

An Introduction to Non-Compete Agreements (Part 2 of 2)

[This is the second part of a two-part article. The first installment addressed the basic definition of a non-compete agreement, the fact that such agreements are enforceable in Indiana and Michigan, and why you as an employer or business owner should care about such agreements. This second installment will expand on enforceability issues under Indiana and Michigan law and provide some basic fact patterns where such an agreement might be more or less likely to be enforced by a court.]

In Part 1 of this article, we noted that non-compete agreements are enforceable in Indiana and Michigan, but only to the extent that they are being enforced in appropriate factual circumstances and have been drafted so that their restrictions are as narrow as reasonably necessary to protect the business' legitimate interests.

In Indiana and Michigan, non-compete provisions are considered to be restraints on trade and accordingly courts in both states will consider them to be valid and enforceable only in limited circumstances. As a result, the enforceability of any particular non-compete provision is very dependent on both the exact language of the non-compete provision and the exact facts and circumstances surrounding the employer and employee, their relationship during the term of employment, and the nature of the employee's conduct and activities after the termination of that employment.

In general, in order to be enforceable a non-compete provision must be reasonable with respect to the employer, the employee, and the public interest. In determining whether or not a non-compete provision is reasonable, courts will generally consider whether the employer has legitimate interests to protect in the context of the applicable non-compete provision's restrictions on the employee's right to practice his trade or profession over a period of time and within a certain geographical location. In order to be enforceable, the non-compete restrictions, including the scope of the restricted activity, the length of time the restriction lasts, and the geographic area to which the restriction applies, must generally all be determined to be both reasonable and necessary to protect the employer's legitimate business interests under the particular facts and circumstance of the case (including the specific facts and circumstances of the employer, the specific employee, and the specific post-termination conduct and activities of the employee).

Michigan and Indiana law differ in at least one very important respect when it comes to the interpretation and enforcement of non-compete provisions. Indiana courts subscribe to the "blue pencil doctrine." Under this doctrine, if an Indiana court finds a provision of a non-compete agreement to be to be unreasonable, the court will only strike-through and delete language from the provision, but will not add any language to the provision. If the court cannot revise the agreement in this manner to make the provision reasonable, then the court will most likely not

enforce that provision of the agreement. Michigan courts, on the other hand, apply a different standard based on Michigan statutory and case law. Under Michigan law, if the covenant is unreasonable in any respect, the court may limit its terms in order to render it reasonable in light of the circumstances in which it was made and specifically enforce it. Michigan courts do not limit themselves to only deleting language from the unreasonable provision, but also permit themselves latitude to add or change language to make the provision enforceable.

The following is a fact pattern describing a relatively common scenario for a company's employment and development of a sales person. That fact pattern is followed by examples of two different non-compete agreements the company might want that employee to sign, one of which would most likely be enforceable if carefully drafted and the other of which would most likely not be enforceable.

Fact Pattern:

Acme Company ("Acme") employs Wiley Coyote ("Coyote") as a sales person to sell Acme's product line. Acme provides Coyote with sales training, establishes Coyote's sales territory as the entire State of Indiana, and introduces Coyote to Acme's customers for the product line in that sales territory. Acme encourages and facilitates Coyote's establishment of good personal relationships with the primary purchasing contacts at each of the customers for the product line in Coyote's territory. During Coyote's employment, Coyote makes sales to Acme's customers throughout all of Indiana, but does not make sales to any of Acme's customers outside of Indiana.

Likely Enforceable:

At the outset of Acme's employment of Coyote, Acme has Coyote sign a non-compete agreement. The non-compete agreement provides that during the term of Coyote's employment and for a period of one year after the termination of employment by Coyote for any reason or by Acme for cause, Coyote will not solicit any of Acme's existing customers in Indiana that were served by Coyote during his employment by Acme. This restriction is further limited to solicitations of those customers for the purpose of causing them to become customers of any business that provides products or services similar to Acme's within Indiana. After Coyote works for Acme for two years, he notifies Acme that he is leaving Acme to become a sales person for Beta Company ("Beta"), a direct regional competitor of Acme, selling a directly competing product line to the same customer base in Indiana. Acme will most likely be successful in enforcing its non-compete agreement against Coyote and, if necessary, against Beta, to prohibit Coyote from soliciting for Beta any of Acme's customers in Indiana that were served by Coyote during his employment by Acme.

Likely NOT Enforceable:

At the outset of Acme's employment of Coyote, Acme does not have Coyote sign a non-compete agreement. Two years later, however, Acme requires that Coyote sign a non-compete agreement as a condition of his continued employment. The non-compete agreement provides that during the term of Coyote's employment and for a period of three years after the termination of that employment by Acme or Coyote for any reason, Coyote will not work in any capacity for

any company that directly or indirectly competes with Acme anywhere in the states of Indiana, Illinois, Michigan, and Ohio in regard to any product or service provided by Acme. Six months after Coyote signs the non-compete agreement, Acme terminates Coyote's employment without cause. Needing to make a living and provide for his family, Coyote is able to secure a job with Beta in a non-sales capacity at one of Beta's plant locations across the state line in Michigan. If Acme were to seek to enforce the non-compete agreement against Coyote, or Beta, to prohibit Beta's employment of Coyote in a non-sales capacity in Michigan, Acme would most likely not be successful in doing so.

The two examples above intentionally represent opposite ends of the spectrum of enforceability. There are a number of reasons for the conclusion that that one of the non-compete agreements would likely be enforceable and the other would not. Some of those reasons relate to the different provisions included in the non-compete agreements and others relate to the different factual circumstances in which the agreements are to be enforced. Some of the reasons are seemingly based on fairness and common-sense, while others are seemingly based on application of abstract legal principles. Perhaps most importantly, some of the reasons that you may feel are important in making the determination may not be even be considered by a court or if considered may be inconclusive.

Non-compete agreements can be a valuable and relatively inexpensive tool for an employer to reasonably protect its business interests, but the use of these agreements is not simple and not without risk. Please note that the above discussion is intended only as a summary and should not be relied upon to determine the enforceability of any individual non-compete agreement, since the enforceability of a non-compete agreement is highly dependent on the individual facts and circumstances of the employer, the employee, and the actual language of the non-compete agreement.

If you are considering the use of a non-compete agreement with your employees, or if you are confronted with a circumstance involving a prospective or current employee's non-compete agreement obligations to a former employer, please seek the advice of a legal professional.



eseigel@thklawfirm.com
www.thklawfirm.com

Eric W. Seigel, Partner

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This article is for informational purposes only and should not be relied upon as legal advice. If you are in need of assistance with the preparation or review of a non-compete agreement, you should seek the advice of a legal professional.