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NEW MASSACHUSETTS LAW SPECIFIES REQUIREMENTS FOR NONCOMPETITION AGREEMENTS

The Massachusetts Noncompetition Agreement Act (the “Act”) codifies new requirements for noncompetition agreements entered into with Massachusetts employees and independent contractors on or after October 1, 2018.

The Act contains a number of explicit rules employers must follow in drafting noncompetition agreements, while simultaneously leaving many questions unanswered.

NOT ALL RESTRICTIVE COVENANTS ARE NONCOMPETITION AGREEMENTS

The term “non-compete” often can be used casually to refer to all post-employment restrictions. However, noncompetition agreements are actually only one subset of a much larger group of post-employment restrictions. That group includes:

- 1) covenants not to solicit or hire employees;
- 2) covenants not to solicit or transact business with customers, clients or vendors;
- 3) nondisclosure or confidentiality agreements; and
- 4) invention assignment agreements, among others.

The Act does not apply to any of the foregoing restrictions and also expressly exempts:

THE BOTTOM LINE

With this Act going into effect on October 1, 2018, it is critical that employers in Massachusetts: (1) review their existing restrictive covenant agreements to ensure that they are enforceable, and (2) update their form documents to comply with the Act going forward.

- 1) certain agreements made in connection with the sale of a business entity or other similar circumstances;
- 2) agreements outside of an employment relationship;
- 3) certain forfeiture agreements;
- 4) separation agreements (if the employee is expressly given seven business days to rescind acceptance); and
- 5) agreements by which an employee agrees to not reapply to the same employer after termination.

The Act only applies to “noncompetition agreements,” which it defines as agreements “under which the employee or expected employee agrees that they will not

engage in certain specified competitive activities with the employer after the employment relationship has ended.” Accordingly, employers should continue to be guided by existing Massachusetts law in the drafting and implementation of other restrictive covenants.

NOT ALL EMPLOYEES ARE CREATED EQUAL

Many employers use the same form of restrictive covenants for all employees – from the mail room to the C-suite. While this was not the recommended practice even before implementation of the Act, it is now clear that different levels of employees will require different agreements. The Act lists certain groups of employees with whom employers may not enter into

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noncompetition agreements. Those groups are:

- 1) employees classified as nonexempt under the Fair Labor Standards Act;
- 2) students;
- 3) employees who have been terminated without cause or laid off; and
- 4) employees who are 18 years old or under.

As a result, employers will need to refine their form restrictive covenant documents and create a tiered system of documents based on each employee's level within the company.

NONCOMPETITION AGREEMENT REQUIREMENTS

The Act requires that all permissible noncompetition agreements must meet certain basic requirements. They are:

- >> Agreements must be in writing and signed by both parties.
- >> They must state that the employee may consult with counsel prior to signing.
- >> If the employee enters into the agreement in connection with the commencement of employment, it must be provided before a formal offer of employment is made or 10 business days before they start work, whichever comes first.
- >> If the agreement is entered into while the employee is working, the employer must provide the agreement at least 10 business days before its effective date and it must be supported by "fair and reasonable consideration independent from the continuation of employment."
- >> The agreement must protect a legitimate business interest of the employer (trade secrets, confidential information or goodwill).
- >> Noncompetition periods should be limited to one year or less. However, "springing" noncompetition provisions would allow employers to extend the period up to two years (total) if the employer discovers that the employee engaged in theft or other breach of a fiduciary duty.
- >> The geographic scope may include only those locations where the employee provided services or had a material presence or influence within the last two years of employment.
- >> Employers must provide either "garden leave" or "other mutually-agreed-upon consideration" during the noncompetition period.

SUFFICIENCY OF CONSIDERATION DEPENDS ON WHEN THE AGREEMENT IS PROVIDED

If an employer asks a prospective employee to enter into a noncompetition agreement, the consideration for the agreement is that offer of employment. Accordingly, the Act does not require any further consideration at the time it is executed. However, if the agreement is provided during employment, the mere continuation of employment is not sufficient consideration, and instead the Act requires that other "fair and reasonable" consideration be provided. "Fair and reasonable" consideration is not defined in the Act, but based on pre-Act case law in Massachusetts, a promotion, bonus or raise should meet this standard. Case law that develops after passage of the Act will help employers as they endeavor to meet this requirement.

The Act also requires employers to provide either "garden leave" or "other mutually-agreed-upon consideration" during the period of noncompetition. The Act defines "garden leave" as a "provision within a noncompetition agreement by which an employer agrees to pay the employee during the restricted period." If the employer provides garden leave, the employer must pay the employee at least 50 percent of their highest annualized base salary over the two years preceding the termination. Employers

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do have the option to waive the noncompetition obligation to avoid such garden leave payments. However, once the employer elects to enforce the provision, it generally may not unilaterally discontinue payment unless the employee breaches the agreement or the employer discovers that the employee engaged in theft or other breach of a fiduciary duty.

If the employer does not provide garden leave, it must provide “other mutually-agreed upon consideration.” The Act does not define or provide any examples of what would be sufficient alternative consideration.

ENFORCING YOUR AGREEMENTS AND THE FABLED BLUE PENCIL

Employers seeking to enforce noncompetition agreements must bring legal action in the county where the employee lives or, if agreed between the parties, in Suffolk County (Massachusetts). The Act applies to actions brought against employees

who have lived or worked in Massachusetts for the 30 days prior to termination of employment. Choice of law or venue provisions inconsistent with the Act will not be enforced.

Compliance with the Act should ensure enforceability, but it is possible that a court will find that an employer overreached (e.g. the geographic area or scope of prohibited competitive activities is overbroad). However, even with such a finding, employers are not without protection. The Act states that courts have the discretion, but not the obligation, to revise an unenforceable noncompetition agreement to render it valid, and where an invalid noncompetition provision is part of a larger agreement, the court may uphold the rest of the agreement. This is often referred to as “blue-penciling” when the court uses a metaphorical blue pencil to cross out or revise unenforceable provisions and then enforces what remains.

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