The Best Laid Plans … How Attempts to Enforce Restrictive Covenants Can Go Terribly Awry in Today's Legal Environment

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Imagine this scenario: Your business partners come to you visibly angry that a key employee has resigned to work for a direct competitor. The employee had signed a non-compete agreement supposedly precluding this move. The business directs you, as the company's general counsel, to "go to the mattresses" and spare no expense in suing the employee. A message must be sent. The business has grown weary of its chief rival poaching employees.

As the non-compete agreement is reasonably narrow, you are confident it complies with Tennessee law. You retain your go-to outside counsel, and they file suit in Tennessee. Although the employee works out-of-state, a forum-selection clause in the agreement designates Music City as the appropriate venue. The case seems like a slam dunk. The contract states the employee cannot work for a direct competitor.

To your surprise, the employee responds with a motion to dismiss, asserting the state in which he resides makes out-of-state forum selection clauses illegal, thus the voiding the entire contract. Making matters worse, the employee also files a charge of discrimination with the National Labor Relations Board (NLRB), arguing that your suit to enforce the restrictive covenant violates Sections 7 and 8 of the National Labor Relations Act (NLRA). Your company is union-free and you have had no dealings this agency.

The NLRB finds cause and takes the matter to complaint. The agency seeks to invalidate not just the employee's restrictive covenant, but *all such agreements* signed by *anyone* in your organization. Your business partners, perhaps forgetting their Sonny Corleone directive, are now angry with you, wondering how the business got to the point where all of the company's restrictive covenants might soon be voided.

How can this happen?

Recent developments in the non-competition landscape have made this scenario a realistic possibility. The validity of restrictive covenants is coming under

increasing pressure on seemingly all fronts and attempts to enforce such agreements require navigating many landmines.

Significantly, the NLRB has taken an aggressive stance on Section 7 rights, seeking to expand the NLRA's reach. On May 30, 2023, the NLRB General Counsel Jennifer Abruzzo issued a Memorandum titled "Non-Compete Agreements that Violate the National Labor Relations Act." In the press release announcing the Memorandum, General Counsel Abruzzo stated, "[T]he proffer, maintenance, and enforcement non-compete provisions in employment contracts and severance agreements violate the National Labor Relations Act except in limited circumstances." in her opinion, such agreements are unlawful because they chill employees from exercising their rights under Section 7 of the NLRA. Section 7 protects employees' rights to take collective action to improve their working conditions.

As the current NLRB sees it, in most circumstances, "[n]on-compete provisions reasonably tend to chill employees in the exercise of Section 7 rights when the provisions could reasonably be construed by employees to deny them the ability to quit or change jobs by cutting off their access to other employment opportunities that they are qualified for based on their experience, aptitudes, and preferences as to type and location of work."

General Counsel Abruzzo continued:

> This denial of access to employment opportunities interferes with workers engaging in Section 7 activity in a number of ways—for example, workers know that they will have greater difficulty replacing their lost income if they are discharged for exercising their statutory rights to organize and act together to improve working conditions; their bargaining power is undermined in the context of lockouts, strikes and other labor disputes; and their social ties and solidarity leading to improvements in working conditions at workplaces are lost as they scatter to the four winds.

As the dust has settled in the months since the general counsel's declaration on restrictive covenants, the NLRB has enforced its view on Section 7 and its application to such agreements. The agency has found cause on charges alleging violations of the NLRA when an employer filed suit against a former employee seeking to enforce a non-compete agreement. When taking the matter to complaint in such instances, the NLRB has sought significant remedies, including:

- Full attorneys' fees incurred by the former employee in defending the non-compete litigation;
- Rescission of the former employee's restrictive covenant;
- Rescission of *all* employees' covenants;
- Letters of apology from the CEO; and
- Nationwide postings of the NLRB's findings.

The agency has demanded that a company stay its pending non-compete litigation while the NLRB proceedings play out (perhaps for years). The consequences for getting on the NLRB's radar when attempting to enforce a restrictive covenant can be severe.

Restrictive covenants are also facing headwinds at the state level. California, Colorado, Oklahoma, Minnesota, and North Dakota have enacted complete bars to enforcing such agreements in most, if not all, circumstances. New York's governor recently vetoed such a bill but called for the legislature to send her a more narrowly tailored version to sign. Other states, such as Washington, have made it illegal to require an employee based in that state to enter a non-compete agreement with an out-of-state forum-selection clause. Violations of the NLRA come with strict liability for attorneys' fees and either statutory penalties or actual damages, whichever is greater.

When that business partner comes to you fuming that an employee is jumping ship, keep these bear traps in mind. Filing suit to enforce a non-compete agreement can bring great risk. Before taking on that risk, one must consider if the potential damage to the business by the employee's competition is worth it. A typical departure probably does not justify the risk of an NLRB enforcement action. If the potential damage to the business is truly worth it, consider how to plead to lessen that risk. If the former employee is arguably a supervisor, plead as such with particularity, as supervisors typically are not covered by the NLRA. General Counsel Abruzzo opined that there can be limited "special circumstances" where a non-compete might not violate Section 7. If you think such special circumstances exist with your employee's job duties or departure, plead them.

If the employee engaged in malfeasance prior to leaving (downloading files, emailing documents to herself, and the like), those bad acts may alter the balance of risk as this kind of activity makes the employee less sympathetic to the NLRB.

Remember to consider state law. Tennessee has generally maintained a reasonable hospitableness to narrowly tailored restrictive covenants. If your former employee is based in another state, however, that state's laws must be considered. A Tennessee forum selection clause may be of no use if the outside state is hostile to non-compete agreements (and threatens potential penalties and fees).

Lastly, one must also evaluate upcoming rulemaking by the Federal Trade Commission ("FTC"). On January 5, 2023, the FTC announced it was considering banning non-compete agreements in most circumstances. The notice and comment period has ended, and a final rule may be implemented soon.

In the right circumstance, where the risk to the business is truly dire, it may still make strategic sense to seek enforcement of a non-competition agreement through litigation. In today's environment, it is important to proceed cautiously.