

Enforcing Noncompetition Agreements Part I: Assessing the Need and Putting Agreements in Place

Employers often ask: “Are noncompete agreements enforceable?” The answer is yes — and no. Courts generally enforce reasonable agreements when necessary to protect particular employer interests. On the other hand, courts generally do not enforce noncompete agreements when no real protectable interests are at stake, the restrictions are unreasonable, or the employer has undermined its ability to enforce them by, for example, engaging in “selective enforcement” of such agreements. This month’s edition of the *Employment Law Advisor* will review some noncompete basics and address steps employers should take to put enforceable agreements in place. Next month’s edition will focus on what an employer can do upon learning that an employee is leaving to join a competitor.

When Is a Noncompete Appropriate?

A noncompetition agreement is a type of “restrictive covenant,” i.e., a promise by an employee not to engage in certain behavior that is contrary to the employer’s interests. A covenant “not to compete” generally is a promise that the employee will not engage in business competitive with the employer during and for a certain time period following termination of employment. Such covenants are often accompanied by covenants “not to solicit” the employer’s customers and covenants “not to disclose” the employer’s confidential business information.

To be enforceable, a noncompete must be (i) necessary to protect an employer’s legitimate business interests, (ii) reasonable in time and scope, (iii) consistent with public interest and (iv) supported by consideration.

The two key protectable employer interests are (i) an employer’s relationship with customers, clients and vendors (also called “good will”) and (ii) trade secrets and other confidential business information.

Goodwill encompasses a variety of intangibles, including market position and reputation. Confidential business informa-

Do your Noncompetition Agreements:

- ✓ Encompass reasonable duration and appropriate geographical scope?
- ✓ Offer “consideration” to the employee signing?
- ✓ Permit the you to assign the agreement to an aquiror if necessary?

Then, read on...

tion encompasses commercially valuable information not generally known outside of the company, which the company has taken reasonable measures to protect. Unless good will or trade secrets/confidential business information is at stake, an employer cannot prevent an employee from leaving to go to a competitor. In other words, noncompetes can be used to prevent unfair competition (involving misappropriation of good will or confidential business information) but not ordinary competition.

Before requiring an employee to sign a noncompete the employer should ask itself: Will this employee control customer relationships and/or have access to confidential business information? Will the employee be in a position to harm the employer’s business if the employee were to use the good will or confidential information on behalf of a competitor? If the answer to both questions is yes, then the employer should consider whether covenants not to solicit customers and not to disclose confidential information are adequate to protect the employer’s business interests, or whether it is necessary for the employer to restrict the employee from even working for a competitor.

The unnecessary and overly broad use of noncompetes may negatively impact an employer’s ability to enforce such an agreement when it really matters. If every employee from the night janitor to the CEO is expected to sign a noncompete, a court may question whether any protectable interests are truly at stake.

What Is the Proper Scope of Noncompete Restrictions?

Noncompetes must be reasonable in duration and geographical scope. Employers are at risk if they draft agreements in broad terms and presume that a court will enforce them on a scaled back basis. In Massachusetts and many other states courts may scale back overly broad noncompetes as appropriate, but courts also may refuse to enforce unreasonable noncompetes altogether. The much better approach is for employers to use noncompetes that provide only the protection needed.

Except in situations involving a sale of a business, noncompete restrictions of more than one year in duration may not be enforced. In some lines of business six months may be more appropriate. Further, it is not unusual to set different durations for different types of restrictive covenants. For example, an agreement may provide that non-compete restrictions continue for six months while the covenant not to solicit customers continues for one year and the covenant not to disclose confidential information continues indefinitely.

The appropriate geographical scope for a noncompete usually depends on the nature and scope of the employer’s business and the protectable interest(s) at stake. Where good will is the only busi-



ness interest involved and the employee's customer contact is limited to a particular region, the noncompete should be limited to that region. Where confidential business information is the business interest (and a covenant not to disclose may not provide adequate protection), it may be appropriate for the noncompete to have no geographical limitations.

Because the scope and types of restrictive covenants that are appropriate typically vary from position to position, it is often not possible (or at least not wise) for an employer to have a one-size-fits-all agreement for all employees to sign. Moreover, courts may be more inclined to enforce a noncompete that is specific to a particular employee, as opposed to a fill-in-the-blank agreement.

What Must an Employee Receive in Exchange for the Noncompete?

Noncompetes and other restrictive covenants must be supported by "consideration." This means that an employee must receive a benefit — either a promise or something else of value — in exchange for the employee's promise not to work for a competitor. When an employee is presented with a noncompete prior to starting new employment, there is no question that consideration exists to support the agreement. In this situation, the employer should make the requirement of signing a noncompete clear in its offer letter so that the employee cannot later assert that the noncompete was imposed after the offer of employment was accepted. In fact, we suggest that employers attach a form of the noncompete to the offer letter so that the employee cannot later claim that he or she did not receive full disclosure of the restrictive covenants.

When an employee is asked to sign a noncompete "mid-employment" the employer can take the position that continued employment of the employee constitutes sufficient consideration to make the noncompete covenant enforceable. However, the law is unsettled in this area, and some courts have held that the promise of continued at-will employment does not suffice. Consequently, we recommend that employers offer employees something of value as additional

consideration for mid-employment noncompetes. This consideration can be in the form of additional compensation, such as a raise, bonus, stock options, or acceleration of a benefit.

What happens to a noncompete if an employee's position changes due to a promotion or transfer? A few Massachusetts cases have held that each time an employee's relationship with an employer changes materially, a new noncompete must be signed. Whether a particular promotion or job transfer is a material change is a matter of degree. Consequently, we recommend that employers review the noncompete (and other restrictive covenants) for each employee who has a change in position. An employer may require the employee to sign a new noncompete, or sign a document acknowledging the position change and that the employee's noncompete remains in effect. A less burdensome (but possibly less effective) response to this issue is to include in all restrictive covenants language which puts the employee on notice that the covenant will remain in force and effect regardless of any changes in the terms and conditions of employment, including changes in duties, position or compensation.

What Are Other Important Provisions and Considerations?

Injunctive Relief and Attorneys' Fees

Noncompetes should identify the protectable interests and include an acknowledgment that the interests are vitally important, that breach of the noncompete will cause irreparable harm to the employer's business, and that the employer is entitled to immediate injunctive relief in the event of such breach. Noncompetes also should require the employee to reimburse the employer for its attorneys' fees if the employer has to file suit to enforce the agreement. While a court ultimately may choose not to enforce an attorneys' fees provision, the existence of such a provision can provide substantial leverage to the employer.

Choice of Law and Forum Selection

Noncompetes should provide that the law of a particular state, such as Massachusetts, controls the interpretation and enforcement of the noncompete agreement, that all actions involving disputes arising under the agreement must be brought in the particular state, and that the employee consents and submits to the jurisdiction of the

courts in the state. Many employers have multistate operations and in some states, most notably California, noncompetes may be enforceable only in very limited circumstances. "Choice of law" and "forum selection" clauses give employers some degree of predictability in assessing the likely outcome of a noncompete dispute, as well as where it will be litigated.

Assignment

Noncompetes should expressly permit the employer to assign the agreement to an acquirer. The existence of enforceable noncompete agreements for key people is often an important issue when a business is being acquired. Unless a noncompete contains a proper assignment clause, courts are unlikely to permit the assignment of the noncompete to the acquirer without the employee's express consent.

Take a Careful and Consistent Approach

Employers should take steps to ensure that all restricted covenants are, in fact, (i) signed by the employee and employer and (ii) maintained in a secure place. It is not unusual for an employer to discover that a signed noncompete is "missing" after an employee has left to join a competitor. Employers should also be careful to treat confidential business information as confidential. Developing a program to protect proprietary information and trade secrets (e.g., labeling "confidential" and restricting access) strengthens an employer's position that its business information is truly confidential and that the restrictive covenant should be enforced.

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