

Drafting Noncompete Agreements: The Employee Perspective

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General Points

- Note:
 - This outline is written from the employee perspective and how employees with noncompete agreements written into their contracts can get around enforcement when a new opportunity in the same sphere of business presents itself.
- We know that courts have seen an increase in litigation surrounding noncompete agreements. This trend didn't just happen on its own. More and more companies are requiring their employees to sign noncompete agreements. Twenty years ago, these contracts were tied to higher level jobs. However, in many areas of business, they are becoming the norm.
- Trade secret and noncompete cases have increased over two times in the last decade. <http://www.tradesecretnoncompete.com/tags/utsa/>
- In a tough economy, employers are enforcing their noncompete agreements through litigation more often to protect their legitimate business interests.
- Judges have also become more sympathetic to employees, given high unemployment rates.
- Laws generally favor open competition and employers battling it out to keep top employees happy. At-will employees are always free to leave their employment and find something better.
- California courts have led the trend against overly broad noncompete agreements by basically making such covenants unenforceable. Cal. Bus. & Prof. Code § 16600; see e.g., Edwards v. Arthur Andersen LLP, 44 Cal. 4th 937 (Cal. 2008).
- Rule 5.6 of the Rules of Professional Conduct prohibits attorneys from restricting their ability to practice law, so attorneys cannot be bound by a noncompete.

Preliminary Advice to Clients Before Signing

- Try to Negotiate and Consult an Attorney
 - Attorneys should encourage clients to negotiate specific terms of their noncompete and understand which terms are enforceable.
 - Clients should know that it could be worth it in the long run, especially if they are going into a competitive industry.

The Simple Definition

- A noncompete is an agreement between two parties in which one party agrees not to pursue comparable employment with a competitor.
- There are two types of noncompetes. Employee noncompetes arise out of an employment relationship. The other is a catch-all type noncompete that arises out of another situation, such as the sale of a business or a partnership agreement.

Some Generally Suspect Clauses in Noncompetes

- (1) Geographic Limitations
 - Employers can try to make their noncompetes as broad as possible with respect to geography and, in some cases, may try to restrict the whole country or region as off limits.
 - If the dispute goes to litigation, and you left your company in Minnesota and are trying to go to a competing company in North Carolina or even trying to establish a relationship with a new client there on your own, and your previous employer has never done business in North Carolina, you have very strong argument for a judge that preventing you from pursuing that work is retaliatory.
- (2) Time Span Restrictions
 - The standard time on most noncompetes is six months to a year. Anything more than two years will likely be held to be unreasonable.
- (3) Another Way: The Non-Disclosure and Non-Solicitation Agreements
 - Traditional noncompetes will usually have the time limit restriction clause, discussed above. Another option would be to try to fight for a "non-disclosure" or "non-solicitation" agreement that allows for immediate employment after departure.
 - Non-disclosure agreements stipulate that departing employees can't make off with valuable research.
 - Non-solicitation agreements bar former employees from going after important clients, minus those they cultivated before joining the company.

The Question of Enforceability

- The General Rules:
 - The state recognizes noncompete agreements.
 - There is consideration, just like any other contract.
 - There is a legitimate business interest.
 - The restriction is not more than what is necessary to protect the employer's business interest (not overbroad).
 - There is no undue burden on the ability of the employee to make a living.

- (1) The Forum
 - Noncompete agreements are enforceable throughout the country, with California being the exception to the general rule. As noted, California has an across the board prohibition on noncompete agreements in the employment context.
 - However, employers are not barred from bring actions against former employees that allege improper use of trade secrets obtained during their former employment.
 - As noted, enforcement of noncompetes depends greatly on the circumstances surrounding the agreement. State courts also will have a wide variance of dispositions in how they deal with noncompetes.
 - One thing does remain constant across borders, if the noncompete agreement has a limited reach, a limited time frame, and limited geographic boundaries, it will most likely be enforceable.
 - The legitimate business interests’ employers must have for enforcement also has a wide variance state to state, but will usually call for the protection of goodwill, trade secrets, and important documents/information of the employer.

- (2) Consideration
 - Most states require very little consideration, beyond general employment.

- (3) The Legitimate Business Interest
 - Employer must have a legitimate business interest.
 - Some quick examples where the employer has no legitimate business interest:
 - Lower-level employees.
 - An employer no longer has a legitimate business interest if it phases out of an area of their business.

 - Examples of Legitimate Business Interests (recognized by most states)
 - Trade secrets
 - Confidential business information
 - Customer or client lists

 - What’s a “Trade Secret?”
 - Trade secrets are the only major type of intellectual property law governed primarily by state law.
 - The definition varies from state to state, but for those that have adopted Uniform Trade Secret Act (UTSA), the following definition applies:
 - “information, including a formula, pattern, compilation, program device, method, technique, or process, that: (i) derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use, and (ii) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.”

- There are three main components that constitute a trade secret: (1) information; (2) value; and (3) secrecy.
- Many companies are implementing Trade Secret Protection Programs.
 - These programs seek to guard against the above concern by having a team of people look at agreements, identifying trade secrets, and confirming the company is making an effort to keep the secrets secret.
- (4) The Noncompete is too Broad
 - Blue Penciling
 - This legal concept, for states that have it, allows courts to redraft and redraw noncompetes as they see fit. Usually this takes place because the noncompete agreement is way too broad. The objective behind this concept is to grant courts the authority to make the agreement no broader than it has to be in order to protect the legitimate business interests of the employer.
 - Remember, the employer first must prove they have a legitimate business interest. However, if they fail to do so, the blue pencil won't necessarily be too dull to write. The court is still likely to restrict the employee in some way because they signed the agreement. However, if the court tries and fails to redraft the borders of the noncompete, it has the authority to nullify it.
- (5) Undue Burden
 - Also referred to as undue hardship. An example of a noncompete that could be voided on these grounds would be one that goes beyond the two year reasonable time frame ban on seeking employment with a competitor.
 - Some employers pay former employees during the noncompete period in order to get around an undue burden argument.
- Additional Point: The Facts Always Count
 - It could be important why you left.
 - If you quit, a noncompete is more easily enforceable.
 - If you were laid off, it might not.
 - Courts are more reluctant to enforce noncompetes when job loss is not the employee's fault.
 - Were you fairly compensated for signing the noncompete?
 - Employees are giving up some of their rights when they sign noncompetes.
 - The job itself, as consideration, is usually enough.
 - But if you are already employed and your employer approaches you with a noncompete, but does not offer you any additional consideration, or threatens termination if you do not sign it, enforcement is unlikely.

Miscellaneous Issues

- (1) Inevitable Disclosure
 - The doctrine of inevitable disclosure is based on the concept that an employee will use trade secrets of his former employer in a new position, because of the type of industry and the similarity between his current and former employers, “unless [he] possesse[s] an uncanny ability to compartmentalize information.” PepsiCo, Inc. v. Redmond, 54 F.3d 1262, 1269 (7th Cir. 1995).

- (2) Duty of Loyalty
 - When an employee in a position of power, or who may be deemed as a key employee, puts her own interests ahead of that of her former company to benefit her, and/or her current employer, she has breached the duty of loyalty. “An employee who uses the power of his employment responsibilities to harm his employer breaches his duty of loyalty” InfoCorp, LLC v. Hunt, Case No. 2007AP2887, 2009 WL 4800140 (Wis. Ct. App. Dec. 8, 2009) citing Burg v. Miniature Precision Components, Inc., 111 Wis.2d 1, 330 N.W.2d 192 (1983).

- (3) Severability
 - If a specific provision in a noncompete is found to be invalid or not enforceable, the court can disregard that specific provision, but still enforce the rest of the agreement.

- (4) Garden Leave
 - These clauses are relatively new. If the employer wants to put a buffer-zone in place for a reasonable period of time before an employee can be terminated to safeguard their interests, they may try and put in this type of provision in their noncompetes.
 - Essentially, there are two types of garden leave clauses in use.
 - The first is a notice restriction where the employee will be required to provide the higher ups at his employer with ample notice, as provided for, before effectively resigning.
 - The second is a noncompete agreement with pay and a direct severance arrangement. This clause essentially compensates the employee for the period between the end of their employment with their previous employer and their new employer, as provided for by the clause.
 - The first type of clause can be structured to provide for immediate removal of the resigning employee, with pay, if the employee wants to leave immediately. The employment is then effectively terminated but the resigning employee must still receive a paycheck for that interim period. Their ability to get that paycheck also could hinge

upon showing that they cannot find another job because of the garden clause provision.

- The goal of the garden leave clause is to provide the former employer with notice and a short period of relief when a high-level executive leaves the company voluntarily.