

# Strategies for Defending Against Non-Compete Litigation

by R. Scott Oswald and Jason Zuckerman

## I. Introduction

To prevent losing valuable employees and trade secrets to competitors, a growing number of employers are requiring employees to sign non-compete agreements. In the current economic climate, it is fairly challenging for most persons to find work. Trying to find a job that is consistent with the limitations in a non-compete can be unduly burdensome and in some instances may preclude a laid-off worker from earning a livelihood, without receiving any compensation from the former employer whose restrictive covenant is preventing the employee from working. The good news for employees is that in Virginia, non-competes are critically examined and a broad-form agreement that is not narrowly tailored to serve the employer's business interest is likely unenforceable. In addition, an employer's effort to enforce an invalid non-compete can give rise to sanctions and tort liability. This article suggests strategies to consider when defending against a lawsuit seeking to enforce a non-compete.<sup>1</sup>

## II. Is the Restrictive Covenant Valid?

In Virginia, courts enforce non-compete agreements only when "the contract (1) is narrowly drawn to protect the employer's legitimate business interest, (2) is not unduly burdensome on the employee's ability to earn a living, and (3) is not against public policy."<sup>2</sup> This analysis focuses primarily on the following factors: (1) the temporal scope of the non-compete; (2) the geographic scope of the non-compete; and (3) the clarity and unambiguous nature of the non-compete.

In other words, an employer must narrowly tailor

the time, function, and geographic restrictions in a non-compete agreement to protect nothing more than its legitimate business interest.<sup>3</sup>

## A Non-Compete Must be Narrowly Drafted

In *Omniplex World Servs. Corp. v. United States Investigations Serv.*,<sup>4</sup> for example, the Virginia Supreme Court held that the non-compete provision in question was overly broad and unenforceable because the language of the restrictive covenant barred the employee from performing "any services... for any other employer in a position supporting OMNIPLEX's customer."<sup>5</sup> The employee provided "general administrative security support, monitoring alarms and intrusion detection system[s]" for her employer, Omniplex.<sup>6</sup> After a few months of employment with Omniplex, the employee received a job offer for an administrative assistant position with another company where her duties would be limited to arranging travel, and obtaining visas and passports.<sup>7</sup> Despite the obvious differences between the employee's new duties and those performed in her former position, Omniplex filed suit against her to enforce the non-compete. According to Omniplex, the employee violated the non-compete by working for an employer who supported an Omniplex customer.<sup>8</sup> The Court, however, rejected Omniplex's argument, finding that a covenant not to compete is enforceable only where it prohibits employees from competing directly with the former employer or prevents employment with a direct competitor, not where it prohibits a former employee from any form of employment, including work wholly unrelated to the employee's work for the former employer.<sup>9</sup> The Virginia Supreme Court reiterated this principle in *Motion Control Sys. Inc. v. East*,<sup>10</sup> when it declared a non-compete unenforceable because it "imposed additional restraints which [were] greater than reasonably necessary to protect [the employer] in [its] legitimate business enterprise."<sup>11</sup> In particular, the non-compete restricted a former engineering manager from doing work for "any business that designs, manufactures, sells or distributes motors."<sup>12</sup> The Court found that the stated prohibitions could include a wide range of enterprises unrelated to "the business actually being protected," and there-

fore could not be enforced.<sup>13</sup> The message to be gleaned from these cases is that a Virginia court will not enforce a non-compete that fails to limit the scope of prohibited employment to those businesses that engage in activities that are “the same or similar” to those of the former employer.

## **B Non-Compete Must Not Be Unduly Burdensome on the Employee**

To be enforceable, a non-compete must be reasonable in function, duration, and geographic scope. For example, Virginia courts likely would not enforce a restrictive covenant that forbids an employee from engaging in the business of importing cigars anywhere in the world due to the unlimited geographic scope of the provision.<sup>14</sup> Similarly, a non-compete that prohibits a former plumber from working in any “household” in 38 states is likely unenforceable because the restriction would unduly hinder the plumber’s ability to earn a living.<sup>15</sup> Virginia courts will not enforce a restrictive covenant that is “unduly harsh, and oppressive in curtailing [an employee’s] legitimate efforts to pursue her livelihood,”<sup>16</sup> including a non-compete that:

- applies for an unlimited time;
- extends the restrictions to areas where the employer once did business;<sup>17</sup>
- extends the restrictions to locations where the employer only intends to do business; or
- extends the geographic reach of the agreement to an area that is not coterminous with that of the business at the time of the agreement.<sup>18</sup>

In determining the reasonableness and enforceability of restrictive covenants, however, courts do not consider function, geographical scope, and duration as three separate and distinct issues,<sup>19</sup> but instead consider these limitations together.<sup>20</sup> Thus, courts will enforce an agreement that, for one year and without geographical limitations, forbids an employee from selling publications that compete with the employer’s publication because it “limits the prohibited activities to those in direct competition” with the employer and “does not prohibit [the employee] from continuing to work in [his] field.”<sup>21</sup> Conversely, Virginia courts will

find a non-compete that lacks geographic limitation, applies a lengthy time restriction, and restricts “any business similar to the type of business conducted” by the corporation, unduly harsh and unenforceable.<sup>22</sup> While these examples provide guidance on what Virginia courts likely will consider reasonable, there is no hard and fast rule. Each case will turn on its own facts and the reasonableness of the restraint will, among other things, be determined by the position and seniority of the employee, the length of the employee’s service, the nature of the industry, and the length of time during which any trade secrets giving rise to enforcement of a non-compete are expected to remain economically valuable to the employer.

## **C Non-Compete Must Not Be Contrary to Public Policy**

A non-compete may be unenforceable where it goes against public policy, including where the non-compete imposes anticompetitive restraints on trade,<sup>23</sup> requires an employee to abandon the only occupation for which the employee is trained, or obliges an employee to relocate in order to be able to work. For example, in *Wheeler v. Fredericksburg Orthopedic Assocs., Inc.*,<sup>24</sup> the covenant restricted a doctor in a sub-specialty medical practice from practicing medicine within a thirty-five mile radius of his former employer. The court invalidated the restrictive covenant, finding that Fredericksburg residents would suffer irreparable harm if the former employee was not allowed to practice medicine within a thirty-five mile radius of the city. In general, a Virginia court is likely to find a non-compete that restrains trade and defeats competition void as against public policy and thus unenforceable under Virginia law.

## **III. Consider Filing a Declaratory Judgment Against the Employer**

Where a former employer threatens to bring an action to enforce an invalid non-compete, consider striking first by filing a declaratory judgment action to declare the non-compete unenforceable. This strategy turns the table by forcing the employer to defend the

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validity of the non-compete and puts the plaintiff in the driver's seat. Prior to pursuing this strategy, however, it is important to evaluate potential counterclaims that the employer may bring once it is sued.

### IV. Assert the "Unclean Hands" Defense

To challenge an employer's attempt to enforce a non-compete, an employee may rely upon the "unclean hands" doctrine. According to this doctrine, "he who asks equity must do equity, and he who comes into equity must come with clean hands."<sup>25</sup> In the context of non-compete litigation, this doctrine provides that a court of equity will not enforce a non-compete where there is evidence demonstrating that the employer engaged in wrongful or inequitable conduct with respect to the matter in litigation. This defense is often raised where an employer unilaterally changes the terms and conditions of the employment agreement or breaches the employment agreement by refusing to pay an employee for owed wages and bonuses.<sup>26</sup> Other types of employer conduct that might constitute unclean hands include sexual harassment, racial discrimination, termination without cause, and retaliation against an employee who discloses information about the employer's violation of a federal or state regulation.

### V. Potential Tort Liability for Attempting to Enforce an Unenforceable Non-Compete

To apply maximum pressure on a former employee to comply with a non-compete, some employers routinely send demand letters to a former employee's new employer demanding that the new employer terminate its relationship with the employee. Where the employer is seeking to enforce an invalid non-compete, this tactic can give rise to tort liability.<sup>27</sup>

Virginia courts recognize a cause of action for tortious interference of a business or contractual relationship where there is an "intentional interference with contract inducing or causing a breach or termination of the relationship or expectancy."<sup>28</sup> The tort of tortious interference requires a plaintiff to establish: (1) the existence of a valid contractual relationship or business expectancy; (2) knowledge of the relationship or

expectancy on the part of the interferer; (3) intentional interference inducing or causing a breach or termination of the relationship or expectancy; and (4) resultant damage to the party whose relationship or expectancy has been disrupted.<sup>29</sup> While Virginia courts have not yet addressed a claim for tortious interference against a former employer, cases from other states hold that a former employer can be liable for tortious interference where a new or potential employer withdraws an offer of employment because the former employer, in bad faith, threatened to enforce a non-compete. In *Voorhees v. Guyan Mach. Co.*,<sup>30</sup> a West Virginia court recognized a claim for tortious interference where a former employee's new employer terminated his employment after receiving threats that the former employer "would go to the highest court of the land to enforce [the non-compete]," and the employee was terminated by his new employer. The *Voorhees* Court concluded that the extent of competition between the former and new employer was so minimal that the former employer lacked a legitimate business interest warranting enforcement of the non-compete. The employee recovered both compensatory and punitive damages for the harm he suffered as a result of the employer's improper threat to enforce an unenforceable non-compete.

### VI. Potential Sanctions for an Employer Seeking to Enforce an Invalid Non-Compete

Virginia law prevents courts from revising or "blue-penciling" overly broad portions of a non-compete to sever unenforceable provisions. Thus, if one provision is invalid, the entire non-compete is invalid and unenforceable as a matter of law. If an employer seeks to enforce a non-compete that is obviously void, an employee may move for sanctions against the employer and its attorney for bringing a frivolous suit.

### VII. Request the Inclusion of a Garden-Leave Provision

Before signing a non-compete agreement, an employee should request that the employer include a "garden-leave" provision in the non-compete. A garden-leave clause requires the employer to continue pay-

ing the former employee her salary and benefits in exchange for the employee's agreement not to compete with the employer. This arrangement benefits both the employer and the employee because it gives employers necessary protection against unfair competition yet ensures that employees are financially secure during the non-compete period. While Virginia courts have not yet addressed the enforceability of a garden-leave provision, other courts have held that a former employee is entitled to garden-leave pay where she is unable to find new employment because of a non-compete.<sup>31</sup>

## VIII. Conclusion

In sum, an employee faced with a lawsuit to enforce a non-compete or faced with the threat of non-compete litigation has many options to challenge the enforceability of the non-compete, including the unclean hands defense. In addition, an improper attempt by an employer to enforce a non-compete can give rise to tort liability and sanctions. As a lawsuit to enforce a non-compete is typically accompanied by a motion for a preliminary injunction or a motion for a temporary restraining order, it is critical to quickly assess and implement options available to the employee to gain the upper hand in the litigation.

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<sup>1</sup> This article is intended only to provide basic information concerning non-compete litigation. It is not, nor is it intended to be, legal advice upon which you should rely or act.

<sup>2</sup> *Omniplex World Servs. Corp. v. United States Investigations Servs., Inc.*, 270 Va. 246, 249 (2005).

<sup>3</sup> *Simmons v. Miller*, 261 Va. 561, 581 (2001) (holding that analysis of the three factors "requires consideration of the restriction in terms of function, geographic scope, and duration."); See also *Advanced Marine Enters., Inc. v. PRC, Inc.*, 256 Va. 106, 119 (1998) (finding that eight-month duration informed the evaluation of both the geographic scope and function components of a restrictive covenant).

<sup>4</sup> *Omniplex*, 270 Va. at 250 (2005).

<sup>5</sup> *Id.*

<sup>6</sup> *Id.* at 248.

<sup>7</sup> *Id.*

<sup>8</sup> *Id.* at 254.

<sup>9</sup> *Id.* at 249.

<sup>10</sup> *Motion Control Sys., Inc. v. East*, 262 Va. 33, 36 (2001). See also *Modern Env't Inc. v. Stinnett*, 263 Va. 491, 493-94 (2002).

<sup>11</sup> *Id.*

<sup>12</sup> *Id.* at 38.

<sup>13</sup> *Id.* at 36, 38.

<sup>14</sup> *Id.*

<sup>15</sup> *Phoenix Renovation Corp. v. Rodriguez*, 439 F. Supp. 2d 510, 521-22 (E.D. Va. 2006)

<sup>16</sup> *Simmons v. Miller*, 261 Va. 561, 581 (2001) (finding a non-compete agreement to be unenforceable where the restriction was lengthy in duration, was without any geographical limitation, and was unduly harsh and oppressive in curtailing the employee's legitimate efforts to pursue her livelihood).

<sup>17</sup> *Roanoke Eng'g Sales Co. Inc. v. Rosenbaum*, 223 Va. 548, 553 (1982).

<sup>18</sup> See e.g., *Meissel v. Finley*, 198 Va. 577, 582 (1956) (affirming non-compete agreement that prohibited former partner from writing insurance or surety bonds for five years within 50-mile radius).

<sup>19</sup> *Omniplex*, 270 Va. at 255.

<sup>20</sup> *Id.*

<sup>21</sup> *Mkt. Access Int'l., Inc., v. KMD Media, LLC*, 272 Va. Cir. 355, 359 (Fairfax County 2006) (non-compete agreement that had no geographical limitation was still enforceable because it allowed employee to continue to work in his field).

<sup>22</sup> *Simmons*, 261 Va. at 581.

<sup>23</sup> *Omniplex*, 270 Va. at 249 (concluding that "[b]ecause such restrictive covenants are disfavored restraints on trade... any ambiguities in the contract will be construed in favor of the employee.").

<sup>24</sup> *Wheeler v. Fredericksburg Orthopedic Assoc.*, 44 Va. Cir. 399, 402 (1998).

<sup>25</sup> *Albert v. Albert*, 38 Va. App. 284, 299 (2002) (citing *Walker v. Henderson*, 151 Va. 913, 927-28 (1928)).

<sup>26</sup> *Parr v. Alderwoods Group, Inc.*, 268 Va. 461 (2004) (Employer's breach of the integrated contract precluded it from enforcing the remaining provisions of the contract, including the non-compete provisions. Accordingly, employee was relieved of any obligations under the restrictive covenant).

<sup>27</sup> *Hilb, Rogal & Hamilton Co. of Richmond v. DePew*, 247 Va. 240 (1994) (articulating the rule that a tort action exists against one who intentionally interferes with another's contractual rights).