



NINETEENTH JUDICIAL CIRCUIT OF VIRGINIA

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February 17, 2021

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Re: *Geneva Enterprises, LLC, et. al. v. Donald Bavely*
Case No. CL-2018-18124

Dear Counsel:

The primary issue before the Court is whether an employer may claw back an employee's salary, bonuses, and other forms of compensation paid prior to termination, but during a time when the employee's concealed acts would have justified termination. The Court holds the employer may not claw back compensation on this basis unless: (1) the employment contract provided for this relief, or (2) the employer can point to specific wrongdoing that led to specific damages. In this latter instance the relief is the value of the actual damages on a transactional basis, not a general recoupment of the compensation paid.

OPINION LETTER

The Court sustains Defendant Donald Bavely's Demurrer to Counts 20-23 of Plaintiff Geneva Enterprises' ("Geneva's") First Amended Complaint ("Amended Complaint").

Another judge of this Court, in a related case, reached an indistinguishable, opposite holding on a similar issue. *Donna Bavely v. Geneva Enterprises, Inc., et. al.*, CL-2017-17979 (October 25, 2019 Order) (allowing Geneva to assert claims of fraud against a different employee and seek recovery of past compensation paid prior to learning of the employee's misdeeds) ("2019 Order"). Because these two holdings are irreconcilable, the Court issues this Opinion Letter to explain its reasons for its holding.

Secondary issues taken under advisement along with this primary issue do not warrant an Opinion Letter. They are whether a cause of action exists to support Counts 14-16 and 24-27 of the Amended Complaint and are separately addressed in the Memorandum Order memorializing the Court's rulings.

I. Overview.

Geneva alleges Bavely defrauded it.¹ Robert Rosenthal built the Rosenthal Automotive Organization, an auto dealership group, "which currently encompasses fifteen sales and service locations in the D.C.-Maryland-Virginia region." (Am. Compl. ¶ 1.) Mr. Rosenthal "entrusted the day-to-day operations of the Rosenthal Automotive Organization to Bavely, as President" in the early 2000's. (*Id.*) Geneva claims Bavely "exploited his position" by "help[ing] himself" to the business and concealing his actions while Mr. Rosenthal advanced in age and declined in health. (*Id.* ¶ 1, 2.) Geneva alleges Bavely "surreptitiously usurped Mr. Rosenthal's authority on multiple issues of corporate control, repeatedly made strategic decisions and investments for his own personal benefit to the detriment of Mr. Rosenthal, his family and Geneva, and duplicitously schemed to seize control of the business upon Mr. Rosenthal's passing." (*Id.* ¶ 2.) Some of the wrongful actions Geneva alleges Bavely engaged in include: creating "Diversionsary LLCs" that "diverted corporate opportunities—and siphoned away revenue and voting control—from both Mr. Rosenthal and Geneva (*Id.* ¶ 3(a)), issuing unauthorized loans (*Id.* ¶ 3(b)), engaging in workplace misconduct such as bullying employees who "resisted his misconduct" (*Id.* ¶ 3(c)), and misusing company resources for personal benefit, like purchasing a personal vehicle for a Hawaiian vacation home (*Id.* ¶ 3(d)).

The relevant counts of the Amended Complaint are: Count Twenty (Fraud Claim—Unearned Salaries, Bonuses, Ownership Interests, and Distributions), Count Twenty-One (Conversion Claim—Unearned Salaries, Bonuses, Ownership Interests, and Distributions), Count Twenty-Two (Unjust Enrichment Claim—Unearned Salaries, Bonuses, Ownership Interests, and Distributions), and Count Twenty-Three (Claim for Money Had and Received).

¹ For the purposes of this Demurrer the Court assumes as true Geneva's factual allegations, as it must. See *Tingler v. Greystone Homes, Inc.*, 298 Va. 63, 72 (2019). The Court's conclusory recitation of the allegations in this Opinion Letter are not findings.

Each count alleges Bavely signed an “Employee Handbook” with numerous policies, including prohibitions against “(i) discrimination and harassment; (ii) usage of company computers for personal affairs; (iii) misappropriation or theft of company property; (iv) unauthorized usage of company vehicles; (v) unethical or questionable practices for personal gain; (vi) engaging in activities that conflict with the company’s best interests; (vii) engaging in any activity which is a violation of local, state, or federal law; (viii) providing kickbacks or rebates to himself or others; (ix) making false or misleading entries in company books and records; and (x) otherwise participating in situations that create a conflict of interest.” (Am. Compl. ¶ 301, 314, 325, and 339.) Violations of the policies were grounds for immediate termination. (*Id.* ¶ 303, 316, 327, and 341.) Bavely violated these policies and wrongfully concealed them. (*Id.* ¶ 305, 318, 329, and 343.) Had Geneva known of the violations it would have terminated him. (*Id.* ¶ 307, 319, 330, 344.) It seeks reimbursement from Bavely for all compensation it paid him after the time it would have fired Bavely had it known of the violations. (*Id.* ¶ 308, 320, 331, 345.)

II. Employers May Not Generally Claw Back Employee Pre-Termination Compensation for Concealed Wrongful Acts.

Geneva promotes a new cause of action that would be an employer’s fantasy: upon discovering an employee surreptitiously violated company policy, or any duty to the company, the employer is not limited to terminating the employment for cause. It is not limited to seeking damages directly tied to the employee’s wrongdoing. *It may also recoup all the salary it paid that employee from the time of the violation.* As Geneva asserts, this claw back can reach as far as a decade-old violation by Bavely. This novel cause of action has no direct support in Virginia law outside of this Court’s 2019 Order, which is a summary order that does not explain the Court’s reasons.² As with most fantasies, however, this one is not real.

Just last year, the Supreme Court of Virginia cited with approval respect for “the ancient maxim” that Virginia law disfavors forfeitures. *See Hunter v. Hunter*, 298 Va. 414, 424 (2020) (citing *Jones v. Guaranty & Indem. Co.*, 101 U.S. 622, 628 (1879)). *Hunter* raised this point in the context of will contests. *Hunter*, 298 Va. at 424. However, the Court recognized that principle was applicable to “many platforms of legal doctrine.” *Id.* Moreover, “[p]rovisions that require forfeiture are not favored in the law generally and will not be enforced *except according to their clear terms.*” *Rafalko v. Georgiadis*, 290 Va. 384, 402 (2015) (emphasis supplied) (internal citation omitted). From these cases, the clear principle is that forfeiture is disfavored,

² Geneva cites another unexplained Circuit Court Order, *Cent. Fid Bank v. First Nat’l Exch. Bank*, 1981 WL 188341, at *8 (Roanoke Cir. Ct. Sept. 4, 1981). As with the 2019 Order, *Cent. Fid* is a summary order without explanation or citation to any authority for its ruling. The *Cent. Fid.* court directed employees who stole an employer’s customer list just before quitting en masse to reimburse the employer their last month salary. This Court cannot find *Cent. Fid.* persuasive without knowing on what authority that court relied on to hold the employees’ last month salary was subject to forfeiture under Virginia law.

and unless a contract expressly provides for forfeiture, a court will not permit that remedy. This explains why so many companies include forfeiture provisions in their employee contracts.³

Contracts drive employment law in Virginia. *Willoughby v. Thomas*, 65 Va. 521, 532 (1874). It is true that every contract of employment implies the employee will obey lawful and reasonable orders from an employer. *Spotswood Arms Corp. v. Este*, 147 Va. 1047, 1061 (1926). However, the usual remedy is rescission of the contract—termination of the employment, not the recoupment of all compensation already paid. *See id.* The Restatement (Second) of Agency § 399 (1958) catalogues available remedies for when an employee violates his duties to an employer. Recoupment or claw-back of salary already paid is not one of the eleven possible remedies. The closest remedy on the list to Geneva's position is "restitution." However, Comment D lists examples of restitution—overpayment, erroneous payment, reimbursement for goods wrongfully sold, and reimbursement for use of a trade secret. It does not suggest full salary claw-back. Moreover, Geneva seeks equitable remedies for its causes of action. Thus, it limits itself to specific performance, rescission of the contract, and reformation of the contract. 1 Virginia Remedies § 36-7(K).⁴

Geneva does not argue a contractual right to forfeiture. Rather, it argues a general equitable right to recover employee compensation as damages for concealed employee wrongdoing. However, it fails to persuade the Court that Virginia law countenances a cause of action that permits wholesale forfeiture of wages already paid. To support its position, Geneva's most persuasive authority is the Restatement for the principle that:

[a]n agent is entitled to no compensation for conduct which is disobedient or which is a breach of his duty of loyalty; if such conduct constitutes a willful and deliberate breach of his contract of service, he is not entitled to compensation even for properly performed services for which no compensation is apportioned.

Restatement (Second) of Agency § 469 (1958).⁵ However, Geneva reads this rule too literally. In the comments, the Restatement clarifies that a wrongdoing agent "is not entitled to compensation which otherwise would be due him *because of the transaction.*" *Id.* at cmt. A (emphasis supplied). To claw back compensation already paid, a principal must tie specific payments to specific bad acts of the agent. It is not enough for the principal to cite the agent's wrongdoing and reclaim all payments it paid the agent without a tie-in. Geneva asks the Court to focus on

³ For a list of plan documents and individual agreements included in securities filings containing employee compensation claw back provisions as a remedy for breaches of company policy, see Executive Compensation 2019: Strategy, Design, and Implementation, SA018 ALI-CLE 83 (2019).

⁴ Damages are permitted in rescission cases on a transactional basis. 1 Virginia Remedies § 36-7(K) (citing *Millboro Lumber v. Augusta Wood Products*, 140 Va. 409 (1924) ("the party profiting by the fraud [may be ordered] to surrender the benefit he has received in the transaction")).

⁵ Geneva also cites to *E.L. Hamm & Assocs., Inc. v. Sparrow*, 306 B.R. 812, 841 (Bankr. E.D. Va. 2003) and Restat. 2d of Agency, § 469, cmt. E ("If the principal, in ignorance of the agent's faulty conduct, pays to the agent compensation or indemnity to which he is not entitled, the principal can maintain an action to recover the amount.")

Comment E, which does not have the transactional language of A. However, to read Comment E as Geneva does would neutralize Comment A. It would also be inconsistent with *Sunrise Continuing Care, LLC v. Wright*, 277 Va. 148, 157 (2009), wherein the Supreme Court of Virginia disallowed a principal from simply clawing back all monthly fees it paid its wrongdoing agent. “When an [employer] has proved a breach of contract, the burden of proof regarding damages does not then shift to the [employee]. The burden of proof remains with the [employer] to prove with reasonable certainty the measure of damages sustained.” *Id.* The high court did not allow the employer a blanket recoupment of all money it already paid the employee—it was required to tie the payment to the wrongdoing, or “the transaction” to use the Restatement’s language.

Geneva also relies on *Jackson v. Pleasanton*, 101 Va. 282, 289-90 (1903) for the proposition that a disloyal agent forfeits benefits received during the period of disloyalty. In that case, an agent agreed to purchase land for his principal and, after taking title in his own name, refused possession to the principal. The Court held the agent was not entitled to compensation for services and was liable for the fair rental value. However, cancellation of a commission from a specific, limited transaction is far removed from an employment arrangement such as that between Geneva and Bavely, spanning over a decade. The *Jackson* case cited a specific transaction and tied it to specific damages. Geneva does not do this. Rather it catalogues a list of Bavely’s transgressions and, without tying any of them to specific loss, seeks to reclaim all the compensation it paid him. Geneva cannot do this. It must match the damage to the transaction. For the same reason, Geneva’s reliance on *Schmidt v. Wallinger*, 125 Va. 361, 377 (1919), is misplaced. That case involved a brokerage commission on a real estate transaction tinged by broker fraud—again, a specific transgression tied to a specific commission.

Similarly, the final two cases cited by Geneva are unpersuasive. In *Nat’l Legal Rsch. Grp. v. Lathan*, 1994 WL 667058, at *2-3 (4th Cir. Nov. 30, 1994) (unpubl.) the court announced an “apportionment” concept wherein a court distinguishes between an employee’s properly rendered services and services tainted by disloyalty. “If an agent’s pay is apportioned, for example, to ‘periods of time’ or to ‘specified items of work,’ he will only lose his compensation for those periods or items that his disloyalty affected.” *Id.* at 2 (citing Restatement (Second) of Agency § 456 & cmt. B (1958)). In the present case, Geneva does not wield a scalpel to carve out compensation intimately connected to a specific act of wrongdoing by Bavely. Rather, it catalogues a long list of historical wrongdoing and, without considering any value Bavely may have added during his employment, simply claims all Bavely’s salary and benefits paid since 2007. This would fail even the *Lathan* apportionment test, which is really just the Restatement’s transactional rule by a different name.

In the present case, Geneva makes a blanket assertion that all Bavely’s wrongdoings should result in the forfeiture of over a decade of his compensation. Neither Geneva’s employee manual nor any contract requires Bavely to forfeit compensation already paid to him as a remedy for his violations of company policy. So, Geneva cannot pursue this remedy on that basis. If Geneva seeks Bavely’s compensation forfeiture on a transactional basis, its Amended Complaint must tie specific bad acts with a specific loss to recover damages, transaction by transaction. To

some extent, Geneva does this. It alleges Bavely used corporate resources for personal gain. (Am. Compl. ¶ 80-89.) However, the remedy for this is specific restitution, not general forfeiture of all salary and other compensation Geneva paid Bavely. The Court sustains Bavely's demurrer with leave to amend.

III. CONCLUSION

The Court holds an employer may not claw back an employee's salary, bonuses, and other forms of compensation the employer paid during a time when the employees concealed acts would have justified termination unless: (1) the employment contract provided for this relief, or (2) the employer can point to specific wrongdoing that led to specific damages. The relief would not be a recoupment of the compensation paid, but the value of the actual damages.

The Court sustains the Demurrer to Counts 20-23 of Geneva's Amended Complaint.

An appropriate Order is attached.

Kind regards,



David A. Oblon
Judge, Circuit Court of Fairfax County
19th Judicial Circuit of Virginia

Enclosure

OPINION LETTER

VIRGINIA:

IN THE CIRCUIT COURT OF FAIRFAX COUNTY

GENEVA ENTERPRISES, LLC,)
 et. al.,)
 Plaintiffs,)
v.) CL-2018-18124
)
DONALD B. BAVELY,)
 Defendant.)

MEMORANDUM ORDER

THIS MATTER came before the Court on Defendant Donald B. Bavely’s (“Bavely’s”) Demurrer to Plaintiffs’¹ (“Geneva’s”) First Amended Complaint. And,

CONSIDERING Bavely demurs to all but one count of the Amended Complaint;

CONSIDERING the Court, in an Order dated February 1, 2021, overruled the Demurrer as to Counts 2-12 and 17-19 and sustained the Demurrer as to Count 13 of the Amended Complaint; and

CONSIDERING the Court took the Demurrer to the remaining counts under advisement; it is

ORDERED the Demurrer to Counts 20-23 is SUSTAINED WITH LEAVE TO AMEND for the reasons set forth in the Opinion Letter dated February 17, 2021, which is incorporated herein by reference. And,

CONSIDERING Counts 14-16 allege against Bavely: Conversion, Money Had and Received, and Unjust Enrichment in the context of “Diversionary LLCs”; and

¹ The Plaintiffs are Geneva Enterprises, LLC and the Estate of Robert M. Rosenthal, represented by its Personal Representatives. In this Order the Court refers to both collectively as “Geneva.”

CONSIDERING “Diversionary LLCs” are “at least five limited liability companies that diverted corporate opportunities—and siphoned away revenue and voting control—from both Mr. Rosenthal and Geneva.” (Am. Compl. ¶ 3(a).) Those companies include Mobile Spartan, LLC; Dealer PPC; Jefferson Davis Porsche, LLC; Executive Lease Portfolio Management, LLC; and Stonecroft Trading, LLC. (*Id.* at ¶ 3(a)(i-v)); it is

ADJUDGED the Demurrer should be overruled for the same reasons stated from the bench when the Court overruled the Demurrer to Counts 17-19 of the Amended Complaint. They adequately state causes of action for which relief may be granted; and it is

ORDERED the Demurrer to Counts 14-16 is OVERRULED. And,

CONSIDERING Counts 24-27 allege against Bavely: Fraud, Conversion, Unjust Enrichment, and Money Had and Received in the context of the acquisition of interests in AV Automotive, LLC (“AV”); it is

ADJUDGED the gravamen of Counts 24-27 is Geneva’s claim it was tricked into making an unauthorized \$1 million loan to Bavely, with which Bavely obtained his interest in AV; and

ADJUDGED Geneva’s remedy can only be the proceeds of the wrongful loan, plus interest. However, Geneva is not seeking this—rather, it seeks to trace Bavely’s use of the loan money to unwind the value of Bavely’s investments made using that money. This is overreaching. By analogy, if a borrower tricks a lender into extending a loan, the lender’s remedy is the loan proceeds, plus interest—not the gains of any investment the borrower made from the loan funds. The analogy does not logically change if the lender and borrower jointly invest the loan funds. In both instances, the wrongful act was obtaining the loan. Geneva cites no persuasive authority for the proposition that a civil “fruit of the poisonous tree” doctrine exists wherein a defrauded lender’s remedies extend beyond the loss of the loan money plus interest to include investments made from that money. *Cf.*, 1 Virginia Remedies § 12-5 (2020) (“Traditional case law states that the recovery of a plaintiff in conversion cases is the value of the property taken, with interest.”) (citing *Buckeye Nat’l Bank v. Huff & Cook*, 114 Va. 1, 10-11 (1912)). Therefore, it is

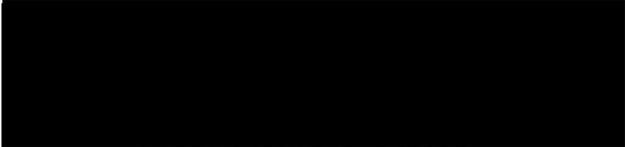
ORDERED the Demurrer to Counts 24-27 is SUSTAINED WITH LEAVE TO AMEND; and

ORDERED Geneva must file an Answer or Second Amended Complaint, if so advised, within 21 days of this Order. If no Second Amended Complaint is filed within 21 days, the counts for which the Court sustained the Demurrer shall be DISMISSED.

AND THIS CAUSE CONTINUES.

FEB 17 2021

Entered



Judge David A. Oblon

ENDORSEMENT OF THIS ORDER BY COUNSEL OF RECORD FOR THE PARTIES IS WAIVED
IN THE DISCRETION OF THE COURT PURSUANT TO RULE 1:13 OF THE SUPREME COURT OF VIRGINIA. OBJECTIONS
MUST BE FILED WITHIN 15 DAYS.