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Understanding Non-Competition Agreements in New York

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Although non-competition agreements with employees are permitted in New York, courts generally enforce them in favor of employers only where the agreements are supported by adequate consideration and are deemed reasonable in scope. This article discusses the requirements under New York law governing provisions in employment agreements that restrict an employee's ability to compete.

Adequate Consideration

The adequacy of consideration is usually determined by a fact-specific inquiry. Typical forms of consideration highlighted in the case law have included: initial employment; continued employment of an at-will employee where discharge was the alternative, or where continued employment is for a "substantial period" after the non-competition agreement was entered into; promotion to a position of responsibility; a special monetary payment that the employee is not otherwise entitled to; and payment of benefits and salary during the employee's period of non-competition. See, e.g., *Zellner v. Stephen D. Conrad, M.D., P.C.*, 589 N.Y.S.2d 903, 907 (2d Dep't 1992) (continued employment); *BDO Seidman v. Hirshberg*, 690 N.Y.S.2d 854, 856-57 (1999) (promotion); *Maltby v. Harlow Meyer Savage, Inc.*, 633 N.Y.S.2d 926, 928 (Sup. Ct. N.Y. Cty. 1995) (payment of salary during garden leave period), aff'd, 637 N.Y.S.2d 110 (1996). The adequacy of consideration is typically not the determining factor or focus when parties litigate non-competition agreements.

What Makes an Agreement 'Reasonable'?

New York courts will enforce non-competition agreements if the agreements are deemed "reasonable." A non-competition agreement is reasonable only if it:

(1) is no greater than required to protect the employer's legitimate interest;

(2) does not impose undue hardship on the employee; and

(3) is not injurious to the public.

See *BDO Seidman*, 690 N.Y.S.2d at 856-57.

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Limited Scope

In assessing the reasonableness of the scope of a covenant not to compete, New York courts typically look at the temporal and geographic scope of the restrictions and the scope of the business activity restricted. Assessing the scope of a non-competition provision is a fact-specific inquiry. In some instances, the narrowness of one restriction might balance the breadth of another.

New York courts have generally found restrictions of six months or less reasonable. See, e.g., *Ticor Title Ins. Co.*, 173 F.3d 63, 70 (2d Cir. 1999) (six months); *Natsource v. Paribello*, 151 F. Supp. 2d 465, 470-71 (S.D.N.Y. 2001) (three months). Longer periods might also survive scrutiny based on the specific facts of the case. See, e.g., *Pontone v. York Grp.*, No. 08 CIV. 6314 (WHP), 2008 WL 4539488, at *5 (S.D.N.Y. Oct. 10, 2008) (three-year non-competition provision as part of a sale of business was reasonable where the buyer paid a significant amount of money to purchase the goodwill of the company, and the restricted individual was represented by counsel in the negotiations for the sale of the business, was intimately involved in the operations of the family business, and customers likely associated him with the company's reputation). But see *Heartland Sec. v. Gerstenblatt*, No. 99 Civ. 3694, 2000 WL 303274, at *7 (S.D.N.Y. March 22, 2000) (restrictive covenant of two years with no geographic limitation was unreasonable).

Similarly, New York courts will not enforce geographically over-broad restrictions. However, a broad geographic restriction might be enforceable where it is balanced by other, narrower terms. See, e.g., *Maltby*, 633 N.Y.S.2d at 928 (a restrictive covenant that prevented the former employee from working within the New York Metropolitan area, Los Angeles, Toronto, London, and Continental Europe was reasonable due to its six month duration and payment of the employee's base salary during this period).

> There is no overall state statute or regulation governing agreements not to compete in New York. However, certain industry-specific statutes and rules do apply.

New York courts will also not enforce restrictions on business activity that are deemed over-broad. See, e.g., *Godoy v. FDR Services Corp.*, No. 152540/2012, 2013 WL 1966707, at *1 (Sup. Ct. N.Y. Cty. May 6, 2013) (on a preliminary injunction motion, holding that a non-competition provision, "which contains no geographic limitation, [and] seeks to bar Plaintiff from working in an entire industry" was unenforceable).

Protectable Interests

New York courts have recognized, among others, the following "legitimate business interests" that may be protected by a non-competition agreement:

- An employer's trade secrets or confidential information.
- An employer's goodwill within an industry or market.
- An employer's interest in preventing competition with an employee whose services are special or unique.

See *BDO Seidman*, 690 N.Y.S.2d at 858-59; *Ticor*, 173 F.3d at 70.

Undue Hardship and Public Injury

A non-competition provision must not impose an "undue hardship" on the employee, nor cause "injury" to the public. For example, firing an employee without cause may nullify a non-competition agreement. See *Arakelian v. Omnicare*, 735 F. Supp. 2d 22, 41 (S.D.N.Y. 2010) ("Enforcing a non-competition provision when the employee has been discharged without cause would be unconscionable.") (internal citation and quotation marks omitted). Public policy concerns may also "militate against" a restrictive covenant that unduly fetters an employee's right to apply skills and knowledge acquired by the overall experience of the employee's previous employment. *Reed, Roberts Assocs. v. Strauman*, 40 N.Y.2d 303, 307 (1976) (citation omitted).

Exception to 'Reasonableness' Requirement

New York courts will enforce a non-competition provision regardless of reasonableness if the

"employee choice doctrine" applies. The doctrine applies in the case of voluntary terminations and "where an employer conditions receipt of postemployment benefits upon compliance with a restrictive covenant." *Morris v. Schroder Capital Mgmt. Int'l*, 7 N.Y.3d 616, 620-21 (2006). In such a circumstance, the employee has the choice of accepting the benefits and not working for a competitor or working for a competitor and forfeiting the postemployment benefits. Id. at 621.

Blue-Pencil

New York courts may blue-pencil an over-broad non-competition provision to make it enforceable, but are not required to do so. See *BDO Seidman*, 690 N.Y.S.2d at 860. In certain circumstances, an over-broad non-competition provision will be considered *un*enforceable and not subject to blue-pencil revisions, e.g., if the court finds the employer procured the non-competition agreement through overreach or coercion. See *Brown & Brown v. Johnson*, 12 N.Y.S.3d 606, 611 (3d Dep't 2015).

Drafting

Employers seeking to draft enforceable non-competition provisions must keep in mind how New York courts assess the reasonableness of such provisions. Employers can take steps to enhance the enforceability of non-competition provisions. For example, employers should explicitly identify the "legitimate purpose" for which the provision is necessary; narrowly tailor the provision to serve that purpose; and include an explicit "blue-pencil" provision. Employers should also take other steps to protect their "legitimate interests." For example, if the employer's legitimate interest is protection of trade secrets, the employer should also have the employee sign a strong and enforceable confidentiality provision and take practical steps to guard the trade secrets. This strengthens the employer's argument for enforcing the agreement not to compete, but also protects the employer if the court blue-pencils the non-competition provision or strikes it.

Avoiding Violation

Employers should be mindful that non-competition provisions are routinely included in employment agreements and that it is vital to determine whether potential new hires may be bound by such provisions with their prior employers. Depending on the terms and scope of the provision, an employer might be able to take steps with the new hire to avoid violating the non-competition provision. For example, a prospective employer could place temporary restrictions on a new hire's job duties during the non-competition period, or depending on the circumstances, may put the new hire on immediate garden leave (i.e., paid a salary, but not required to perform any duties) until the non-competition period ends. See, e.g., *Ticor*, 173 F.3d at 71 (holding that the former employer's restrictive covenant was enforceable, but the employee could be hired and immediately put on garden leave by his new employer). Ideally, the employer should seek to obtain from the prospective hire the actual language of the non-competition provision at issue, assuming of course that the prospective hire is not restricted from sharing it.

Statutes and Rules

There is no overall state statute or regulation governing agreements not to compete in New York. However, certain industry-specific statutes and rules do apply. New York Labor Law §202-k prohibits non-competes in the broadcast industry; Rule 5.6 of the New York Rules of Professional Conduct prohibits lawyers from participating in agreements that restrict their right to practice; and FINRA Rules 2140 and 11870 prohibit non-competition agreements that interfere with a customer's request to transfer the customer's account in connection with a registered representative moving from one FINRA member to another.