ENFORCEMENT OF COVENANTS NOT TO COMPETE

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Employment contracts may contain clauses that forbid the employee from competition with the employer during and after leaving employment. Agreements not to compete are only enforceable if reasonable. Most states have statutes that set out the following requirements to make a covenant not to compete enforceable:

- The covenant must be ancillary to an otherwise enforceable agreement but if the covenant not to compete is executed on a date other than the date on which the underlying agreement is executed, such covenant must be supported by independent valuable consideration; and

- The covenant must contain reasonable limitations as to the time, geographic area, and scope of activity to be restrained that do not impose a greater restraint than is necessary to protect the goodwill or other business interest of the employer.

In most states, a covenant not to compete executed at the beginning or during an at-will employment agreement is unenforceable because it is not ancillary to an otherwise enforceable agreement.

The level of "independent valuable consideration" required to support a covenant not to compete, executed on a date other than the date on which the underlying agreement is executed, is an open question. Some courts have specifically stated that "special training or knowledge acquired by an employee during employment may constitute independent valuable consideration." Often, the courts have not defined "special training or knowledge" nor have they further defined what else, other than special training or knowledge, can constitute sufficient consideration in employment contracts to render a covenant not to compete with an employee forcible. In most states, continuation of an at-will employment agreement is insufficient consideration to support a covenant not to compete.

In order to be enforceable, any covenant restricting employment must be reasonable. It must have reasonable limitations as to time, area and activity and propose no greater restraint or restriction than absolutely necessary to protect the employer's business interests. Where unreasonable, courts typically reform and do not abrogate the restrictive covenant.

In most states, the following apply:

- A covenant not to compete entered into on day one or mid-term in an employment at-will relationship is unenforceable unless supported by "independent valuable consideration."

- What constitutes "independent valuable consideration" is uncertain. It includes special training and knowledge (subject to adequate proof) and may include other types of considerations such as monetary gain and promotions or raises.

- A covenant not to compete entered into by an employee who performs his work in a particular state will normally be construed under the law of that state.

In order to enter into an enforceable covenant not to compete with an employee, an employer can try one of the following: (i) offer an employment contract for definite term with a just cause termination provision (thus circumventing the employment at-will problem); or (ii) provide "independent valuable consideration" to the employee and recite the same in the covenant not to compete agreement.

The employer should also consider including several additional provisions to make the document more reasonable on its face. For example, the employer should consider (i) identifying the employer's interests to be protected; (ii) including an acknowledgment by the employee that the employer will suffer irreparable harm, requiring injunctive relief, if the agreement is violated; and (iii) providing the employee with the option of obtaining the employer's acknowledgment that the employee's new employer is not a competitor within the meaning of the agreement.

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