

Enforceability of Employment Based Non-Competition Agreements

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Is my non-competition agreement enforceable? It is a question that is often asked and can result in a variety of answers, from "it is not worth the paper it is printed on" to "it is absolutely enforceable." The reality is that non-competition agreements between an employer and employee can cover a range of subjects and their enforceability will depend on a variety of factors, including the subjects covered by the agreement.

Noncompetition agreements generally impose one or more restrictions on an employee's activities following termination of employment. Common non-competition clauses (also referred to as restrictive covenants) are those that prohibit a former employee from competing with the employer's business, from soliciting customers or potential customers of the employer's business, and/or from using certain information of the employer. The non-competition clauses must be narrowly tailored to protect a legitimate interest of the employer. If they are not so tailored, the employer runs a substantial risk of a court declaring the covenants invalid.

The seminal case in the enforceability of non-competition covenants in New York is BDO Seidman v. Hirshberg¹, which was decided in 1999. In BDO Seidman, the New York State Court of Appeals declared that a non-competition agreement is enforceable if the restraint: (1) is necessary to protect the legitimate interests of the employer; (2) is reasonable in time and area; (3) does not impose undue hardship on the employee; and (4) is not injurious to the public.² "A violation of any prong renders the covenant invalid."³

¹ BDO Seidman v. Hirschberg, 93 N.Y.2d 382 (1999).

² Id. at 389.

³ Id. at 389.

I. Protection of the Employer's Legitimate Interests

An anti-competitive restraint generally only protects a legitimate interest of the employer if the employee provides unique or extraordinary services, the restraint is necessary to protect the employer's goodwill with its clients or customers, or the restraint is necessary to protect the employer's trade secrets or confidential information.⁴

1. Unique or Extraordinary Services.

The traditional standard for demonstrating that an employee provides unique or extraordinary services has been somewhat difficult to satisfy and is most commonly met when the employee is engaged in one of the professions. The highest court in New York State has specifically recognized that with respect to agreements not to compete between professionals, courts "have given greater weight to the interests of the employer in restricting competition within a confined geographic area."⁵

2. Customer Goodwill.

If the employee does not provide unique or extraordinary services, then protection of the employer's goodwill is often presented as a basis for the enforcement of a restrictive covenant. Protection of customer goodwill generally means protecting customer relationships which pertain peculiarly to the employer and were developed through the substantial investment of the employer, and which the employee acquired in the course of his or her employment.⁶ The protection of customer goodwill generally will not support a covenant that prohibits all competition by the former employee with the employer's business. Protection of customer goodwill generally will only justify a narrowly tailored clause that prohibits the former employee from soliciting customers with whom the employee developed a relationship in the course of the employee's

⁴ Scott, Stackrow & Co., C.P.A.s, P.C. v. Skavina, 9 A.D.3d 805, 806 (3d Dep't 2004).

⁵ BDO Seidman, 93 N.Y.2d at 389.

⁶ Id. at 391.

employment. A customer non-solicitation clause therefore may be rejected as overly broad if it bars the former employee from soliciting or providing services to clients with whom the employee never acquired a relationship through his or her employment or if the covenant extends to personal clients recruited through the employee's independent efforts.⁷ A covenant that seeks to prevent an employee from soliciting or performing work for all of the employer's customers therefore may be overbroad if the employee did not develop relationships with all of the employer's customers during the course of his or her employment.⁸

3. Protection of Trade Secrets.

A third legitimate basis for a non-competition clause is the protection of trade secrets or confidential information. The information must consist of genuine trade secrets or confidential information and the restraint must be reasonably limited to the protection of such information. In many cases, the employer will contend that information regarding the employer's customers, including customer lists, constitutes protected trade secrets. Such information must truly be a trade secret. A customer list can constitute a trade secret if the information on the list is not generally known in the trade and is discoverable only through extraordinary efforts.⁹ Customer lists are not confidential where the customers are readily ascertainable from sources outside the former employee's business.¹⁰ Similarly, an employee's recollection of information pertaining to specific needs and business habits of particular customers is not confidential.¹¹ Prices a customer paid for a product or service are also generally not confidential information.¹² In the absence of

⁷ Scott, Stackrow & Co., C.P.A.s, P.C., 9 A.D.3d at 806; see also BDO Seidman, 93 N.Y.2d at 393.

⁸ Scott, Stackrow & Co., C.P.A.s, P.C., 9 A.D.3d at 807.

⁹ Battenkill Veterinary Equine v. Cangelosi, 1 A.D.3d 856 (3d Dep't 2003).

¹⁰ Walter Karl, Inc. v. Wood, 137 A.D.2d 22, 27 (2d Dep't 1988).

¹¹ Walter Karl, Inc., 137 A.D.2d at 27; Natural Organics, Inc. v. Kirkendall, 52 A.D.2d 488, 489 (2d Dep't 2008).

¹² Marietta Corp. v. Fairhurst, 301 A.D.2d 734, 738-39 (3d Dep't 2003) (holding that pricing data and market strategies do not constitute trade secrets).

evidence that an employee physically took, copied, or intentionally memorized customer information, the protection of customer identities and information that are readily available from public sources will generally not meet the standard of protecting a legitimate interest of the employer for purposes of enforcing a restrictive covenant.

II. Scope of Limitation.

Even if the restriction protects a legitimate interest of the employer, the restriction must still be reasonable in time and geographic scope. A reasonable geographic scope is a fact based analysis and depends on the nature of the employer's business. Prohibiting competition within only a 10 mile radius of the employer's office may be reasonable to protect a walk-in based business while prohibiting competition worldwide may be necessary to protect a business with a global customer base. In almost all cases, there must be a time limit on the restrictions.

Generally, the broader the non-competition restriction, the shorter the period it will be enforced. For example, it may only be reasonable to prohibit a former employee from competing with the employer's business for six (6) months or a year while it may be reasonable to prohibit solicitation for a longer period of time.

III. Undue hardship on the employee/Injurious to the public

The restraint must not impose undue hardship on the employee or be injurious to the public. Determining whether the restriction places an undue hardship on the employee requires consideration of whether the restriction makes it overly difficult for the employee to earn a livelihood. A restriction that prohibits an individual from completely practicing his or her chosen trade or profession in a large geographic area for an extended length of time will likely constitute an undue hardship. In contrast, a covenant that only covers a limited geographic area, that only prohibits a particular aspect of the employee's trade or profession, or that limits the employees'

ability to do business with only certain customers in an industry is less likely to cause undue hardship.

The restraint generally will not be considered injurious to the public if the services provided by the employee are still available to the public from other sources. For example, if a specialist physician is prohibited from practicing in a certain region, a court may be interested in whether there are other specialists servicing the region. If not, the restraint may be injurious to the public.

IV. Partial Enforcement.

Courts will sometimes partially enforce a restrictive covenant that is overbroad as written in the parties' contract. Courts, however, are often reluctant to engage in partial enforcement under the theory that if an employer knows it runs the risk of having an overly broad clause struck down completely, it will have incentive to include only narrowly tailored, legally enforceable clauses in its employment agreements. Courts therefore will analyze certain criteria in determining whether to partially enforce an otherwise overbroad restrictive covenant.

An agreement may be partially enforced if an employer demonstrates an absence of overreaching, coercive use of dominant bargaining power, or other anticompetitive misconduct, and a good faith attempt to protect a legitimate business interest, consistent with reasonable standards of fair dealing.¹³ In contrast, clauses that were clearly overbroad under the current state of the law when written are less likely to be partially enforced. Partial enforcement also is not favored when the covenant is imposed in connection with the hiring or continued employment of the employee, as opposed to being imposed in connection with a promotion to a position of responsibility and trust.¹⁴

¹³ BDO Seidman, 93 N.Y.2d at 394.

¹⁴ See Scott, Stackrow & Co., C.P.A.s, P.C., 9 A.D.3d at 807-808.

Determining whether a particular restrictive covenant is enforceable therefore requires a thorough analysis of the particular business or profession involved, the employee's position, the employee's relationship with the employer's business, and the applicable law.

For more information on this topic or if you have a need for legal services in this area, please contact J. Michael Wood at (585) 295-4009 or by email at mwood@cdog.com.

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