

Preventing Competition as a Way to Compete: A Basic Primer on Non-Competition Employment Agreements in Virginia

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In competitive business environments that are relationship and/or information dependent non-competition agreements are increasingly being seen as a means to gain or maintain a competitive advantage. The actual and perceived growth of these business environments in Virginia has resulted in an ever increasing curiosity as to these special business agreements and how they are regarded under Virginia law.¹ This article is intended to satisfy some of that curiosity with some basic information on the legal fundamentals of non-compete employment agreements in Virginia.²

* **Non-Competition Agreements are Not Favored.** Virginia courts have long recognized that “where the tendency of the agreement between the parties is to lessen competition or raise the price of goods or commodities, it is injurious to the public”. *Klaff v. Pratt*, 117 Va. 739, 748, 86 S.E. 74, 78 (1915). Since competition is commonly viewed as a prime energy source fueling innovation, lower prices, greater productivity, and better products and services, courts take a dim view of contracts which act to restrain competition.

¹ This article is intended only to provide only very basic information concerning selected issues relating to non-competition agreements under Virginia Law. It cannot substitute for competent legal counsel and advice from an experienced and licensed attorney. Every non-competition agreement is viewed under the law with regard to its own specific and unique facts and circumstances.

² Non-competition agreements are also increasingly common in the context of the sale of a business. A discussion of the legal issues related to these similar agreements is not within the scope of this article.

Where the means of restricting competition affect an individual's ability to earn a livelihood, the law takes an even dimmer view of such agreements. The very first principle to know in understanding non-compete agreements is that they will be looked at differently and with a more critical eye than a more run-of-the-mill contract. While the same requirements exist for the formation of a binding non-compete agreement as for any other contract, such as consideration and mutuality of obligation, because these agreements are disfavored they are subject to additional requirements. This does not mean that non-compete agreements are not enforceable, but rather that they are subject to a more rigorous scrutiny by courts.

* **Restrictions Can be No Greater than Necessary.** A corollary principle that flows from the legally disfavored nature of non-compete agreements is that the restrictions contained in the agreement can be no greater than reasonably necessary to protect a legitimate business interest. Logically, restrictions that are greater than necessary would have an undue adverse impact on competition which would be contrary to sound public policy (which favors competition).

Typically the restrictions on employment fall into three general areas that are the subject of legal scrutiny. The most commonly discussed are the restrictions on the duration of the non-competition provision and the geographic area in which the employee is precluded from working. Less commonly discussed, but equally important, is the role or roles, or type of employment, which is to be precluded.

* **Language Construed in Favor of the Employee.** The language of non-compete employment agreements will be construed against the employer and in favor of the employee. "Virginia law requires that non-competition clauses be strictly construed against the employer." *Grant v. Carotek, Inc.*, 737 F.2d 410, 411 (1984). Where the language of the

agreement is subject to more than one meaning, the meaning which favors the employee will be adopted. Some courts have held that where the restrictions can be subject to such a broad application that they would be unreasonable, even though they may also be subject to a narrower and reasonable application, the agreement would be unenforceable. *Roto-Die Company, Inc. v. David Lesser*, 899 F. Supp. 1515, 1520 (1995)).

* **Legitimate Business Interest Required.** Non-compete employment agreements must have as a purpose the protection of a legitimate business interest. “[T]he employer bears the burden to show that the restraint is reasonable and no greater than necessary to protect the employer’s legitimate business interests.” *Motion Control Systems, Inc. v. East*, 262 Va. 33, 37, 546 S.E.2d 424, 425 (2001). Simply protecting against competition is not a legitimate business interest. While a business could enter into non-compete employment agreements with all of its employees, unless the employees have had exposure to confidential or proprietary information or the opportunity to develop unique private customer relationships there may not be a legitimate business interest to protect. For example, there would not likely be a legitimate business interest to protect with janitorial employees, but there likely would be with employees who have access to pricing, confidential customer lists, or product development information.

* **Limited Geographic Area.** Virginia courts have been consistent in ruling that there must be reasonable geographic limits on the reach of non-competition agreements. Some of the decisions seem to state that it is not reasonable to extend the geographic reach of the agreement into any area that is not coterminous with that of the business at the time of the agreement. See e.g., *Meissel v. Finley*, 198 Va. 577, 582, 95 S.E.2d 186, 190 (1956); area “practically coextensive with the business”; *Roanoke Engineering Sales Co. Inc. v.*

Rosenbaum, 223 Va. 548, 553, 290 S.E.2d 882, 885 (1982) “coterminous in area with the territory in which RESCO did business”. Where the employer seeks to extend the restrictions to areas where the employer once did business or intends to do business the agreement may be over broad in its geographic reach and perhaps unenforceable.

* **Restrictions Can Apply for Only a Limited Time.** In evaluating whether the duration of employment restrictions are reasonable, there is no specific time period which applies to all situations. In *Meissel v. Finley*, 198 Va. 577, 583, 95 S.E.2d 186, 190 (1956) the Supreme Court of Virginia upheld a five-year covenant not to compete where the five-year limit was directly related to a specific business need. That case involved an insurance business where the policies came up for renewal at five year intervals. The employee’s knowledge of the customers and when their policies were to expire would have allowed him to contact them prior to the expiration for the purpose of soliciting their business for a competing insurance business. The Court found that it was reasonable for the business to protect against that eventuality. Although each business will have its own particular justifications related to the duration of the restrictions, generally speaking, most employment non-compete agreements do not involve such lengthy durations, but instead, typically tend to preclude competitive employment for a year or two.

* **Restrictions Must be Limited to Actual Competition.** Under Virginia law employment non-competition provisions must not only be reasonable in geographic and duration restrictions, but they must only apply to employment in an actually competing role. Restrictions which prevent an employee from working “in any capacity” for a competing business are at substantial risk of being found unenforceable. This problem is most commonly found where the non-compete agreement has a blanket prohibition against

working for a certain business or industry and does not limit the restrictions to employment that would involve actual competition.

This principle was illustrated in *Modern Env'ts, Inc. v. Stinnett*, 263 Va. at 493-94, 561 S.E.2d at 695, where the Supreme Court of Virginia declared unenforceable a clause that forbade an employee from becoming involved “in any manner with the ownership, management, operation, or control of any business similar to the type of business conducted by the Company or any of its affiliates” The Court noted that the clause did not allow an employee to seek a “non-competing ‘role’” with a competitor company. The Supreme Court of Virginia recently reiterated this principle in *Omniplex World Svcs. Corp. v. U.S. Investigs. Svcs., Inc.*, 2005 Va. LEXIS 77, at *7 (2005) where it struck a non-competition clause for over breadth because the provision was not “limited to provisions competitive with [the employer].”

Under the proper circumstances, when carefully drafted, non-competition agreements may afford some protection for legitimate business resources in addition to unfair competition and trade secret misappropriation claims. Agreements must be carefully drawn with regard to the case specific realities of the business and interests involved. The restrictions must be no greater than reasonably necessary in geographic scope, temporal duration, and functional employment restrictions. Experienced legal counsel is essential both at the drafting and then, if need be, enforcement stage.

About the Author: John B. Simpson received his B.A. from Colgate University and his J.D. from the University of Hawaii’s William S. Richardson School of Law. He has been licensed to practice law since 1981 and is licensed to practice law in both Hawaii and Virginia. Mr. Simpson emphasizes trial advocacy representation primarily in commercial and real property disputes.