Are Your Employment Agreements Up to Date? Top 5 Considerations for Drafting 50-State Compliant Restrictive Covenants

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Does your company have non-competes, non-solicitation agreements, or other restrictive covenants in place with employees? If so, you'll want to review these agreements in light of recent developments. Notably, we are seeing an increased animosity toward restrictive covenants in a variety of ways. At the same time, more employers are looking to put new agreements in place to lock in talent during the Great Resignation. We've handled a number of 50-state agreement projects for clients looking to upgrade and update these important documents — and we wanted to take a few minutes to share some of our thoughts on drafting considerations. What are the top five issues you should consider as you draft and revise your agreements?

1. Restrictive covenants are under review as possible antitrust violations. In late 2016, the U.S. Department of Justice Antitrust Division and the Federal Trade Commission issued a paper titled Antitrust Guidance for Human Resource Professionals. Since then, the federal agencies have taken enforcement actions against employers who agree with competitors not to solicit each other's workers. There have been state enforcement actions also, particularly in the area of franchisor/franchisee agreements. This makes it essential for in-house legal counsel and HR professionals to understand the antitrust concerns in play, especially since the risks are quite high and include potential criminal sanctions.

Drafting consideration: Make sure the context of the intended agreement is not something the government might view as an antitrust violation.

2. Legitimate business purpose for a restriction varies within your workforce. Your highest-level executives deserve and should expect stronger restrictions, both during employment and post-employment, as compared to entry-level hourly workers. We have seen increasing judicial and legislative animosity toward restrictive covenants. This is directed at income thresholds, material contacts with customers and employees, and geographic area of employee activity. In this environment, we no longer suggest having all or even nearly all employees sign the same document. We typically suggest a tiered approach with certain classifications or groupings of employees being offered similar agreements.

Drafting consideration: Perhaps three tiers of restrictions will work for your organization.

- Tier One employees sign an agreement with confidentiality, return-of-property, and assignment of intellectual property provisions.
- Tier Two employees sign an agreement with all the Tier One provisions, plus non-solicitation of employees and customers.
- Tier Three employees sign an agreement with all the Tier Two provisions, plus a reasonable general non-compete provision.

That's just one approach that we have found useful for many clients. The key point here is to increase the likelihood of compliance and enforcement success — but also to customize the restrictions in play based on the portion of your workforce at issue.

3. Differentiation between states on key topics. In addition to tiering across employee classifications, you should consider the state-by-state differences that affect a few key topics and create the need to either tailor each provision in an appendix or go with the lowest common denominator. Some of the key topics from a state law perspective are:

- geographic scope;
- temporal scope;
- material contacts;
- choice of law and venue;
- dispute resolution;
- recovery of fees and costs;
- applicability based on income levels;
- additional considerations for new hires or existing employees; and
- advance notice/presentation of the proposed agreement.

Drafting consideration: Because certain states will not reform or otherwise modify an unenforceable covenant — and others will penalize an employer for simply providing an unenforceable covenant — provisions for those states must be compliant at the outset.

4. Administrative burden when rolling out new covenants cautions against wholesale state-specific documents. For multistate employers, the variances among state laws make it challenging to have one uniform template agreement. In the past we generally suggested state-specific templates, meaning that Ohio residents signed the Ohio template, Texas residents signed the Texas template, and so on. That works well when an enforcement action is being litigated, because it avoids disclosure and litigation over variances among templates. Today, though, there are so many substantive state law variances that this strategy gets quite burdensome on the HR department or other teams responsible for the templates. Plus, in today's changing workforce model, many employees operate remotely and employees are generally much more mobile. We no longer have the

same degree of certainty that the Ohio resident who signed the Ohio template will still reside in Ohio when the time comes to enforce the agreement.

Drafting consideration: We are now typically suggesting a primary template document (for each tier of employees) with state-specific appendices containing the state-specific changes to key provisions or alternative provisions organized by state. Of course, some states — such as California, Colorado, and Massachusetts — have such unique requirements that we sometimes suggest a standalone agreement for those states. A "template with appendices" avoids the problem of employees signing the "wrong" template or causing questions about likelihood of enforcement through changed circumstances. Furthermore, in our experience, many former employees will honor their agreement once they are reminded about their obligations. A court may find, however, that if an employer is able to lessen the restriction in some states but not others, the greater restriction is not necessary to protect its business interests. At the pre-suit stage of an enforcement matter, though, we are not as concerned if the document we are looking to enforce has provisions within it that do not apply to the case at hand.

Another approach is to draft the documents to the lowest common denominator for the post-employment restrictive covenants. This approach will create the greatest enforceability and lessens the number of appendices or alternative provisions. Of course, the downside with that approach is a lower level of protection in those states that permit greater restriction.

5. Enforcement is uncertain. Organizations looking to enforce a restrictive covenant should strive to strike closer to perfection than ever before on all of these aspects: presentation to the employee, plain language drafting, wise selection of choice of law and venue, and development of the case before filing. Notably, employees looking to avoid an enforcement action are more likely these days to be the first to file a lawsuit. Moreover, an increasing number of jurisdictions view it as a violation of law to offer a contract with terms deemed illegal in the particular jurisdiction — and the penalties can add up regardless of whether the provision may be modified.

Additionally, you should note that the FTC recently proposed a new rule that, if enacted, would not only ban virtually all non-compete agreements but also require you to actively rescind existing agreements you've already signed. The proposed rule may also impact your other restrictive covenants. You should stay tuned for more information as this major development unfolds.

Drafting consideration: The bottom line in this changing area is that careful development and customization of a series of templates is the key to developing a restrictive covenant approach more likely to be viewed as compliant in all 50 states.

Conclusion

We will continue to monitor the latest developments and provide updates as warranted, so you should ensure you are subscribed to Fisher Phillips' Insight system to gather the most up-to-date information directly to your inbox. If you have questions, please contact the authors of this Insight

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