misconduct in breach of his duty of loyalty to his employer by self-dealing (drafting operating agreements to increase his personal interests in the business and diverting other employees' interests to himself); conspiring to forge deeds; and fraudulently applying for health insurance benefits for independent contractors as "employees."

As a remedy, the plaintiff sought "disgorgement" or the return of the defendant's salary for the period in which he was disloyal under the "faithless servant doctrine." Though the defendant had breached his duty of loyalty, the trial court grappled with the fact that the breach did not cause actual economic loss to the employer, typically a precondition to damages, and thus denied the disgorgement sought by the employer. The Appellate Division affirmed.

The New Jersey Supreme Court, however, reversed, based on the underpinning of the "faithless servant doctrine." Loyalty is at the core of the employment relationship. In exchange for an employee's loyal performance, the employer compensates him; salary is the consideration for one's faithful performance of his job. If an employee is

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disloyal, his compensation during that period "is, in effect, unearned." *Id.* at 233. Thus, asking, as the trial and appellate courts did, whether an employee's disloyalty resulted in actual economic damages to the employer is beside the point: the economic damage to the employer is that the employee was paid for work he failed to faithfully perform. Accordingly, the Court held that an "employer may seek disgorgement of a disloyal employee's compensation as a remedy for breach of the duty of loyalty, with or without a finding of economic loss." *Id.* at 236.

Conclusion

Although what actually constitutes "disloyalty" will be highly fact-specific, employers often overlook the "faithless servant doctrine" and simply assume that their only recourse in dealing with an employee's misconduct, particularly, absent economic loss, is termination. Employers would do well to remember *Kaye*, as the disgorgement of salary or other compensation is a powerful remedy that in and of itself can amount to significant damages for an employee's misconduct on the job. Further, to the extent that an employer finds itself as a defendant when the employee is terminated for disloyalty and brings suit, the faithless servant doctrine can lead to a potent counterclaim.

The Porzio Employment Law Monthly is a summary of recent developments in employment law. It provides employers with an overview of the various legal issues confronting them as well as practical tips for ensuring compliance with the law and sound business practices. This newsletter, however, should not be relied upon for legal advice in any particular matter.