

Non-Compete Agreements: How Employers can Define and Protect Their Legitimate Business Interests



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Today, downsizing and the reality of transient employment relationships have forced employers to further protect their economic interests. The departure of well-trained, highly productive employees creates a potential threat to the business. These employees often have significant knowledge of the company, which they could share with a competitor or use to start their own business and compete directly with their former employer. To defend their business, and not jeopardize continued, long-term success, one valuable approach is to have employees sign a non-compete agreement ("non-compete"). In the employment context, a non-compete is usually part of an employment agreement where the employee agrees for a specific period of time and within a particular geographic area to refrain from competition with the employer. This may include the employee not working for a competitive business within a certain geography or location; not soliciting clients, accounts or prospects for a period of time; or not hiring certain employees from the former employer.

When properly drafted however, non-competes can provide a legal remedy thereby offering protection. Consequently, it is vital that employers be familiar with how to create an enforceable non-compete. To insure enforceability, employers must balance the necessity of protecting their legitimate business interests with the fair interests of the employee. Each non-compete should be judged independently, paying close consideration to the status of and type of business, the employees involved, the interests of the business to be protected, and the laws of the state interpreting and enforcing the agreement.

A well-constructed non-compete may contain the following provisions:

- (1) A "non-competition" provision preventing a previous employee from engaging in an activity that may, or does, compete with their previous employer;
- (2) A "non-solicitation" provision restricting the employee from soliciting customers and/or prospects;
- (3) A "non-solicitation" provision restricting the employee from soliciting or hiring other employees of the company;
- (4) A "non-disclosure" or "confidentiality" provision, limiting an employee's use of confidential, proprietary, or trade secret information;

(5) A "choice-of-law" and "venue" provision defining which state's law will be used to interpret the agreement and;

(6) An "attorney fee" provision indicating which party is responsible for attorney fees, costs and expenses.

The law values free mobility of employees as well as open and fair competition. Accordingly, some courts disfavor non-competes. Nevertheless, courts will enforce a non-compete if it is reasonable and protects an employer's legitimate business interest.

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Both New Jersey and Pennsylvania protect trade secrets, confidential business information, employer good will, and customer relationships. A non-compete entered into solely to restrict competition will not be enforced.

In New Jersey, the test for determining whether a non-compete is unreasonable, and thus unenforceable, requires the court to determine whether:

- (1) The non-compete was necessary to protect the employer's legitimate business interests;
- (2) Whether it would cause undue hardship to the employee; and
- (3) Whether it would be injurious to the public.

Similarly, in Pennsylvania the non-compete must be:

- (1) Ancillary to either an employment relationship or another lawful transaction between the parties;
- (2) Supported by adequate consideration;
- (3) Reasonably necessary for the protection of legitimate interests of the employer; and
- (4) Reasonably limited in duration and geographic scope.

Prudent employers understand that most courts scrutinize non-competes to determine whether:

- (1) The employer has a legitimate interest in being protected from the competition of the employee;
- (2) The agreement is reasonable in light of all the circumstances;



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(3) The agreement is reasonably limited in time, scope, and geography and;
(4) Enforcement of the agreement will prove harmful or unduly burdensome to the public.

Additionally, these employers consider:

- (1) The employee's ability and intent to compete;
- (2) The employee's relationships and contacts with those who have expertise in the business; and
- (3) The employee's relationships and contacts with customers.

If a non-compete has unreasonable provisions, courts will apply the "blue pencil" rule. Under this approach, courts will strike, modify or rewrite overbroad or vague provisions from the agreement and enforce the reasonable terms. Courts may limit, modify or rewrite a non-compete in duration, geographical area, or scope of activity.

Non-competes are most often governed by principals of contract law and are normally part of an employment agreement. Consequently, to insure enforceability, the employer and employee should provide adequate consideration. New Jersey and Pennsylvania courts hold that the signing of a non-compete at the inception of employment is sufficient consideration. After the employment relationship has begun, and the employer requires the employee to sign a non-compete, the necessity of consideration becomes more important. New Jersey has enforced non-competes entered into after employment has commenced, holding that continued employment is adequate consideration. Converse-

ly, Pennsylvania courts have held that the mere continuation of employment may not be sufficient consideration to support a non-compete entered into after the employment relationship has begun. However, Pennsylvania courts hold that a change (promotion or change in compensation or other adequate consideration) in the employee's position in exchange for signing of the non-compete is sufficient.

A non-compete generally is part of an employment contract. Therefore, assuming the employee has breached a valid agreement between the employer and employee and the agreement contains a non-compete clause with an attorney's fee provision, the attorney's fee provision should be enforced.

In today's business climate, employers must look for ways to protect business from the competition. A properly executed non-compete is an integral document to protect the business interests and the assets of the company. Those employers seeking protection from the competition would be wise to insure that all non-competes they execute are supported by adequate consideration are specifically tailored to each employee and protect a legitimate business interest of the company.

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