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INSIGHTS

Mountains To Monuments: Changing Landscape Around Non-Compete Agreements Enforceability

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Highlights

States continue to narrow the enforceability of non-compete agreements through various requirements, such as minimum salary thresholds and notice requirements

Other legislation has limited the length of enforceable restrictions – from two years to 12 months – with overbroad agreements becoming void

Employers must ensure they comply with these requirements, as states are also increasing penalties for overbroad agreements to include fines and imprisonment

Non-compete agreements can be used to protect employers that spend the time and resources to train employees, share unique business insights with them, or introduce them to their customers and suppliers. But many times courts find that employers exploit restrictive covenants when seeking to restrain trade of employees without legitimate business interests – i.e. a sandwich shop attempting to prevent minimum wage employees from working at other sandwich shops.

The response throughout United States has rapidly changed the

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non-compete landscape, with differences from state to state. State legislation and litigation has focused on the minimum required criteria to find a non-compete agreement enforceable, which can include, among other things:

1. minimum employee wage thresholds
2. notice requirements
3. applicable law and venue requirements
4. penalties for violating the law

For example, Colorado's law, which was revised in June 2022, now significantly limits an employer's ability to enforce non-competes executed after Aug. 10, 2022, its effective date. The statute limits the permissible reasons to enforce a non-compete. For agreements before Aug. 10, Colorado's statutorily permitted reasons included protecting trade secrets and the employee being either an executive or management personnel (or their professional staff). For agreements after Aug. 10, Colorado limited the specified reasons to protecting trade secret disclosure by "highly compensated employees" (HCE) (currently, those earning at least $101,250) and non-solicitation of customers for employees earning over 60 percent of the HCE salary threshold. The HCE salary threshold must be met when the agreement is signed, as well as when it is enforced.

Colorado is not alone in using a salary threshold. It has joined several states that have determined that there is no legitimate business interest presented by anyone who earns less than a certain wage. Each state determines this minimum required wage differently and there is a wide discrepancy in the determined wage.

For example, states can focus on the hourly rate, from as little as $15 an hour required in Maryland, or an annual salary, such as over $100,000 a year in Oregon and Washington. Others, like Nevada and Massachusetts, prohibit non-competes if the employee is paid hourly. Still others require employees to receive a salary of a certain percentage over the federal poverty level, such as Rhode Island (250 percent) and Maine (400 percent). Some states even have built-in increases for the minimum wage, such as Illinois.

In July 2022, Washington, D.C., joined these states by amending its proposed full ban on non-competes. Under the new D.C. law, non-compete agreements entered into after Oct. 1, 2022, will only be enforceable against employees earning a total compensation that is or is reasonably expected to be more than $150,000 per year.

Employee Notice is Required

Colorado's and Washington, D.C.'s new laws also focus on providing employees with notice of the non-compete, so that the employee can truly consider the consequences of the agreement. Under Colorado's law, employers must provide the employee with a separate, written notice of the non-compete and its terms and employees must sign this notice. Similarly, Washington, D.C.'s law requires that employers provide the non-compete to employees in writing at least 14 days prior to the start of employment or execution of the agreement, as well as notice about the act itself.

Colorado and Washington, D.C., are not alone in requiring notice. Illinois

requires employers to provide prospective employees with the non-compete at least 14 days before their start date and advise the employee to consult a lawyer. In Oregon, employers must provide the agreement at least 14 before the employee's start date and provide notice of the requirements after the employee's employment ends.

California, Colorado, and Washington also mandate the use of their law and venue in all agreements containing covered restrictive covenants. For employees in each of these states, the law of the state where the employee is based applies and the proper venue is that state.

Furthermore, many of these state statutes apply to independent contractors as well.

Some states have also statutorily limited the duration of the post-employment restrictive covenants – such as Oregon (generally a 12-month maximum), Idaho and Washington (rebuttable presumption in both that non-competes longer than 18 months are presumed unreasonable). While Colorado's law does not contain such a statutory limit, generally two years is the court-accepted maximum. That said, if an employer wants to avoid having their restrictive covenants found void and assessed penalties, it should err on the side of a more narrowed restricted period.

Employers would be wise to make sure their policies comply with these new requirements because some of the states have steep repercussions. For example, under Colorado law, an employer who provides an employee with a void non-compete as a term of employment or tries to enforce a void non-compete agreement with a penalty of $5,000 per worker harmed (as well as actual damages, injunctive relief, reasonable costs and attorneys' fees).

Similarly, Maine imposes a penalty of at least $5,000, and Washington state imposes a statutory penalty of $5,000 (or actual damages, if greater), along with attorney fees, expenses, and costs. Moreover, Colorado permits criminal liability against a person who knowingly uses an unenforceable, overbroad non-compete agreement as a means of intimidation, forcing the employee to refrain from earning a living can be liable for a class 2 misdemeanor (punishable by 120 days in jail and/or a fine of up to $750).

Each state is taking a unique approach towards assessing and enforcing non-compete agreements. Employers would be wise to continuously review the non-compete laws of any state where an employee resides. These laws continue to develop and, as necessary, employers may need to revise and update their agreements to stay enforceable.

For more information, please contact the Barnes & Thornburg attorney with whom you work with or Terese Connolly at 312-214-4811 or tconnolly@btlaw.com or Christopher Rubey at 574-237-1106 or crubey@btlaw.com.

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