

Virginia

Regulatory Hot Tip 2012 – 4

Professional Insurance Agents Association of Virginia and DC, Inc.

Would the Absence of Non-Compete Agreements Impact Your Business?

Historically, Non-Compete Agreements have been common creatures in the insurance industry. Because the business of insurance is a true personal service business, they have been used to protect proprietary processes and work product related to prospecting, marketing and the actual sales of insurance products. Keeping such information close to the vest, so to speak, has oftentimes helped an agency maintain its competitive edge over other agencies. This is especially true when an agency has located and cultivated a particularly skilled non-owner producer. The loss of, or unfair competition from, such a producer who leaves one agency for another or who goes out on his or her own has caused Non-Compete Agreements to be a norm in our industry.

Non-Compete Agreements are part of a body of agreements also known as restrictive covenants, which include non-solicitation, non-disclosure, non-circumvention, and other related agreements that restrict the manner in which the signatory conducts business ongoing after leaving a former employer or business relationship. Non-Competes come in a variety of forms, but commonly include restrictions on the geographic area in which the signatory can operate a competing

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business and/or restrictions on contacting former clients or employees with the intention of getting them to move their business.

Remember that a Non-Compete Agreement is first and foremost a contract, meaning that among other things, it needs certain legal elements to be enforceable, including an offer, an acceptance and consideration. When employers decide that they want their existing employees to sign a Non-Compete Agreement in the middle of their employment term, it brings up the issue of consideration. What is the employer willing to pay his or her current employees for accepting those restrictions? If the employer is not willing to give something up in return for the employees' acceptance of the restrictions, then there is no consideration and the Non-Compete Agreement would not be enforceable.

It is important to note that Non-Compete Agreements are not appropriate for every employee. Be selective and consider which employee positions really call for such restrictions or your business will suffer damage. In addition, make sure that you draft any and all restrictions as narrowly as possible to protect the employer's legitimate business interests as well as the employee's ability to find comparable work.

Some advocates of Non-Compete Agreements might argue that such restrictions are crucial to maintaining the integrity of the insurance industry as we know it because the presence of restrictive covenants tends to add to the value of insurance businesses. If employees could freely take customer lists, trade secrets concerning the sales process, or other proprietary information with them when they depart, and use this information to compete with their former employer in that employer's trade territory, some might conclude that the employer's business value would be drastically reduced.

Yet, during the 2012 session of the Virginia General Assembly, an attempt was made to all but eliminate Non-Compete Agreements in Virginia. Although this bill did not make it out of committee, we feel certain that we have not seen the last of this issue. The supporters of this legislation have been very vocal in their quest to rid the Commonwealth of Virginia of Non-Compete Agreements in most situations.¹

This bill effectively would have made it unlawful to restrict employees through Non-Compete Agreements which "restrict(s) an employee or former employee

¹ Exceptions in the proposed 2012 legislation allowed non-compete agreements related to the sale of a business or the departure of a former member of an LLC or former partner in a partnership.

from engaging in a lawful profession, trade, or business of any kind.”² Of note is a savings clause at the end of the proposed 2012 legislation stating that the proposed language was not intended to “limit the creation or application of nondisclosure agreements intended to prohibit the sharing of certain information, including but not limited to trade secrets and proprietary or confidential information.”³ Advocates of the abolition of Non-Compete Agreements argue vociferously that they restrict free trade, and an individual’s right to use his or her education and training in another position within the restricted footprint.⁴

Historically, Virginia courts have enforced Non-Compete Agreements provided they are narrowly drawn. However, the Supreme Court of Virginia appears to be slowly altering its position regarding the enforceability of such restrictive covenants. In fact, in a recent 2011 decision, the Court held that a certain non-compete provision was not enforceable;⁵ what makes this decision so interesting is that in 1989 the Court held that the exact same contract was enforceable.⁶ In its recent opinion, the court indicated that there have been incremental changes over time that have caused this reversal in its determination of whether the contract was “enforceable.”

The dissenting opinion in this recent Supreme Court opinion pointed out that the two cases involved the very same company and business interests and the recent agreement was identical to the non-compete upheld in 1989. The dissent opined that “[i]n overruling *Paramount*, the majority in effect penalizes the eminently and uniquely justified reliance of this Virginia business upon this prior precedent in ordering its affairs after prevailing in the prior case.” Because such agreements do act as a restraint on trade and arguably prevent citizens from pursuing a lawful trade or occupation, Virginia courts interpret such contracts very carefully, and resolve any ambiguity against the Agreement’s drafter, who is usually the former employer. It is this tension between the right of an employer to protect the value of his business and the right of a citizen to earn a living that is at the heart of every Non-Compete Agreement.

Many of you have signed Non-Compete Agreements in one format or another. Many of you routinely ask your licensed employees or independent contractors to sign Non-Compete Agreements. You should be aware of legislative efforts to

² H.B. 1187, 2012 Gen. Assemb., Reg. Sess. (Va. 2012).

³ *Id.*

⁴ Todd Benjamin, *Non-Compete Agreements Harm Workers, Business*, RICH. TIMES DISPATCH, Feb. 6, 2012, at A13.

⁵ *Home Paramount Pest Control Companies, Inc. v. Shaffer*, 282 Va. 412, 718 S.E.2d 762 (2011).

⁶ *Paramount Termite Control Co., Inc. v. Rector*, 238 Va. 171, 380 S.E.2d 922 (1989).

restrict or eliminate such agreements in the future, and you should also make sure that any Non-Compete Agreements that you use are carefully reviewed by your counsel prior to use.