Employer Beware: Is Your Noncompete Agreement Enforceable?

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Employers routinely require employees to enter into noncompete and nonsolicitation agreements upon commencing employment in order to protect confidential information, trade secrets, and business relationships from being used for competitive advantage. Once an employee executes noncompetition and nonsolicitation covenants (often referred to as restrictive covenants), many employers assume such information and relationships will be legally protected after the employee separates from employment. This is not necessarily the case.

Laws regarding noncompete and nonsolicitation agreements vary from state to state. This article focuses on restrictive covenants entered into in the employment context. In addressing this topic, it is important to draw a clear distinction between restrictive covenants entered into in the employment context and those entered into in the sale of business context (which are typically subject to less scrutiny because they are viewed as necessary to protect the goodwill purchased by the buyer). While several jurisdictions generally support reasonable restrictive covenants in the employment context, a number of others strictly limit an employer’s ability to restrict the actions of departing employees. Certain of those states imposing particularly strict limitations are briefly addressed below.

In California, a state that is widely recognized as employee—not employer—friendly, noncompetition agreements in the employment context are invalid and unenforceable. Further, nonsolicitation covenants are subject to very strict limitations that allow the employer to protect against only the use of the employer’s trade secrets in soliciting customers post-termination of employment. Similarly, North Dakota, Oklahoma and Montana law also contain strict provisions regarding restrictive covenants in the employment context.

North Dakota law explicitly prohibits noncompetition agreements by statute; the North Dakota Supreme Court has also determined that agreements prohibiting the post-employment solicitation of customers are invalid pursuant to this statute. Oklahoma law bars noncompete agreements, though an exception exists allowing an employer to prohibit former employees from directly soliciting the sale of goods, services, or a combination of goods and services “from the established customers” of a former employer. Montana’s noncompete statute generally prohibits restrictive covenants in the employment context. Despite this prohibition, however, Montana has upheld restrictive covenants contained in employment agreements under certain narrow factual circumstances.

Several other states also severely restrict the scope of such agreements. Colorado law, for example, limits
covenants not to compete in the employment context to:
(1) executive and management personnel and officers and
employees who constitute professional staff to executive
and management personnel; (2) contractual provisions
providing for the recovery of the expense of educating
and training an employee who has served an employer for
less than two years; and (3) contracts for the protection of
trade secrets. Restrictive covenants not falling within the
statutory exceptions are void under Colorado law.

In Louisiana, noncompete and nonsolicitation provisions
are only valid if limited to a specified parish or parishes,
municipality or municipalities, or parts thereof, as long as
the former employer carries on a like business therein, and
the covenant does not exceed two years from termination
of employment. Similarly, South Dakota law provides
that an employee may agree with an employer not to
directly or indirectly engage in the same business or
profession as his/her employer for a period not to exceed
two years, or to refrain from soliciting existing customers
of the employer within a specified county, municipality
or other area for a period not to exceed two years from
termination, if the employer carries on a like business
therein.

A few states, like Wisconsin, Nebraska and Arkansas,
allow reasonable noncompetition and nonsolicitation
agreements, but will simply invalidate an agreement
entirely if a court determines the agreement is not
reasonable. These states, along with some others,
generally refuse to modify or otherwise reform
agreements determined to be overbroad in scope. In such
states, it is particularly important to narrowly tailor
noncompetition and nonsolicitation covenants in order to
maximize the likelihood of enforcement.

With the above as brief background, it should be clear
there is no “form” noncompetition or nonsolicitation
covenant that will pass muster in every state. Employers
should carefully consider an employee’s position, the
interests the employer desires to protect, and the state
in which the employer and employee reside in crafting
restrictive covenants for a particular employee. The failure
to do so may result in severe and damaging business
consequences.

Is your noncompete enforceable? Employers are
encouraged to contact qualified legal counsel to assess the
enforceability of current agreements with employees and
before drafting new agreements in order to increase the
likelihood that such agreements will be enforceable.

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