

Colorado Joins Majority of Courts in Holding that Continued Employment Suffices As Consideration to Support a Non-Compete

Insights

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As with any contract, to be enforceable, a post-employment restrictive covenant must be supported by consideration. In some states, if a restrictive covenant is signed by an at-will employee after the inception of employment, the covenant must be supported by new and independent consideration (such as a promotion or a raise in salary). In other states, the promise of continued employment—even to an at-will employee—constitutes sufficient consideration. Because the law varies from state to state, employers with nationwide operations must be aware of each state’s law regarding the validity of restrictive covenants signed by employees after the employee has commenced employment.

The Colorado Supreme Court recently fell in line with the clear majority position among those states that have addressed the question, holding that continued employment alone is sufficient consideration. In *Lucht’s Concrete Pumping, Inc. v. Horner*, the Court explained: [w]e hold that an employer that forbears from terminating an existing at-will employee forbears from exercising a legal right, and that therefore such forbearance constitutes adequate consideration for a noncompetition agreement.” (A copy of the court’s opinion is available in pdf format below.)

In *Lucht’s*, the former employer originally hired the employee in 2001. In 2003, the employee signed a non-compete agreement, and he was not offered any pay increase, promotion or any other additional

benefit. In 2004, the employee resigned and joined a competitor. Not long thereafter, the former employer sued to enforce the restrictive covenant, and the trial court found it unenforceable due to a lack of consideration. The Colorado Court of Appeals agreed because, in its view, the continued employment of an at-will employee cannot by itself constitute consideration for a non-compete agreement. The appellate court reasoned that under these circumstances, nothing prevents the employer from discharging the employee after he signs the non-compete, and therefore, the at-will employee receives nothing more than what he was already promised at the inception of at-will employment.

The Colorado Supreme Court disagreed, and stated that it chose to join the majority of jurisdictions “that conclude that an employer’s forbearance of the right to terminate an existing at-will employee constitutes adequate consideration to support a noncompetition agreement.” The Court reasoned that when an employer presents a restrictive covenant to an at-will employee, it is essentially offering to renegotiate the terms of employment, and the employee can choose to stay or choose to go. If the employee chooses to stay, in effect, he accepts the offer of continued employment subject to the terms of the non-compete agreement.

As for the lower court’s concern that an employer could turn around and immediately fire an employee who signs a restrictive covenant, the Colorado Supreme Court noted that such covenants must always be assessed for reasonableness upon the facts of each case. Therefore, “legitimate consideration exists as long as the employer does not act in bad faith by terminating the employee shortly after the employee signs the covenant.”

While Colorado has followed the majority rule, there are some states that see the issue differently. For example, the New Hampshire Supreme Court has implied that mere continuing employment would be insufficient consideration to support a covenant entered into after commencement of employment. In *Merrimack Wood Products v. Near*, 876 A.2d 757, 764-65 (N.H. 2005), the Court declined to modify an overbroad covenant so that it could be enforced more narrowly, concluding that the employer was not entitled to this equitable benefit because it had not “acted in good faith” in connection with the execution of the covenant. The evidence of the employer’s “bad faith” was the fact that the covenant was not discussed with the employee during his job interview, it was not presented to him until six months after he started work, and he was told his continued employment was contingent on his signing the covenant. The Court concluded that this was adequate evidence of “bad faith” to preclude modification of the covenant. Although the Court did not address the issue as one of consideration, and although it is not apparent what the Court would have done with an after-thought covenant that was otherwise reasonable, its conclusion that providing a covenant after commencement of employment amounted to “bad faith” suggests that late-signed covenants may be treated with disfavor in New Hampshire.

The question thus becomes “If additional consideration is required, what type of consideration will suffice?” In practice, the answer to this question may be as multi-faceted as the number of judges sitting on the bench. The enforcement of a restrictive covenant is subject to a court’s equitable

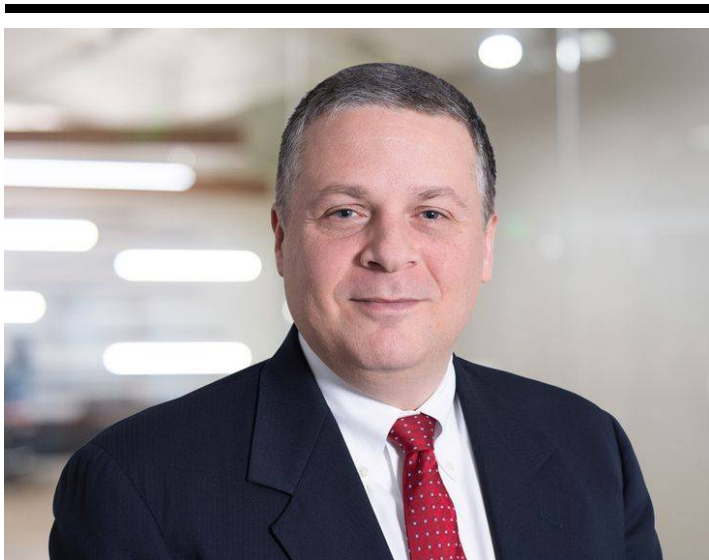
discretion and is often framed in terms of reasonableness. Most judges will try to reach the result that is fair and equitable under the circumstances provided it is consistent with controlling law. If they believe enforcement of a non-compete would be inequitable, they may be more inclined to take issue with the adequacy of consideration. In contrast, if they believe an employee is up to no good, they may find the consideration in question to be sufficient. That being said, employers seeking to strike the correct balance may find the following guideline to be useful: provide the employee with some appreciable, tangible benefit to which he or she was not already entitled. A new promotion accompanied by a raise and additional responsibilities may pass muster more easily than an extra week of vacation time. Employers might also consider stock grants or specialized training. Benefits to which the employee was already arguably entitled (such as an annual raise) may meet with more scrutiny.

In short, employers must be keep in mind the consideration requirements of each state in which they attempt to bind employees to restrictive covenants after the inception of employment. In the event that additional consideration beyond continued employment is required, the employer may increase the odds of enforceability by bestowing an appreciable benefit to which the employee was not already entitled.

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