

So, you're concerned about employee competition. Tips for effective covenants not to compete.

By John F. Reha

DISCLAIMER/NOTE: The author is not giving any legal advice to the reader of this article. The reader is advised to seek advice from counsel competent in the areas of competition restrictions before taking any action. No attorney-client relationship exists between the author and the reader unless and until the reader formally retains the author as counsel.

Increasingly, employers are turning to agreements restricting employees from competing or using confidential information. Colorado's Non-Compete Statute presents numerous issues not present in other states regarding the validity and enforceability of non-competes. This article provides tips for drafting effective and enforceable competition and trade secrecy restrictions.

1. The Non-Compete Statute's Default Rule of Invalidity. The Non-Compete Statute starts by declaring all non-competes "void." Void means completely invalid and unenforceable.

2. Exceptions. The Non-Compete Statute then goes on to create three exceptions where non-competes will be enforced. They are:

a. Sale of business. If the covenant not to compete arises out of the sale of a business it will be enforced, *at least as to those persons who are involved in the sale itself such as stockholders, owners, etc.* Enforcement under this exception does not extend to employees who have no meaningful ownership position in the business.

b. Professional staff. Non-competes entered into with "executive and management personnel and officers and employees who constitute professional staff to executive and management personnel" are also enforceable. Whether an employee is an executive or management employee will depend upon that employee's duties. The Colorado courts have stated that actual management responsibilities such as supervising other employees is necessary for an employee to be a manager or executive. Further, "professional staff to executive or management personnel" has been limited to those employees who are both (1) employed as "professionals," and (2) engage in their profession as part of the employer's key management team. Thus, the professional staff portion of this exception reaches only a few employees.

c. Trade secrecy. Non-competes are also enforced to the extent they protect legitimate trade secrets. What qualifies as a legitimate trade secret is often a major point of contention that centers around the Colorado Uniform Trade Secrets Act and associated case law. Thus, a comprehensive understanding of the law is essential to navigating through this fluid concept. The trade secrecy exception will not support a complete bar to any post-termination competition, but only the use of a trade secret in such competition.

3. Reasonableness. If a non-compete satisfies the Non-Compete Statute, it must still be reasonable as to time, geography and scope. In a number of states, this “reasonableness” rule is the only limitation to enforcement of non-competes. While the Non-Compete Statute renders this untrue in Colorado, to be enforceable the competition restriction must still meet all reasonableness considerations, even assuming it falls into one of the three exceptions noted above.

4. Effective drafting. Obviously, the goal of any agreement not to compete in Colorado is to comply with the Non-Compete Statute. This usually equates to language incorporating the three exceptions above. Non-competes that are part of a business sale will be enforced, as will those with employees who truly are executives or managers. For others (typically non-manager salespersons), effective trade secrecy language is necessary in order for enforcement under the trade secrecy exception. Provisions for effective remedies, including injunctive relief, should be considered as well.

5. Meaningful enforcement. When it comes to enforcing competition restrictions, time really is money. Since a customer base can rapidly disappear, pursuing rapid injunctive relief barring the ex-employee from competition should be strongly considered. Monetary damages may be sought as well.

6. Other Law. Colorado has a number of other legal principles that are applicable to employee competition, trade secrecy misappropriation and other matters. Knowledgeable counsel should know and understand these.

7. What to do. If you are contemplating incorporating a competition restriction with your employees, you should consult with counsel that has expertise in the areas of competition and trade secrecy. While some attorneys specialize in this area, a number of attorneys do not. It is thus doubly important that the client seek out an attorney who has a full, in-depth understanding of the special rules that apply to competition and trade secrecy in Colorado and the other legal principles associated with these subjects. Validity of any restrictions may ride on it.

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