# THE EVER-CHANGING PLAYING FIELD: EVOLVING LEGISLATIVE AND JUDICIAL SCRUTINY OF NON-COMPETE AGREEMENTS

By: Matthew A. Moeller

In business, change is both constant and inevitable. One change that often causes concern is when an employee or group of employees leaves a company and later goes to work for a competitor. This occurrence often triggers the application of a non-compete agreement that was executed at or likely near outset of the employment relationship. This can send both corporate and outside counsel scurrying to review the agreement to determine what is in it and how it will affect the departing employee's ability to compete with the company. Non-competes are used to protect a company's confidential information, client relationships, trade secrets and workforce. As a general concept, non-competes are disfavored but allowed, with North Dakota being the only state in the country that has a blanket prohibition against non-competes.

Recent developments in state judiciaries and legislatures demonstrate that just as in business, change is also constant and inevitable in the law of non-competes. Legislatures and courts have been proactive in limiting non-competes and scrutinizing certain aspects of the agreements. Legislative activity has been especially brisk in the healthcare and technology sectors. In July 2016, both Connecticut and Rhode Island passed laws restricting the application of non-competes to physicians. The Rhode Island law eliminates any restriction on the right to practice medicine in an employment contract, partnership, or other professional relationship involving a state-licensed physician. However, the law does not apply to the sale and/or purchase of a medical practice if the non-compete is less than five years in duration.

Similarly, while not as comprehensive, the Connecticut legislature established specific limits for the enforceability of a non-compete in any new, amended, or renewed physician agreement. The new law allows a duration of only a year and limited the geographical scope to a mere fifteen miles from the primary site where the physician practices. The law also renders a physician non-compete unenforceable if the physician's employment is terminated without cause. However, the law is silent as to the circumstances which would constitute termination without cause. Furthermore, in July 2015, the Hawaii legislature passed a law that prohibited non-competes relating to an employee of a technology business. The law defines a technology business as one that drives most of its gross income from the sale or license of products or services resulting from its software development or information technology development or both. The actions by state law makers illustrate the importance they place on not restraining trade in high demand industries that heavily influence society.

Recent court decisions emphasize the importance of the interplay between the concept of consideration and the nature of the employment relationship. In *Durrell vs. Tech Electronics, Inc.,* an at will employee, who was terminated after returning from a Family Medical Leave Act absence, filed suit seeking damages and a declaration that the non-compete portions of his employment agreement were unenforceable. *Durrell vs. Tech Electronics, Inc.*, No. 4:16 CV 1367 CDP, 2016 WL 6696070 (E.D. Mo. Nov. 15, 2016). The non-compete portion of his agreement prohibited the association with any company carrying on a similar trade or business within a one hundred fifty-mile radius of St. Louis or Columbia, Missouri for a post-termination period of one year. The plaintiff claimed that the agreement was unenforceable because an at will relationship cannot form the basis of consideration for a non-compete. The United States District Court for the Eastern District of Missouri agreed, reasoning that in such a relationship the employer makes no promise to do or refrain from doing anything that it is not already entitled to do, and the employer can still terminate the employee for any reason. Consequently, there must be another source of consideration.

Similarly, in *Jumbosack Corp. v. Buyck,* an employer sought review of the trial court's summary judgment ruling that its non-compete was not supported by valid consideration. *JumboSack Corp. v. Buyck*, 407 S.W.3d 51 (Mo. Ct. App. 2013). After working for six months, the defendant employee executed a non-compete that

*Continued on page 15*

## THE EVER-CHANGING...

Continued from page 6

prohibited contact with the company customers for three years after the termination of his employment. He later resigned, and accepted a position with a competitor. The company sought a temporary and permanent restraining order, injunctive relief, and damages based on an alleged breach of the agreement. After granting the company's petition for a TRO, the trial court granted the employee's motion for summary judgment explaining that the employer cannot enforce the non-compete agreement due to employer's prior breach of the employment agreement and lack of consideration. However, the appellate court found that access to the employers new and existing customers as well as continued at will employment, salary, and commissions constituted adequate consideration for a non-compete agreement. The court further reasoned that the continued attendant access to protectable information and relationships was adequate consideration for a non-compete executed six months after the consummation of the employment relationship.

Courts are also focusing on the nature of an employee's departure in determining the enforceability of a non-compete. For example, a New York court recently held that employer who terminated an employee without cause could not enforce a non-compete agreement. In *Buchanan Capital Mkts, LLC v. DeLucca,* an employer sought to enforce non-solicitation portions of a non-compete against employees who sought business from the employer's clients soon after being terminated. *Buchanan Capital Mkts, LLC v. DeLucca, et al* 41 N.Y.S.3d 229 (N.Y. App. Div. 2016). The court reasoned that the plaintiff could not show the necessary likelihood of success on the merits because, as a matter of law, such restrictive covenants are not enforceable if the employer (plaintiff) does not demonstrate "continued willingness to employ the party covenanting not to compete."

Even more recently, a Texas court affirmed summary judgment on behalf of an employee based on language that did not clearly specify whether a non-compete provision was triggered solely through the employer's termination of the employment relationship. In *East Texas Copy Systems, Inc. v. Player,* the defendant sold his business and entered into an asset purchase agreement that contained a non-compete provision and incorporated a separate non-compete agreement. *E. Texas Copy Sys., Inc. v. Player, No.* 06-16-00035-CV, 2016 WL 6638865 (Tex. App. Nov. 10, 2016). The agreements provided that if his employment was terminated without cause within two years, the non-compete provisions would no longer be binding. The defendant resigned within the two-year period and immediately resumed work at a competing business. The trial court granted summary judgment for the defendant, and the appellate court affirmed. The court reasoned that despite the presumed understanding that the provision was to protect defendant from a pre-mature, not-for-cause termination, the evidence was insufficient to demonstrate that was its sole purpose. The court further articulated that the bilateral right made sense from a risk allocation standpoint since this was a new, un-tested business venture.

The recent legislation and court decisions demonstrate that scrutiny of non-competes is as intense as ever. Both corporate and outside counsel must have a thorough understanding of the requirements for a bona fide non-compete as well as possible nuances in the applicable state jurisprudence on enforceability. It's clear that in the healthcare and technology sectors, states are taking a very aggressive line on non-competes. It will be interesting to see if other states follow suit, eventually eliminating or severely limiting non-competes across both sectors and other sectors that are viewed as highly important. Moreover, the context of the employment relationship is also drawing a very discerning eye regarding valid consideration and the nature of the termination of the employment relationship. Courts are trending towards requiring more than a simple at will employment relationship in order to enforce a non-compete, and termination without cause may preclude an employer from enforcing a non-compete regardless of who terminates the relationship.

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