D R A F T

FOR DISCUSSION ONLY

Covenants Not to Compete Act

[Tentative new name: Noncompete Agreement Act]

Uniform Law Commission

May 12, 2021 Drafting Committee Video Conference

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May 11, 2021

Covenants Not to Compete Act

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Covenants Not to Compete Act

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Covenants Not to Compete Act

Section 1. Title

This [act] may be cited as the Covenants Not to Compete Act. [Tentative new name: Noncompete Agreement Act.]

Section 2. Definitions

In this [act]:

(1) "Apprentice" means an individual who is in an apprenticeship program registrable under [state or] federal law to learn a skilled occupation.

(2) "Confidentiality agreement" means an agreement that expressly prohibits a worker from disclosing or using information and is not entered into as a condition of settlement or other resolution of an employment dispute.

(3) "Electronic" means relating to technology having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities.

(4) "Employer" means an individual or entity that hires or contracts with a worker.

(5) "Entity":

(A) means:

(i) a business corporation;

(ii) a nonprofit corporation;

(iii) a general partnership, including a limited liability partnership;

(iv) a limited partnership, including a limited liability limited partnership;

(v) a limited liability company;

[(vi) a general cooperative association;]

(vii) a limited cooperative association;

(viii) an unincorporated nonprofit association;

(ix) a statutory trust, business trust, or common-law business trust; or

(x) any other person that has:

(I) a legal existence separate from any interest holder of that person; or

(II) the power to acquire an interest in real property in its own name; and

(B) does not include:

(i) an individual;

(ii) a trust with a predominately donative purpose or charitable trust;

(iii) an association or relationship that is not listed in subparagraph (A) and is not a partnership under the rules stated in Section 3-202(c) or a similar provision of the law of another jurisdiction;

(iv) a decedent's estate; or

(v) a government or governmental subdivision, agency, or instrumentality.

(6) "Intern" means an individual who performs uncompensated service to earn credit awarded by an educational institution, learn a trade or occupation, or gain work experience.

(7) “Less restrictive agreement” means an agreement that limits but does not expressly prohibit, except for a no-business agreement, the worker from some work, including a confidentiality agreement, no-business agreement, no-recruit agreement, nosolicitation agreement, , payment-for-competition agreement, and training-repayment agreement.

(8) “Noncompete agreement” means an agreement that expressly prohibits a worker from some work.

(9) “No-business agreement” means an agreement that expressly prohibits a worker from working for a client or customer of the employer.

(10) “No-recruit agreement” means an agreement that expressly prohibits a worker from hiring or recruiting another worker of the employer.

(11) “Nonsolicitation agreement” means an agreement that expressly prohibits a worker from soliciting a client or customer of the employer.

(12) “Payment-for-competition agreement” means an agreement that by its terms, other than prohibition of some work, or manner of enforcement imposes adverse financial consequences on a worker for work-related activities elsewhere.

(13) “Record” means information:

(A) inscribed on a tangible medium; or

(B) stored in an electronic or other medium and retrievable in perceivable form.

(14) “Restrictive employment agreement” means an agreement, whether alone or part of an agreement between an employer and worker or potential worker, that prohibits or requires an action after the work relationship ends or a sale of business is consummated, including a noncompete agreement and less restrictive agreement.

(15) "Sale of business" means sale or merger of an entity or a subdivision of substantially all of the operating assets or ownership interest of the entity.

(16) "Sign" means, with present intent to authenticate or adopt a record:

(A) execute or adopt a tangible symbol; or

(B) attach to or logically associate with the record an electronic symbol, sound, or process.

(17) "Special training" means instruction, teaching, or other education received by a worker from a source other than the employer that is designed to enhance the ability of the worker to perform the worker's work, is not normally received by other workers, and is a significant and identifiable cost to the employer distinct from ordinary on-the-job training.

(18) "Stated rate of pay" means the definite annual compensation, including wage, salary, professional fee, and other amount received as compensation for personal service actually rendered, including the fair market value of all remuneration paid in any medium other than cash. The term does not include a healthcare benefit, severance pay, retirement benefit, expense reimbursement, amount paid by a person that represents a distribution of earnings and profit rather than as compensation for personal service, or anticipated but indeterminable compensation such as tips, bonuses, and commissions.

(19) "Trade secrets" are as defined by the [cite to Uniform Trade Secrets Act].

(20) "Training-repayment agreement" means an agreement whereby the employer requires a worker to repay the employer for training expenses incurred by the employer.

(21) "Volunteer" means an individual who, of the individual's own free will, provides services without any financial gain.

(22) "Work" means providing service to an employer.

(23) "Worker" means an individual who works. The term includes an employee, independent contractor, partner, intern, volunteer, and apprentice. The term does not include a member of a board of directors or other governing board, investor, or vendor of goods.

Section 3. Scope

(a) This [act] applies to a restrictive employment agreement. To the extent a restrictive employment agreement is part of an agreement, the restrictive employment agreement is subject to this [act], and the rest of the agreement is not affected by this [act].

(b) This [act] supersedes the statutory and common law of a restrictive employment agreement but does not affect:

(1) the common law of contract;

(2) the common law of agency;

(3) any law or regulation that restricts an attorney's ability to enter into a restrictive employment agreement; and

(4) [cite to other state law that prohibits or limits enforceability of a restrictive employment agreement.]

Legislative Note*: The state should identify pre-existing statutes that prohibit or limit the enforceability of a specific type of restrictive employment agreement that are consistent with this [act] and can remain in force. [To the Drafting Committee only: For example, many states, such as Arizona, Connecticut, and Illinois, prohibit the use of noncompete agreements in the broadcasting industry.]*

Section 4. Notice Requirements

A restrictive employment agreement is prohibited and unenforceable unless:

(1) a copy of the proposed agreement is provided in a record to:

(A) a prospective worker before the worker's acceptance of employment or 10 business days before the commencement of employment, whichever is earlier; or

(B) a current worker who receives a material increase in earned income before the worker's acceptance of a change in job status or responsibilities or 10 business days before the increase, whichever is earlier;

(2) in conjunction with a copy of the proposed agreement, the employer:

(A) notifies the worker in a record of the worker's right to consult with an attorney prior to signing the agreement; and

(B) gives the following notice in a record in substantially the following form as prepared by the [Department of Labor]:

Notice Required by the Noncompete Agreement Act

You may be prevented from some future work if you sign this agreement

---

1. Why am I getting this notice?

You are getting this notice because your employer is proposing that you sign an agreement that limits your ability to work after your work relationship ends. The law requires your employer to provide you with this notice, which will help you understand whether your employer may or may not impose these limits.

2. What documents must your employer provide?

Your employer must give you a copy of the proposed agreement as well as a copy of the final signed agreement. You may also request at any time during your employment a copy of the agreement which your employer must give to you within 10 business days of your request. You have 10 business days before starting work to review the agreement. If you decide to start work earlier, or you have already been working for your employer, you have 10 business days after receiving the agreement to review it.

3. Are these agreements prohibited and unenforceable against some workers?

Yes. Most of these agreements will not be enforceable against a physician or other healthcare worker, volunteer, apprentice, intern, worker under 18 years, worker terminated without good cause, or worker earning less than the state's annual mean wage. The annual mean wage can be found at https://www.bls.gov/oes/current/oessrcst.htm by selecting your state, and then looking at the annual mean wage for All Occupations.

4. In what ways will I be restricted from work if I sign the agreement?

Your employer has proposed one or more of the following agreements: noncompete agreement, confidentiality agreement, no-business agreement, no-recruit agreement, nonsolicitation agreement, payment-for-competition agreement, or training-repayment agreement. Your employer will highlight which of the agreements it is proposing. These agreements limit what you can do after your work ends and must be reasonable.

--a noncompete agreement prevents you from working for a competitor for up to 1 year and is only enforceable if your employer has a valid reason for requesting the agreement and it is as limited as possible.

--a confidentiality agreement prevents you from disclosing information and is only valid if it covers nonpublic and business-related information.

--a no-business agreement prevents you from doing any business with certain clients or customers for up to 6 months.

--a no-recruit agreement prevents you from recruiting some of your former co-workers for up to 6 months.

--a nonsolicitation agreement prevents you from reaching out to former clients or customers for up to 1 year.

--a payment-for-competition agreement makes you pay your employer for competition and must be reasonable.

--a training-repayment agreement requires you to repay your employer for specialized training expenses if you leave work within 2 years after the training ends.

5. What options do I have?

You have at least four options:

a. Talk with a lawyer. A lawyer can explain the situation to you and help you decide whether to sign the agreement.

b. Contact the [Department of Labor]. The [Department of Labor] can take action against your employer for having you sign a prohibited agreement.

c. Negotiate with your employer. Even if the agreement is enforceable, you can ask your employer to reduce the limitations in the proposed agreement.

d. Sign the agreement. If the agreement is acceptable, you can sign it.

6. What if I sign an agreement that is prohibited by this law?

If you sign an agreement that is prohibited, the employer cannot use it against you. If your employer takes you to court and you win, your employer may be required to pay for your defense costs and any damage done to you. In some situations, you may also sue your employer;

(3) the proposed agreement and the agreement clearly specify the information, type of work, or competitive activity that is restricted or prohibited after the work relationship ends;

(4) the agreement is in a record separately signed by the worker and an agent of the employer and a copy of the agreement is given to the worker promptly after signing; and

(5) the employer gives a copy of the agreement to the worker within [10] business

days of a worker's request in a record for a copy, unless the employer when acting in good faith is unable to provide the record within [10] business days and the worker is not prejudiced by the delay.

Comment

The separately signed requirement is included for those situations where the restrictive employment agreement is part of a larger work agreement. In this situation, the worker and agent of the employer are specifically required to sign the restrictive employment agreement on its own whether or not they sign the larger work agreement.

Section 5. Worker Not Subject to Restrictive Employment Agreement

A restrictive employment agreement, except for a confidentiality agreement, is prohibited and unenforceable unless:

(1) the worker has, when accepting the restrictive employment agreement and throughout employment, a stated rate of pay greater than the annual mean wage of employees in [State] as determined by [State Department of Labor] [U.S. Department of Labor, Bureau of Labor Statistics];

(2) the worker voluntarily quits without good cause attributable to the employer or is terminated for individual performance-related cause; and

(3) the worker is at least 18 years of age and is not an intern, volunteer, or apprentice when the agreement is signed.

Comment

Paragraph (1) is a core part of the act. It prohibits and makes unenforceable a restrictive employment agreement (other than a confidentiality agreement) unless the worker has an annual rate of pay above the threshold amount. The state annual mean wage has several desirable features for being this threshold figure. First, it automatically adjusts for inflation. Second, the figure is easily accessible. The U.S. Department of Labor Bureau of Labor Statistics tracks this number on a state-by-state basis and updates its database yearly.[1] Thus, even if a state does not collect or publish its own annual wage data, it can refer to an easily accessible federal source. Third, the figure varies by state, reflecting the particular economic status of each state. Fourth,

[1] https://www.bls.gov/oes/current/oessrcst.htm.

the figure is not based on an arbitrary multiple of some other statistics. Fifth, the figure is a core aspect of the labor market rather than tangentially related.

Other possible thresholds lack one or more of these characteristics. For example, a fixed dollar amount does not adjust to inflation and, unless each state separately picks a number, it is not tailored to local labor conditions. A multiple of the minimum wage does not change readily with inflation and requires an arbitrary multiple to be meaningful. A threshold based on the poverty level requires an arbitrary multiple and the base number is not directly related to the labor market.

A major feature of the annual mean wage threshold is that it roughly corresponds to workers whose restrictive covenants would typically be unenforceable on common-law trade-secrets criteria anyway. It thus adds clarity and certainty to the question of enforceability without greatly altering the validity of a restrictive agreement for which the employer has a legitimate interest. Few workers making less than the annual mean wage have meaningful access to trade secrets. In 2020, the annual mean wage nationwide was $56,310, ranging from $41,600 in Mississippi to $70,010 in Massachusetts (with greater ranges in U.S. territories). Workers making more than the annual mean wage typically have a college degree, while those making less than the annual mean wage have less education. Having a college degree, in turn, makes it twice as likely the worker has a trade secret.[2]

While empirical data are somewhat less clear for customer relationships than trade secrets, the annual mean wage threshold likely gives a rough correspondence with an unenforceable interest in customer relationships as well. A worker making less than the average mean wage rarely has enough star power or is engaged in a near-permanent customer relationship such that the customer will follow the worker to a new employer. Higher-paid customer representatives may have such power, and thus the employer is more likely to have a protectable interest in the customer relationships enjoyed by a worker paid more than the annual mean wage.

Paragraph (1) uses "stated rate of pay" (as defined in Section 2(18)) as the figure to compare to the annual mean wage, rather than all earnings or amount earned in the prior year. This figure is used to add clarity at the moment of contracting. Both worker and employer should know the definite amount the worker will be making, based on the rate of pay and the expected hours, and thus should be able to easily determine whether it is more or less than the annual mean wage. Annual earnings, particularly when they depend on commissions, bonuses, or premium pay, would be much less certain at the time of hiring, and thus create ambiguity in

[2] For details see, U.S. Dep't of Treasury Office of Economic Policy, Non-Compete Contracts: Economic Effects and Policy Implications 4, https://www.treasury.gov/resource-center/economic-policy/Documents/UST%20Non-competes%20Report.pdf (Mar. 2016); Elka Torpey, *Education Pays*, U.S. Bureau of Labor Statistics, https://www.bls.gov/careeroutlook/2019/data-on-display/education_pays.htm (Feb. 2019); According to a 2016 Report on Non-Compete Contracts by the Treasury Department, workers with four-year degrees are twice as likely to possess trade secrets as those without four-year degrees. In 2018, the median annual earnings corresponding to educational attainment was approximately as follows: bachelor's degree-$62,000, associate's degree-$45,000, and less than an associate's degree-$40,000 or less. Generally in line with these statistics, the Treasury Department Report also showed that workers earning less than $40,000 possess trade secrets at less than half the rate of their higher-earning counterparts.

enforcement at this critical time in the employment relationship.

This paragraph requires that the stated rate of pay must remain above the annual mean wage throughout the employment relationship, as well as at the initial acceptance of the restrictive agreement. For example, if the stated rate of pay barely exceeds the annual mean wage at acceptance and does not rise as much over the year as the annual mean wage, the restrictive agreement may become prohibited and unenforceable over time.

Section 6. Requirements for Noncompete Agreement

A noncompete agreement is prohibited and unenforceable unless:

(1) the agreement protects one or more of the following legitimate business interests:

(A) the sale of a business in which the worker is a substantial owner and consents to the sale;

(B) the employer's trade secrets; or

(C) the employer's current and ongoing customer relationships;

(2) the agreement, at the time it is entered and through the time of enforcement, is reasonable and narrowly tailored in duration, geographical area, and scope of actual competition to further an interest of paragraph (1), and the interest cannot be substantially protected by a less restrictive agreement; and

(3) the agreement lasts no longer than:

(A) five years when furthering an interest under paragraph (1)(A); or

(B) one year when furthering an interest only under paragraph (1)(B) or (C).

Section 7. Requirements for Less Restrictive Agreement

A less restrictive agreement is prohibited and unenforceable unless the agreement is reasonable. An agreement is not reasonable, if in the case of a:

(1) confidentiality agreement, it prohibits the worker from using or disclosing:

(A) the worker's general training, knowledge, skill, or experience gained on the job or otherwise; or

(B) information that is:

(i) readily accessible to the relevant public; or

(ii) not relevant to the employer's business;

(2) no-business agreement, it extends beyond a current and ongoing client or customer of the employer with whom the worker had personally worked or lasts longer than six months after termination;

(3) no-recruit agreement, it extends beyond a fellow worker currently working for the employer with whom the worker had personally worked or lasts longer than six months after termination;

(4) nonsolicitation agreement, it extends beyond a current and ongoing client or customer of the employer with whom the worker had personally worked or lasts longer than one year after termination;

(5) payment-for-competition agreement, the financial consequence exceeds the actual competitive harm to the employer caused by the worker or lasts longer than one year after termination of employment; and

(6) training-repayment agreement, it requires payment to the employer of greater than the cost of special training, requires repayment for longer than two years after the training is completed, or does not prorate the repayment during the two-year post-training period.

Section 8. Waivable and Nonwaivable Provision

(a) Except as provided in subsection (b), a party to a restrictive employment agreement

may not waive or stipulate to a fact to avoid a requirement of this [act].

(b) A worker may waive the 10-business-day time requirement of Section 4(1)(A) if the worker receives a copy of the proposed agreement before accepting employment. If the worker so waives, the agreement is not enforceable unless the worker subsequently works at least 10 business days for the employer.

Section 9. Enforcement and Remedy

(a) The court may not modify a restrictive employment agreement [that restricts a worker beyond an enumerated maximum duration under this [act]] to make it enforceable. [The court may modify an agreement that otherwise violates this [act] only on a finding that the employer reasonably and in good faith believed the agreement was enforceable under this [act] and only to the minimum restriction necessary to protect the employer's interest and render the agreement enforceable.]

(b) The court may remedy an actual or threatened breach of a valid restrictive employment agreement with injunctive relief, actual damages, legally enforceable liquidated damages specified in the agreement, and costs.

(c) An affected worker or employer, including an employer not a party to the restrictive employment agreement who is considering hiring an affected worker, may seek a declaratory judgment that the agreement is unenforceable.

(d) The court may award injunctive relief, actual and liquidated damages, costs, and reasonable attorney's fees to a private party that successfully challenges or defends against the enforceability of a restrictive employment agreement or demonstrates a violation of this [act].

(e) A party seeking to enforce a restrictive employment agreement has the burden of proof on every element in any proceeding.

(f) An employer that enters a restrictive employment agreement that the employer knows or reasonably should know is unenforceable under this [act] commits a civil violation. The [Attorney General and Department of Labor] may bring an action on behalf of an affected worker, or an affected worker may bring a private action, against an employer to enforce this subsection, for which liquidated damages of not more than $[5,000] per worker per agreement may be adjudged for each violation.

Legislative Note: *The state should specify that the Attorney General or Department of Labor, in bringing an action under section 9(f), has its usual powers to investigate claims and reach conciliation or settlement.*

Section 10. Healthcare Provider

A noncompete agreement, no-business agreement, no-recruitment agreement, or nonsolicitation agreement is prohibited and unenforceable against a physician or other healthcare provider as defined by [state regulation of healthcare providers] when working as a physician or other healthcare provider.

Comment

This section enacts a fundamental policy that patients have the right to choose and to continue treatment with their own healthcare provider. The policy is analogous to the prohibition on noncompetes and restricting lawyers. This section makes the listed agreements unenforceable against a healthcare provider even when ancillary to a sale of business. This is similar to the regulation of the equivalent lawyer agreements, which generally are not enforceable even ancillary to a sale of business. Just as the Rules of Professional Conduct allow for the enforceability of some payment-for-competition agreements against lawyers, however, this section allows for the enforceability of payment-for-competition agreements against a healthcare provider, so long as the agreement meets the other requirements of this [act].

Section 11. Choice of Law and Forum

(a) A choice of law provision in a restrictive employment agreement is prohibited and unenforceable unless it calls for a dispute arising out of the agreement to be governed by the law of the jurisdiction where the worker primarily works or, if the work relationship has ended, the jurisdiction where the worker primarily worked at the time of termination.

(b) A choice of forum provision is prohibited and unenforceable unless it allows the dispute to be decided by a court or arbitrator in a jurisdiction where the worker primarily works or, if the work relationship has ended, a jurisdiction where the worker primarily worked at the time of termination.

(c) Subsection (b) does not apply to a choice of forum provision to the extent that application would conflict with the Federal Arbitration Act, 9 U.S.C. Sections 1 through 307.

Comment

A central purpose of this [act] is to have clear, predictable, and uniform laws govern restrictive employment agreements. If many jurisdictions adopt this uniform act (and courts further the goal expressed in section 12 of applying and construing the act with uniformity in mind), the choice-of-law provision matters less because the law of many jurisdictions will be substantively the same. Until then, each state adopting this act enhances uniformity by insisting that the choice-of-law provision call for the law where the worker works, rather than, for example, the law where the contract was negotiated or signed or where the employer has its principal place of business or incorporation.

This section does not require the parties to have a choice of law or choice of forum provision. Nor does it limit the powers of any court or arbitrator or change a state's general choice of law doctrine. Rather, it focuses on the agreement between employer and worker and declares that the choice-of-law provision, if the parties have made one that applies to a restrictive employment agreement, must choose the law of the state where the worker primarily works. Further, the choice-of-forum provision, if there is one, must allow for (but not necessarily require) the dispute be decided in the state where the worker works.

Sometimes a worker, such as a traveling salesperson, works in several states at the same time. Here, the primary place of work supplies the governing law. Additionally, a worker may move between states over time while working for the same employer. If the choice-of-law provision calls for the primary place where the worker works when the dispute occurs, then the governing law changes as the worker changes jurisdictions. However, if the provision calls for a specific state, which the parties may have anticipated as the primary place of work, and the worker moves, the choice-of-law provision is no longer enforceable.

Subsection (b) does not insist on a single forum in a choice-of-forum provision, but does require that the provision allow the dispute to be handled by a court or arbitrator in the state where the worker primarily works or worked at the time of termination. In that sense, subsection (b) calls for a nonexclusive forum selection provision but does not require an exclusive forum selection provision in the jurisdiction of work. The parties can still agree, at the time of initial contracting or later, to use a different forum, as long as the jurisdiction where the worker primarily works or worded remains an option.

Section 12. Uniformity of Application and Construction

In applying and construing this uniform act, a court shall consider the promotion of uniformity of the law among jurisdictions that enact it.

Section 13. Relation to Electronic Signatures in Global and National Commerce Act

This [act] modifies, limits, or supersedes the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. Section 7001 et seq.[, as amended], but does not modify, limit, or supersede 15 U.S.C. Section 7001(c), or authorize electronic delivery of any of the notices described in 15 U.S.C. Section 7003(b).

Legislative Note: *It is the intent of this act to incorporate future amendments to the cited federal law. A state in which the constitution or other law does not permit incorporation of future amendments when a federal statute is incorporated into state law should omit the phrase "as amended". A state in which, in the absence of a legislative declaration, future amendments are incorporated into state law also should omit the phrase.*

Section 14. Saving Provision

Sections 4(5) and 5 of this [act] apply to a restrictive employment agreement regardless of the date in which it was entered. The other provisions of this [act] do not affect the validity of an agreement in effect before [the effective date of this [act]].

[Section 15. Severability

If a provision of this [act] or its application to a worker or employer is held invalid, the invalidity does not affect another provision or application that can be given effect without the invalid provision.]

Legislative Note: *Include this section only if the state lacks a general severability statute or a decision by the highest court of the state adopting a general rule of severability.*

Section 16. Repeals; Conforming Amendments

(a) . . .

(b) . . .

Legislative Note: *The state should examine its statutes to determine whether conforming revisions are required by provisions of this act relating to { }. See Section { }.*

Section 17. Effective Date

This [act] takes effect . . .