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Noncompetition Agreements

Employers Should Avoid One-Size-Fits-All Noncompetition Agreements, Attorneys Say

It's a common practice for employers to have executive-level employees and workers with special skills or access to confidential information sign noncompetition agreements, but recent attention has been brought to restrictive covenants signed by lower-level employees.

There are several reasons employers choose to have workers sign noncompetition agreements, employment attorneys said in a series of interviews.

They serve to protect the client relationship, particularly in sales and other customer-facing positions, Kenneth J. Vanko, an attorney with Clingen Callow & McLean LLC in Lisle, Ill., told Bloomberg BNA Feb. 16. They also protect trade secrets and other information that may be damaging in the hands of a competitor, he said.

Noncompetition agreements also can be used as a retention tool, Katherine S. Somervell, a management-side attorney at Bullivant Houser Bailey PC in Portland, Ore., and Seattle, told Bloomberg BNA Feb. 19.

''Recent revelations that low-wage earners have been subject to restrictive covenants at companies like Jimmy John's and Amazon have created some backlash to the practice,'' Erin J. Hendrickson, a professor at William & Mary Law School, told Bloomberg BNA Feb. 18 in an e-mail.

''Low-wage earners who leave their jobs to work for competitors are not often going to be in a position to compromise legitimate business interests. Therefore, it's appropriate to be skeptical of these agreements, since they limit the ability of employees to earn a living,'' said Hendrickson, who formerly represented the Internal Revenue Service in labor and employment matters.

''However, from an employer's point of view, having these employees sign non-compete agreements is an easy and inexpensive way to help prevent employee turnover,'' she said.

Low-Wage Worker Agreements Under Scrutiny. ''A reason employers may want to have lower-level employees sign noncompetes is to protect their commitment to training and development,'' Vanko said.

''An employer may not receive much benefit from the employment relationship during a training period, and it therefore may want to protect its investment by limiting the risk of losing that employee to a competitor,'' said Vanko, who represents a mix of employees and employers, including individual executives and small, family-owned businesses.

He said most disputes between businesses and low-wage earners don't get to the litigation stage.

By the time the issue is litigated, the noncompete period has usually passed, Susan Bristow-Ford, a business and intellectual property litigator in Portland, Ore, told Bloomberg BNA Feb. 17. In many cases, injunctive relief is the only remedy that makes sense, she said.

Somervell said noncompetition agreements are generally not enforceable against low-wage earners, because those employees don't usually have the level of information that businesses have an interest in protecting. But some workers may not realize their agreements aren't enforceable, she said.

In the Jimmy John's case, two assistant store managers challenged the sandwich chain's practice of having store employees sign agreements that prevented them from working for competitors within a three-mile radius of the worker's former store (*Brunner v. Liautaud*, 2015 BL 99634 (N.D. Ill. 2015)); (68 DLR A-2, 4/9/15); (206 DLR A-11, 10/24/14).

The employees sought declaratory and injunctive relief to determine the legal interests, validity and enforceability of the agreements, but the court found that the assistant store managers didn't have standing to bring the claims.

Judge Charles P. Kocoras of the U.S. District Court for the Northern District of Illinois held that the store managers didn't show a ''reasonable apprehension'' that Jimmy John's intended to enforce the agreements.

''Even if the agreement would be unenforceable, there's a psychological impact in that employees may feel that they don't have the option of seeking employment elsewhere,'' Hendrickson said. ''Further, low-wage employees often won't have the time, resources, or negotiating power to challenge the use of noncompetes.''

Vanko said other potential employers will make hiring decisions based on the path of least resistance. ''If an employer has two equally qualified candidates, it will choose the one without the noncompete,'' he said.

Amazon stopped its practice of having warehouse workers sign noncompetition agreements after it faced public scrutiny over the issue (106 DLR A-16, 6/3/15).

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Enforceability Depends on State Laws. The enforceability of restrictive covenants is examined under state law.

''Some states have passed legislation regarding the use of restrictive covenants, but many have not,'' Hendrickson said.

Somervell said California disfavors noncompetition agreements, whereas Washington will enforce them if they are reasonably necessary to protect the business or the goodwill of the employer.

Under Oregon law, an employer must provide a two-week notice to new hires that they will be required to sign a noncompetition agreement as a condition of employment.

''This is so the employee isn't blindsided at the start of employment,'' Somervell said. It gives workers time to consider the agreement and the opportunity to negotiate the terms, she said.

The Oregon statute has several other components, including a salary threshold. And if an employer wants to have an existing employee sign a noncompetition agreement, it must provide a ''subsequent bona fide advancement.''

There is some debate over what constitutes a bona fide advancement. In a case involving Nike, the U.S. Court of Appeals for the Ninth Circuit said a one-year noncompetition agreement was enforceable under Oregon law against an employee who sought to work for competitor Reebok because he signed it in connection with a promotion to a higher position within Nike (*Nike, Inc. v. McCarthy*, 379 F.3d 576, 21 IER Cases 1089 (9th Cir. 2004)); (157 DLR AA-1, 8/16/04).

Bristow-Ford said it's unlikely that a bonus at the time of separation would work under Oregon law because it isn't an increase in rank.

In *Cardoni v. Prosperity Bank*, 805 F.3d 573, 40 IER Cases 1388 (5th Cir. 2015), the Fifth Circuit denied a preliminary injunction to a bank that sought to enforce restrictive covenants in agreements with former executives (210 DLR AA-1, 10/30/15).

The agreements in *Cardoni* had a choice of law provision designating Texas law, but the bankers were located in Oklahoma.

In that case, the Fifth Circuit held that ''applying Texas law, which takes a more permissive attitude of both noncompetition agreements and the ability to reform them, would contravene Oklahoma's statutory aversion to noncompetition agreements.''

Vanko said another issue employers have to consider for at-will employees, rather than executives with employment agreements in place, is what constitutes consideration for a noncompetition agreement under the state's law.

''States are split on this issue when it comes to at-will employees,'' he said. ''Employers have to consider what the employee needs to receive in order to create a binding agreement.''

Employers Should Tailor Agreements. Employers should identify those employees by title or type of work who should have an agreement in place, Vanko said. They should understand the business interests and tailor the agreement, he said, and they should also have an understanding of what courts have done in the past in their industry.

If an employer looks at the applicable law and notices its noncompetition agreement isn't enforceable, it should have employees sign a nonsolicitation agreement, Somervell said.

A nonsolicitation provision is another form of restrictive covenant that usually prevents employees from pursuing the business's clients or sharing customer lists with a new employer.

Courts, including in California, have generally enforced nonsolicitation agreements, Somervell said.

Even though the court in *Cardoni* declined to enforce the bank's noncompetition provision, it found that nonsolicitation provisions in the executives' agreements may be enforceable. Oklahoma law permits restrictions on soliciting customers from a former employer, it said.

Bristow-Ford also counsels clients to use well-drafted nondisclosure agreements—or confidentiality agreements—that include liquidated damages. A nondisclosure will protect proprietary information, she said.

As for employees, Vanko said they should try to negotiate the terms of the agreement. ''They can attempt to narrow the scope or tailor it to the particular job. They could also ask to reduce the time to one year, nine months or even six months,'' he said.

Vanko also said employees can ask employers to clarify the terms. ''An employer may have pulled the agreement from a website and the terms may not seem to fit the employer's business or the employee's job,'' he added.

''If an employee asks to see the agreement before accepting the job, in some circumstances the employee can evaluate and decide whether the offer is worth taking,'' Vanko said.

Federal and State Proposals Seek to Limit Use. ''There seems to be a growing sense that major corporations should not be allowed to discourage or prevent low-level employees from seeking better, higher paying employment elsewhere,'' Hendrickson said. ''Many see this as yet another example of big business exploiting the little guy to make a buck.''

''Last year, a bill banning the use of non-compete agreements for low-wage earners was introduced in the U.S. Senate, and Washington State is currently considering legislation to limit the use of non-compete agreements,'' she said (106 DLR A-16, 6/3/15). ''Given the current political and economic climate, I would not be surprised to see other similar proposals in the near future.''

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