

# Protecting Your Assets Navigating the New Reality: Restricting Covenants Under Assault

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# Your Company's Most Valuable Assets

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- ◆ Employee, vendor & supplier relationships.
- ◆ Customers and customer information (lists, history, pricing, preferences).
- ◆ Product information/formulas.
- ◆ Business processes, procedures and know-how.
- ◆ Financial information.
- ◆ Pricing methods + profit margins.
- ◆ Marketing plans.
- ◆ Intellectual property.

# How Do You Protect Your Assets?

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## Restrictive Covenant Agreements

- ◆ Non-Competition – Key employees.
- ◆ Non-Solicitation – Key employees.
- ◆ Non-Disclosure – All employees?

# Challenges To Enforcing Agreements

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- ◆ Governed by state law.
  - Increasingly restrictive legislation.
- ◆ Federal legislation & regulation.
- ◆ Disfavored by courts.
- ◆ Strictly construed against employer.

# Candidates For Restrictive Agreements

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- ◆ Executives.
- ◆ Key management.
- ◆ Sales/marketing.
- ◆ R & D.
- ◆ Employees with specialized training.
- ◆ Everyone?
  - At least Non-Disclosure?



# Elements of Enforceable Non-Compete Agreement (SC)

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- ◆ Part of lawful contract;
- ◆ Supported by consideration;
- ◆ Necessary to protect legitimate interest(s);
- ◆ Reasonable as to time, territory, and scope of activity restrained;
- ◆ Not unduly harsh and oppressive in curtailing legitimate efforts of employee to earn a living; and
- ◆ Not against public policy.

*Baugh v. Columbia Heart Clinic, P.A.*, 402 S.C. 1, 738 S.E.2d 480 (CT. APP. 2013); *Rental Uniform Service of Florence, Inc. v. Dudley*, 278 S.C. 674, 301 S.E.2d 142 (1983).

# Temporal Restriction: How Long Is Too Long?

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- ◆ Length of time.
  - 2-3 years generally acceptable in SC.
  - *Oxman v. Proffit*, 241 S.C. 28 (1962); *Rental Uniform Service of Florence v. Dudley*, 278 S.C. 674 (1983).
- ◆ Factors to consider.
  - Nature of protectable interest.
  - Position of employee.
  - Educational level of employee.
  - Years worked in your industry.
- ◆ Sale of business – 5 to 7 years acceptable.

# Geographic Restriction: What Is Reasonable?

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- ◆ Factors to consider:
  - Area in which employer operates.
  - Area assigned to employee.
  - Area employee actually worked and established contacts.
  - Nature of business.
  - Nature of employee's duties.
- ◆ Limit to area necessary to protect interests.
  - Do not overreach.
  - Include step-down provision.
- ◆ Overbroad geographic restriction is likely fatal.
- ◆ Commonly litigated issue.

# Geographic Territory

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- ◆ Statewide restraint unenforceable where employee's solicitations limited to 2 counties.

*Oxman v. Sherman*, 239 S.C. 218 (1961)

- ◆ 15-mile restriction unenforceable where “overwhelming majority” of clients lived much closer than 15 miles.

*Stringer v. Herron*, 424 S.E.2d 547 (1992)

# Customer Non-solicitation

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- ◆ Valid substitute for geographic restriction.
- ◆ Favored by courts.
  - Protectable interest – customer relationship.
  - Less restrictive on employee – not required to move.
- ◆ Must clearly define customers.
  - Should be active/very recent customer.
  - Employee had contact or knowledge of customer info.
  - “Prospective” customers questionable.
- ◆ May be used in addition to geographic restriction.

# Scope of Activity

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- ◆ Rejecting a 3-year limitation barring an esthetician, a former employee of a facial spa, because covenant prevented employee from being connected with any business in any way that gave facials or sold cosmetics
- ◆ e.g., could not work in any sections of department store that sold cosmetics

*Faces Boutique, Ltd. v. Gibbs*, 455 S.E.2d 707 (1995)

# Valuable Consideration

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## ◆ Offer of employment

- Inform applicants of requirement to sign Agreement
  - interview/offer letter.
- Condition of employment.
- Execute on or before start date.
- At-will employment sufficient.

## ◆ Continued at-will employment not sufficient in SC

- Agreements signed after employment starts (due to oversight) likely not enforceable without consideration.

# Valuable Consideration?

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## ◆ Change in terms or conditions

- Promotion.
- Pay increase.
- Company car or other benefits.
- Lump sum payment.
- Promise of severance pay.
- Incentive Compensation Plan.
- Stock options.

# When Should Restrictive Agreements be Signed?

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- ◆ Prior to start date (as a condition of employment).
- ◆ Prior to promotion.
- ◆ As condition of pay increase or lump sum payment.
- ◆ As condition of incentive compensation plan.
- ◆ In Severance Agreement (your last chance!).

# General Drafting Considerations

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- ◆ Do not use “fill-in-the-blank” agreements.
- ◆ Must conform to applicable state laws.
- ◆ Tailor to position.
- ◆ Periodically review and update.
- ◆ Provide consideration if modifying.
- ◆ Do not overreach.
- ◆ South Carolina courts will not “blue pencil.”  
*Poynter Investments, Inc. v. Century Builders of Piedmont, Inc.*, 387 S.C. 583, 694 S.E.2d 15 (2010).



# Contract Provisions

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- ◆ Non-compete & Non-solicit.
- ◆ Confidential Information/Non-Disclosure.
- ◆ No-Raid provision – protects your employees.
- ◆ Return of all company property.
- ◆ Severability.
- ◆ Step-down provision.
- ◆ Choice of law.
- ◆ Forum selection.
- ◆ Tolling.

# Contract Provisions

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- ◆ Notice to Prospective Employers.
- ◆ Other positions and related employers.
  - Agreement should expressly apply to other positions.
- ◆ Garden Leave.

# Contract Provisions

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## ◆ Remedies:

- Forfeiture.
- Irreparable harm.
- Liquidated damages.
- Injunctive relief.
- Costs and attorneys' fees.

## ◆ Defendant Trade Secrets Act and Notice.

# Defend Trade Secrets Act Notice

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- ◆ The DTSA requires that employers provide notice of its immunity and retaliation provisions to employees, consultants, and independent contractors in any agreement entered into after May 11, 2016, that governs the use of trade secrets or other confidential information, including:
  - Employment agreements
  - Independent contractor agreements
  - Consulting agreements
  - Separation and release of claims agreements
  - Severance agreements
  - Non-compete and non-solicitation agreements
  - Confidentiality and proprietary rights agreements
  - Similar agreements included in employee handbooks

# DTSA Notice Language for Agreements

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- ◆ Pursuant to the Defend Trade Secrets Act of 2016, I understand that:
  - An individual may not be held criminally or civilly liable under any federal or state trade secret law for the disclosure of a trade secret that: (a) is made (i) in confidence to a federal, state, or local government official, either directly or indirectly, or to an attorney; and (ii) solely for the purpose of reporting or investigating a suspected violation of law; or (b) is made in a complaint or other document that is filed under seal in a lawsuit or other proceeding
  - Further, an individual who files a lawsuit for retaliation by an employer for reporting a suspected violation of law may disclose the employer's trade secrets to the attorney and use the trade secret information in the court proceeding if the individual: (a) files any document containing the trade secret under seal; and (b) does not disclose the trade secret, except pursuant to court order.

# What Is A Trade Secret?

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## **Information** (in any form)

1. That derives independent economic value;
2. From not being generally known;
3. Or readily ascertainable;
4. By proper means;
5. From persons who can obtain economic value from it; and
6. **Is the subject of reasonable efforts to maintain its secrecy!**

EXAMPLES: formula, pattern, compilation, program, device, method, technique, product, system, process, design, prototype, procedure, code.

# Protecting Your Confidential Information

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- ◆ Not all confidential information is a trade secret, but may still need protection.
- ◆ Require employees to sign confidentiality agreement.
- ◆ Severance agreements should include protective language if no prior agreement.

# Protecting Your Confidential Information

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- ◆ Implement policies addressing access to, and use of, confidential information, company computers, email, etc.
- ◆ Implement policies limiting third-party access.
- ◆ Audit personnel files to ensure that you have fully executed originals of key documents.

# Protecting Your Confidential Information

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- ◆ Mark important documents “CONFIDENTIAL.”
- ◆ Limit access to those with a need to know.



# Protecting Your Confidential Information

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- ◆ Lock file cabinets/offices that contain confidential information.
- ◆ Password protect electronically stored confidential information.
- ◆ Sign-in and badge requirements for visitors.

# Protect Yourself from Claims by Others: New Hire Protocols

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- ◆ **Ask New Hires for All Restrictive Covenant Agreements**
  - stand-alone restrictive covenant agreements;
  - employment agreements;
  - offer letters;
  - stock option agreements;
  - incentive compensation plan participation documents;
  - sale of business agreements.
- ◆ **If you require employees to sign agreements, communicate that you intend to honor the lawful provisions of employee agreements with prior employers.**

# New Hire Protocols

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- ◆ **If New Hire says he signed no agreements, secure written confirmation.**
- ◆ **Determine Circumstances Under Which New Hire Executed Agreements.**
- ◆ **Determine Reasons Why New Hire Is Looking To Leave Employment.**

# New Hire Protocols

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## ◆ **New Hires Should Come Empty-Handed.**

New hires should be informed explicitly:

- Do not download, copy, or email confidential information.
- Return any confidential information stored on personal device or at home.
- When leaving, they should take only purely personal items, and not company records of any kind.
- Have personal information stored on their former employer's electronic devices extracted by former employer.
- Be honest when asked about their new employment.

# New Hire Protocols

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- ◆ **Offer Letters Should Reiterate Key Points.**
- ◆ **Do not bring or disclose confidential information.**
- ◆ **Require compliance with enforceable restrictive covenant agreements.**
- ◆ **Consider including the following in agreement or countersigned offer letter with New Hires:**
  - Representation that New Hire not signed any agreements (other than specific agreements previously provided).
  - Complied with other requirements of being a good leaver, including not taking any files or information, etc.
  - Acknowledgement that neither you nor your counsel have provided legal advice to the New Hire and that it is recommended that New Hire seek his own counsel.
  - In the event of litigation, what would be the arrangements between New Hire and you, including indemnification and whether employment would continue.

# New Hire Protocols

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- ◆ **Manage New Hires' conduct following employment.**
  - No dissemination of confidential information.
  - No solicitation if banned by agreement.
  - Keep New Hire removed from prohibited activity.
- ◆ **How New Hire handles calls from clients and former employees.**
  - Consider not responding at all.
  - Redirect caller to appropriate contact at former employer.
  - If caller insists on contact at your company, New Hire *may be able* to provide contact *if he already provided contact at former employer.*
  - New Hire should explain he is subject to restriction prohibiting contact/solicitation.

# New Hire Protocols

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- ◆ **New Hire Should Not Contact Or Advise Customers or Business Partners of Move.**
  - LinkedIn updates, Facebook posts, etc. may be problematic.
  - Do not turn announcement or a new job notification into a solicitation.
  - Tombstone ads and press releases should be generic and not targeted to specific audiences.

# Protecting Business Interests Before Separation: Exit Protocols

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- ◆ Prepare checklist and follow it.
- ◆ Find out from the employee:
  - When leaving
  - Why leaving
  - Where going
  - New position duties
- ◆ Delete terminating employee's access to computer and confidential information.
- ◆ Discuss confidential information obligations.
- ◆ Discuss the employee's contractual obligations.

# Exit Protocols

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- ◆ Give employee copies of applicable agreements.
- ◆ Make sure all company property is returned.
- ◆ Communicate with key clients.

# Exit Protocols

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- ◆ Following termination:
  - Surveillance (if warranted).
  - Interview co-workers.
  - Review recent assignments.
  - Competitive intelligence.
    - Pretext calls
    - Internet monitoring
    - Industry sources

# Trends in States: Limitations on Restrictive Covenants

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- ◆ **Ban Non-Competes for Lower-Income Workers** (Maine, Maryland, New Hampshire, Rhode Island, Washington);
- ◆ **Ban Non-Competes for FLSA Non-Exempt Employees** (Massachusetts, Rhode Island);
- ◆ **Notice Requirements Regarding Non-Competes** (Maine, Massachusetts, Washington);

# Trends in States: Limitations on Restrictive Covenants

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- ◆ **Prohibit Enforcement of Non-Competes against Workers Discharged Without Cause (Massachusetts);**
- ◆ **Require Employers to Continue Paying Laid Off Workers During Restricted Period (Washington).**

# Pending State Legislation

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- ◆ District of Columbia
- ◆ Hawaii
- ◆ Indiana
- ◆ Iowa
- ◆ Kentucky
- ◆ Massachusetts
- ◆ Michigan
- ◆ Missouri
- ◆ New Hampshire
- New Jersey
- New York
- Oregon
- Rhode Island
- Virginia

# Pending Federal Legislation

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- ◆ **[2019 US S 2614](#) – October 16, 2019**

Bans all non-competes except in the sale of a business or dissolution of a partnership

Status: In First Committee; Hearing on November 14, 2019

- ◆ **[2019 US S 124](#) – January 15, 2019**

Bans non-competes for all employees other than FLSA exempt employees under Section 13(a)(1)

Status: In First Committee; Hearing on November 14, 2019

- ◆ **[2019 US H 1163](#) – January 15, 2019**

Bans non-competes for employees at the Veterans Health Administration

Status: In First Committee; Hearing on September 11, 2019

