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Ask an Employment Lawyer: Should I Have My Employee Sign a Non-Compete Agreement?

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With employees changing jobs in record numbers, it is now more important than ever for banks to ensure their information, property, and customers remain with them when an employee leaves. Thus, more and more banks have been considering whether they should be utilizing non-compete agreements (and/or other restrictive covenants) to further this goal. At the same time, with each passing year, more and more states have moved toward prohibiting or significantly limiting the use of non-compete agreements in the employment setting.

If you are considering implementing a non-compete requirement—or have agreements that have not been reviewed or updated in a while—here are the top five things you need to know:

Laws Regulating Non-Compete Agreements Are State Specific

Each state has its own laws on whether and in what circumstances non-compete agreements are allowed. For example, in North Dakota, California, Colorado, and Oklahoma, non-compete agreements in the employment context are either largely or entirely unenforceable. Other states, including Illinois, Maine, Maryland, New Hampshire, Rhode Island, Oregon, and Washington, have income-related bans on non-competes. Many of these states (as well as others) also have other restrictions or limitations.

Additionally, there may be different rules that apply when non-competes are a part of a sale of a business.

Finally, the penalty for violating a state's non-compete laws also varies by state. For example, some states impose criminal penalties, while others have attorneys' fees provisions and/or other financial penalties.

Note, on January 5, 2023, Federal Trade Commission (FTC) has also proposed a regulation that would ban non-compete agreements between workers and employers. Many banks, savings and loan institutions, and federal credit unions are outside the jurisdiction of the FTC. Thus, even if the proposed ban is ultimately enacted, it may not apply to your workforce. Nonetheless, employers using or considering non-compete agreements should monitor the proposed ban and consult

with legal counsel on potential applicability.

There Is a Trend Toward Restricting the Use of Non-Compete Agreements

As noted above, more and more states have moved toward restricting or prohibiting non-compete agreements. In just the last few years, 24 states and the District of Columbia have implemented changes to their non-compete laws. Indeed, last year alone, there were 66 non-compete bills introduced in 25 different states. Nearly all these changes tightened and/or imposed additional restrictions on non-compete agreements.

Non-Compete Agreements Require Consideration to Be Valid

Where permitted, a non-compete agreement needs sufficient consideration to be enforceable. This means the employee needs to receive something of value in exchange for his or her agreement not to compete with the bank.

What constitutes sufficient consideration depends on the circumstances, as well as the law in that state. For example, in Wisconsin, employment and good-faith ongoing employment is sufficient consideration for a non-compete agreement. In Minnesota, however, employment is sufficient consideration only if the employee signs the non-compete agreement *before* starting employment. If the agreement is not signed until after employment has started, the employer must give the employee something else of value (such as a raise, promotion, bonus, etc.) in order for the non-compete agreement to be valid. The required amount of that additional consideration depends on the circumstances.

There Is No One-Size Fits All

Where permitted, non-compete agreements are allowed to protect legitimate business interests and must be narrowly tailored to serve that purpose. An overly broad agreement may be struck down as unenforceable.

Thus, in states where non-competes are allowed, many require that the agreement be limited in time, geography, and scope. In other words, there is a limit on how long after employment you can prohibit a former employee from competing. There may also be a limit on how and where you prohibit the employee from competing.

What constitutes a legitimate business interest—and what restrictions are reasonable and necessary to protect that interest—will depend on the circumstances. For example, if you require a loan officer to sign a non-compete agreement to help protect your bank's goodwill and customer relationships, a court may strike down the agreement if it prohibits *any* employment at *any* competitor, even when the position does not involve customer contact.

Ultimately, it is important to understand exactly what the non-compete agreement needs to protect and craft restrictions that directly address that concern—and no more.

Non-Compete Agreements Are One of Many Tools That Can Be Used to Protect Legitimate Business Interests

If allowed and crafted well, a non-compete agreement can be a valuable tool to help protect your business and relationships. Often, they are used in conjunction with other restrictive covenants, such as a non-solicitation and/or confidentiality agreement. A non-solicitation agreement can prevent the employee from soliciting the bank's customers and/or other employees after he or she has left. A confidentiality agreement prohibits the employee from using, disclosing, or misappropriating the bank's (and its customers') confidential information. These agreements can be used together or individually, e.g., if the bank needs a restrictive covenant but cannot—or does not want to—use a non-compete agreement. However, as with non-competes, keep in mind that these other restrictive covenants have their own legal requirements.