Virginia
Regulatory Hot Tip 2016 – 3
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NON-COMPETE AGREEMENTS: SWORD AND SHIELD

In an era of intense business competition and unprecedented employee turnover, your agency may become involved with non-compete agreements ("non-competes"). These agreements place certain restrictions on an employee's ability to work for a different company in the same field. Any employer who does not understand the role of non-competes (i) risks injury to his agency when a key employee leaves, or (ii) faces potential liability to a competitor when hiring one of its former employees.

Historically, there were few constraints on an employee's ability to work for a rival business after leaving his former employer. Business owners gradually began using non-competes to limit their employees' future mobility in the marketplace. The response of the judicial system was to regard non-competes as unenforceable restraints on trade. Gradually, however, courts became more willing to uphold these restrictions as long as they passed a three-pronged test.

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The **first prong** addresses a non-compete's *reasonableness as to the employer*. Is enforcement of the restriction necessary to protect the employer's legitimate business interests, and does it go no further than protecting those interests? An affirmative answer supports enforcing the restriction and then leads to the **second prong**.

Is the restraint *reasonable as to the former employee*? Three factors are key in resolving this issue. Is the non-compete agreement reasonable as to prohibited duration? Courts have held that non-competes extending for as long as five years are enforceable. There are numerous decisions granting employers protection for two or three years. The current trend favors shorter periods.

Next, is it reasonable as to the prohibited territory? Sometimes a non-compete will restrict the former employee within a certain radius from the location of the employer's business. Non-competes with as much as a 50-mile radius have been enforced. Another approach prohibits dealing with the customers of the employer without regard to the employer's location. Courts tend to respond favorably to this approach.

The remaining factor is reasonableness as to prohibited activity. Courts tend to favor non-competes if they preclude only those activities in which the employee engaged in his previous employment. An employer must be careful not to impose constraints on activities in which the employee did not participate even if the employer's business encompasses such activities. For example, an automobile dealership should avoid attempting to prevent one of its mechanics from accepting a sales position at another dealership, because the mechanic did not sell cars in his former position.

If the non-compete is reasonable as to duration, territory and activity, courts then consider the **third prong**: *reasonableness as a matter of public policy*. Although the public interest is generally served when contracts are enforced, there may be judicial concern over limiting the availability of certain services in a particular community. For example, if there is a shortage of emergency medical personnel in a rural locality, public policy may be violated by restricting someone from participating in that field. As a general rule, however, public policy considerations do not invalidate an otherwise reasonable non-compete. This is likely to be true in the insurance business.

An employee and his would-be employer can test the enforceability of a non-compete by filing what is known as a declaratory judgment lawsuit. In that proceeding, a judge will declare the rights and obligations of the parties *before* the employee begins

working for a new company. However, do not expect a ruling within a few months; for that reason alone, declaratory judgment actions may not be a practical solution.

If the employee has already begun working for a competitor, the former employer can request a court to enjoin the violation of a non-compete. Although injunctive relief is an extraordinary remedy, it can be granted where the former employer's damages are both ongoing and difficult to calculate. The former employer may also pursue being awarded the new employer's profits already derived from a non-compete violation.

A word of caution: Virginia courts will not revise a non-compete in order to enforce it. Overwhelmingly, judges decline to impose on the parties a contract different from their original one by re-writing the non-compete to either eliminate or modify objectionable language. Thus, be conservative in imposing restrictions on the employee. A narrowly-drawn but nonetheless enforceable non-compete is far better than one giving you greater protection but which may be declared as unenforceable.

Another word of caution: Do not attempt to draft a non-compete without legal assistance. Consider it akin to cutting a diamond—one wrong move and you will render it worthless.