

# You thought you were protected? Enforceability of noncompetes now and in the future

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JANUARY 20, 2023

Non-compete clauses in employment agreements have been the source of much controversy over the years. Employers want them to protect their human capital and to prevent competitors from stealing their valued employees. Employees dislike them because they prevent mobility of employment. There are good arguments on both sides.

Recently, there have been developments that seem to erode the enforceability of non-competes. This includes a new proposal from the Federal Trade Commission on banning them altogether. As an employer, what do you need to know about the current state of non-compete clauses?

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Here's a hypothetical: You are looking to hire a salesperson, and you find just the right person, John. Your company has a great non-compete agreement that will ensure that when John leaves your employment, he cannot work for a competitor for two years.

To save time on his first day, HR sends an onboarding package to John, asking him to complete the new hire paperwork, including the non-compete agreement, and return it. John signs the non-compete and sends it in. You and John agree that he will start work in two weeks, and John gives notice to his current employer. Perfect, right?

## **Some states won't enforce non-competes unless the person was an employee at signing**

As we all know, non-compete law is state-specific.

At least two states, Alabama and Louisiana, require that a person be an employee when he signs the noncompete or it is not enforceable.

- Alabama's requirement<sup>1</sup> is part of its statute and allows restrictive covenants with employees, which has been read to

require that the person actually be employed when he or she signs a non-compete agreement.

- Louisiana's requirement stems from a recent Fifth Circuit case, *Rouses Enterprises, LLC v. Clapp*<sup>2</sup>. In the Rouses matter, James Clapp signed a non-compete and started work sometime later. The court held that the agreement was not enforceable because he was not an employee at the time of signing.

## **Some states won't enforce non-competes unless the person was given sufficient notice of the non-compete**

Other states have recently taken another approach — requiring potential employees or employees to be given a certain amount of notice concerning a non-compete, such as the following:

- In Colorado, for non-competes entered into on August 10, 2022 or after, the employer must provide notice in a separate document to the potential employee before the individual accepts the employment offer of the non-compete as well as the non-compete's terms. For current employees asked to sign non-competes, the employer must provide notice of the non-compete and the non-compete's terms at least 14 days before the effective date of the non-compete or any additional compensation or other consideration received for signing the non-compete, whichever is earlier.
- In Illinois, for non-competes entered into on January 1, 2022 or after, the employer must provide employees with at least 14 days' notice of the non-compete to make it potentially enforceable. Although it is not 100% clear on whether prospective employees must be provided 14 days' notice as well, a best practice would be for employers to provide potential employees with at least the same 14 days' notice.
- In Oregon, a non-compete is void unless an employer informs the employee at least two-weeks in advance of the non-compete's terms, or the non-compete is entered into upon a subsequent bona fide advancement of the employee by the employer, such as a promotion.

Many other states have other restrictions on non-compete agreements. Some limit them in the time period they can be applied. Others limit the geographic scope of the restriction.

Others, like Colorado and Illinois, say that if you don't pay an employee at least a certain amount of money, then you can't enforce a non-compete against that employee.

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There is significant momentum among some states to add additional requirements like this to try and avoid lower-wage employees being subject to non-compete agreements.

### Federal Trade Commission proposal

On January 5, 2023, the FTC gave notice of a proposed rule that would essentially outlaw non-compete clauses in employment agreements. In a statement by FTC Chair Lina Khan, she noted that in states where non-competes were limited, wages were higher.

The FTC rule would force employers to withdraw any non-compete provisions from existing contracts and to inform their employees that they were no longer under those restrictions. In addition, it would make it illegal for an employer to impose a non-compete obligation as a condition of employment.

This prohibition would not only cover employees, but also independent contractors, volunteers, interns and other workers. The

rule has not yet gone into effect, and it will be interesting to see if employers comment on the rule

### Check the law of your jurisdiction, and sit tight

The moral of the story is that non-competes are tricky and the law can change. In some jurisdictions, such as Alabama and Louisiana, you have to get the employee to sign the agreement on or after employment starts.

This can mean that a non-compete that you get from a terminated individual (as part of a settlement agreement) may not be enforceable. In other states, like Colorado and Illinois, including a non-compete in your standard new-hire packet that an employee signs on their first day is not going to be enforceable if executed after a certain date because the employee was not given sufficient time to review it before execution.

With regard to the FTC proposed rule, it is unclear at this time whether the comment period may provide for some alteration. Even if the current rule goes into effect, you can bet there will be some sort of legal challenge to it. Regardless, the fact that it was proposed and the sweeping nature of the rule shows that this Administration views non-compete agreements as things that should be history.

Check your state law requirements on all aspects of the agreement. You don't want to have a great non-compete that you can't enforce.

### Notes

<sup>1</sup> <http://bit.ly/3CZ3j3L>

<sup>2</sup> *Rouses Enterprises LLC v. Clapp*, No. 21-30293, 2022 WL 686332 (5th Cir. Mar. 8, 2022).

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This article was first published on Westlaw Today on January 20, 2023.