

ENFORCING RESTRICTIVE COVENANTS - WHAT EMPLOYERS NEED TO KNOW

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OVERVIEW

- A. What is a restrictive covenant?

- B. What are the different types of restrictive covenants?
 1. Confidentiality/nondisclosure
 2. Nonsolicitation of employees
 3. Nonsolicitation of customers
 4. Noncompetition

- C. Under what circumstances is it sensible to make use of restrictive covenants?

VALIDITY AND ENFORCEABILITY – PROVING THE ESSENTIAL ELEMENTS

A. What are the legal standards for enforcement of restrictive covenants?

1. Connecticut enforces covenants not to solicit/compete if they are “reasonable under the circumstances.” Connecticut applies a five-part test:

- length of time
- geographic area
- presence of protected interests of the employer
- extent of the restriction on employee’s ability to pursue his/her occupation
- extent of interference with the public’s interest

2. Other states have similar standards.

VALIDITY AND ENFORCEABILITY – PROVING THE ESSENTIAL ELEMENTS

3. California law bars enforcement of restrictive covenants except in connection with the sale of a business, and California courts generally will not enforce restrictive covenants made elsewhere, even if the contract contains a choice of law provision specifying the law of a state where restrictive covenants are enforceable.

VALIDITY AND ENFORCEABILITY – PROVING THE ESSENTIAL ELEMENTS (continued)

B. Presence of protected interests is fundamental.

1. Customer lists/customer relationships
2. Trade secrets
3. Confidential information
4. Other types of protected interests

VALIDITY AND ENFORCEABILITY – PROVING THE ESSENTIAL ELEMENTS (continued)

C. Examples of the other factors

1. Temporal and geographic reasonableness are intertwined, and may depend on the nature of the business involved.
2. Interference with an employee's ability to pursue occupation may be mitigated by payment.

D. defenses to enforcement of valid covenant

1. Employer's prior breach
2. Breach of implied covenant of good faith and fair dealing

CONSIDERATION NECESSARY TO SUPPORT RESTRICTIVE COVENANTS?

- A. Circumstances under which restrictive covenants are made
 - 1. At inception of employment
 - 2. During employment

- B. Where a restrictive covenant is entered into at the start of employment, courts generally hold that it is supported by adequate consideration; namely the employment.

- C. Where a restrictive covenant is entered into during employment, courts have held that there must be some consideration separate from and in addition to continued employment to support the restrictive covenant; but the more recent trend of decisions recognizes that continued employment is adequate consideration.
 - 1. Rationale for all of the seemingly different positions.
 - 2. Can the different positions be reconciled?

BLUE PENCIL ISSUES/SEVERABILITY DOCTRINE

- A. What is the blue pencil doctrine?
- B. Does the blue pencil doctrine apply in Connecticut?
- C. Where does the blue pencil rule apply?
- D. What is the Severability Doctrine? Is it a form of “blue penciling?”

PRELIMINARY INJUNCTIVE RELIEF

- A. Restrictive covenant cases are generally won or lost at the preliminary injunction stage.
- B. What must the employer prove to obtain a preliminary injunction?
 1. State court standard: no adequate remedy at law; irreparable injury absent injunction; likelihood of success on merits; balance of equities
 2. Federal court standard: irreparable harm and either (a) likelihood of success or (b) fair ground for litigation and balance of equities
 3. Where federal jurisdiction is an option: choice of forum likely to depend on more practical considerations – availability of quick hearing, what judge is likely to get the case, etc.

PRELIMINARY INJUNCTIVE RELIEF (continued)

C. How does one prove/attack “irreparable harm”?

1. Employee had access to, developed, and/or used confidential information and/or trade secrets.
2. If the information at issue is a customer list, show that the employee did not bring the customer information with her when she joined the company, that the company assisted her in developing relationships, that the information (customer identities, contact people, needs, plans, financial capacity, etc.) is not readily available to the public, and that the company guards the information against public disclosure.
3. Employee has gone to work for (or says he is going to work for) a competitor, in a capacity where it is likely he will use and/or disclose former employer’s confidential information.
4. Employee has actually used/disclosed former employer’s confidential information. Employee has solicited former employer’s customers. Employee has made sales on behalf of competitor to former employer’s customers.

PRELIMINARY INJUNCTIVE RELIEF (continued)

- D. Irreparable harm is the key to success. The “presumption” of irreparable harm in restrictive covenant cases will not always be applied.
1. Although some courts have held that irreparable harm will be presumed if there is a proven violation, other courts have refused to apply the presumption.
 2. Judge Droney, of the U.S. District Court for the District of Connecticut, recently observed that the presumption of harm is more appropriate when:
 - a. the former employer establishes that the employee possesses and is likely to disclose trade secrets or highly confidential information;
 - b. the companies involved “are highly competitive, are direct rivals in the same markets, and rely on long-term or near-permanent relationships with customers with whom the employee would have had no contact, but for his employment;”
 - c. the action is brought very promptly and insufficient time has passed to demonstrate actual harm.

PRELIMINARY INJUNCTIVE RELIEF (continued)

3. The Second Circuit has noted that where a departing employee seeks to *use* a trade secret, not to disclose it, and has the same incentive as the former employer to maintain secrecy, money damages may be an adequate remedy.
4. Similarly, a liquidated damages provision in the underlying agreement may undermine the claim of irreparable harm.

PRACTICAL ADVICE FOR EMPLOYERS

- A. Don't rely on the inevitable disclosure doctrine.
- B. On the other hand, don't overreach when it comes to restrictive covenants.
- C. Only include the protection you really need.
- D. Enforce your covenants consistently.
- E. Don't dilly-dally. When you can prove a violation, bring suit quickly.

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