

EMPLOYERS GET A WIN ON ENFORCEABILITY OF EQUITY-LINKED RESTRICTIVE COVENANTS IN DELAWARE: 3 KEY TAKEAWAYS

Insights
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Employers Get a Win on Enforceability of Equity-Linked Restrictive Covenants in Delaware: 3 Key Takeaways

The Delaware Supreme Court just delivered good news to employers that use equity and incentives to retain key talent. Those awards are often paired with non-compete and non-solicitation restrictions aimed at protecting customer relationships and confidential information. But what happens if an executive breaches the agreement and forfeits the award, or resigns before the benefits vest? Are the restrictive covenants still supported by consideration? A recent decision from the Delaware Supreme Court offers useful clarity for employers when their agreements are governed by Delaware law: Consideration is evaluated when the contract is formed – not later when the employer seeks to enforce it. Here’s what you need to know about the February 3 ruling, including three major takeaways for employers.

What Happened in This Case?

In [*North American Fire Ultimate Holdings v. Doorly*](#), an employer sought to enforce restrictive covenants in an incentive-unit agreement that the departing executive forfeited by setting up a competing business. Here are the relevant facts according to the court’s opinion:

- The employer granted equity interests to a senior executive that were later restructured and made subject to

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time/performance vesting under an incentive-unit grant agreement.

- Under the agreement, the executive agreed to confidentiality, non-solicitation, and non-competition restrictions.
- After the employer discovered that the executive had formed a competing business, it terminated him for cause, triggering an automatic forfeiture of both vested and unvested incentive units.
- The employer then sued to enforce the restrictive covenants.
- The Delaware Court of Chancery dismissed the contract claims. Since the incentive units were treated as the sole consideration for the covenants, the court said, the incentive forfeiture left the contract unenforceable for lack of consideration at the time of enforcement.

The Delaware Supreme Court reversed. It held that consideration is measured at the time of contracting, not at the time of enforcement, and remanded the case for further proceedings.

Significance for Employers

The *Doorly* decision is significant because many equity arrangements include vesting conditions, for-cause forfeiture, and clawback/recoupment mechanics. These features often become central after a contentious separation.

The appellate court rejected the argument that the consideration was “illusory” just because the value of the equity units was contingent on the occurrence of future events. If the Court of Chancery’s approach had taken hold, it would have created a litigation playbook for departing executives. They could argue “no consideration” at enforcement anytime the equity is forfeited or never vests. The Delaware Supreme Court’s ruling significantly undercuts that strategy.

3 Major Takeaways

Employers with Delaware-governed agreements should note the following key takeaways from the ruling:

1. Don't expect forfeiture to "wipe out" consideration. If your restrictive covenants are supported by consideration at signing, later forfeiture should not (by itself) defeat enforceability on a "no consideration" theory under Delaware law.

2. Your drafting still matters, especially how the bargain is described. This dispute arose in part because the agreement language and structure fueled the argument that the incentive units were the "sole consideration" for the restrictions. Even with this favorable decision, employers should carefully draft consideration language and explain the integration between the plan + award agreement + restrictive covenant section.

3. This decision is not a "free pass" on scope and reasonableness. The ruling addresses consideration timing, not whether the non-compete/non-solicitation agreement is reasonable, properly tailored, and supported by legitimate interests. Those remain the core battleground issues in Delaware restrictive covenant litigation.

Conclusion

We will continue to monitor developments in this area, so make sure you are subscribed to [Fisher Phillips' Insight System](#) to get the most up-to-date information. If you have questions about this decision, please contact your Fisher Phillips attorney, the author of this Insight, or any attorney in our [Employee Defection and Trade Secrets Practice Group](#).