

NON-COMPETITION AND NON-SOLICITATION PROVISIONS

Issues in Drafting/Negotiation and Enforcement



McMahon,
Welch AND
Learned, PLLC

About the Firm

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McMahon, Welch and Learned, PLLC represents many small and mid-sized federal services contractors in Northern Virginia, DC and Maryland, including small-disadvantaged firms, veteran-owned firms, women-owned firms and Hub Zone qualified firms. We also have a strong corporate and acquisitions-support practice which focuses on general business legal matters of significant interest to the broader business community.

Presenters

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William T. Welch, Partner

Mr. Welch has twenty years of experience providing legal counsel for the entire lifecycle of a government contractor from contract negotiation, award, and protests to contract administration and contract claims. Mr. Welch also has experience in teaming agreements, subcontractor agreements, and related issues. In addition, Mr. Welch advises contractors who qualify for small business set-aside awards, 8(a) competitive and non-competitive contracts, and HUBZone and Service-Disabled, Veteran Owned contracts.

Presenters

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Kevin R. Learned, Partner

Mr. Learned's practice focuses on advising clients on general corporate and securities matters, including company formation and governance, buy-sell agreements, operating and stockholder agreements, mergers and acquisitions, private offerings of debt and equity securities (including friends and family, angel, venture capital and private equity investments), corporate divorces and other reorganizations, joint ventures, small business certifications (including 8(a), SDVO, WOSB, HUB Zone and MBE/DBE certifications), executive employment and equity matters, deferred compensation plans, franchise agreements, trademarks, and other commercial contracts and agreements.

Moderator

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J. Patrick McMahan, Partner

Mr. McMahan has nearly thirty years of experience with a primary focus on representation of companies that offer information technology products and services to the federal government. Mr. McMahan advises corporations and other business entities in connection with all aspects of their federal procurement business including contract award and terminations, claims, contract disputes, bid protests, and prime contractor/subcontractor relationships.

Non-Competition and Non-Solicitation Provisions

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Standard Restrictive Covenants

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- Non-solicitation of a company's employees and other service providers
- Non-solicitation of a company's customers and prospective customers
- Non-competition with a company's business

Non-Solicitation of Employees and Other Service Providers

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- Employees vs. Consultants vs. Vendors
- Current and Former
- Non-solicitation vs. Non-hire
- General Advertising Exception

Non-Solicitation of Customers and Prospective Customers

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- Current and Former
- Prospective Customers
 - Direct contact
 - Active plans
- Customers with Involvement
- Who is the Customer?
 - Agencies and Sub-Agencies

Non-Competition

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- What is the Business?
- Current vs. Future Plans
- Competition vs. Exclusivity

Contexts

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- Sale of a Business
- Employment/Consulting Relationship
- Teaming/Subcontract Relationship

Sale of a Business

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- You are selling the goodwill of the business, which includes the business's relationship with its employees and service providers, as well as its customers and prospective customers
- Courts are much more likely to enforce restrictive covenants as part of the sale of a business
- Often long in term and broad in scope
- Often combined with employment-focused restrictions

Employment/Consulting Relationship

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- Courts are likely to enforce non-solicitation provisions if narrowly focused
- Courts are less likely to enforce non-competition provisions if the employee is prohibited from earning a living
- Often short in term (2 years maximum in most states) and narrow in scope

Teaming/Subcontract Relationship

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- Courts are likely to enforce non-solicitation provisions if narrowly focused
- Courts may enforce non-solicitation provisions when the client is the government
 - Recent decision in Virginia
 - But, see 48 C.F.R. 52.203-6 – Restrictions on Subcontractor Sales to the Government
- Often short in term and narrow in scope
 - Limited to specific contractual relationship
- Courts may enforce non-compete provisions
 - No definitive high court ruling on point

Policy Consideration

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- Balancing legitimate business interests of a company versus ability of person to earn a living
 - Are the restrictions reasonable?
 - Duration / Geography / Scope
 - Considered together, but over-breadth of one aspect can invalidate the entire provision
 - Janitor exception
 - Look at both perspectives
- Antitrust and other public policy concerns

Enforceability and Forum Selection

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- Enforcement varies from state to state
 - In California, non-competes are not enforceable at all in the employment/consulting context
- Continued employment as adequate consideration
- Blue pencil and non-Blue pencil states
 - Maryland vs. Virginia
- You can choose your state of enforcement
 - *Western Industries-North, LLP v. Lessard, et al.*, 2012 U.S. Dist. LEXIS 33683
 - Virginia Court honored choice of law provision for New Jersey, which allows blue penciling
 - But, see *Arkley v. Aon Risk Services Companies, Inc.*, (Case No. 2:12-cv-01966-DSF-RZ) (C.D. Cal.)
 - California Court did not honor choice of law provision for Illinois, which would have enforced a non-compete provision

Drafting Notes

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- Less is more – make provisions as narrow as possible
 - Increase chance of enforceability
 - Limit confusion as to scope
- Tailor provisions to specific context
 - Negotiated provisions more likely to be enforced
 - Ensure provisions are not punitive
 - But don't tailor too much
 - Should not vary based on reason for termination
 - Avoid liquidated damages

Drafting Notes

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- Severability
 - Make sure each provision is its own separate paragraph
- Extend duration during breach
- Provide for specific performance and injunctive relief
- Require individual to inform potential employers of the restrictive covenants
- Include confidentiality provisions

Strategies in Enforcement

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- Act quickly if violations suspected
 - ▣ Consider seeking a court order
- Identify and protect computers or other memory devices
- Review and protect all email or other means of stored communications

Strategies in Enforcement (Go After the Third Party)

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- Present evidence of the agreement to third party and intent to seek a court order
- Consider claim for tortious interference against third party and/or business conspiracy
 - Could carry punitive damages
- Consider action under the State or Federal Trade Secrets Act
- Consider relying on confidentiality provisions

Strategies in Defense

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- Consider not hiring the individual
 - ▣ Place the individual in a non-offensive position
- Make a business decision whether to challenge enforceability
- Consider filing a declaratory action to challenge enforceability
- Consider providing individual with separate counsel

Strategies in Defense

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- Negotiate a resolution
 - ▣ Restrict individual's duties
 - ▣ Pay a settlement amount to the company
- Ensure individual is not holding proprietary information
 - ▣ Make arrangements to return immediately
- Consider dragging out the matter
 - ▣ Allow cooler heads to prevail

Recent Case Studies

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- *Preferred Sys. Solutions, Inc. v. GP Consulting, LLC*, 284 Va. 382, 2012 Va. LEXIS 160 (Sept 14, 2012)
- *Home Paramount Pest Control Cos. v. Shaffer*, 282 Va. 412, 718 S.E.2d 762 (2011)

Questions?

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