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Client Alert

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Change in Georgia's Law on Restrictive Covenants Headed for November Ballot

The competitive landscape, and decades of judge-made law about non-compete, non-solicit and non-disclosure agreements, may drastically change after this November's election. On the ballot—following the final necessary vote at the close of this year's session of the Georgia Senate—will be a constitutional referendum that, if approved, will enable and trigger the effective date of this change.

Currently Georgia is one of the most difficult states in which to restrict competitive activity by former employees. The principle is written into our state constitution: any restraint on trade—and these kinds of contracts are considered restraints—are against our public policy. Taking this pro-competition public policy as a point of departure, Georgia's courts crafted a vast and sometimes difficult-to-reconcile body of cases about what is and is not enforceable. Courts are hesitant to enforce all but the most limited non-competes and non-solicits. Frequently, what companies thought were carefully-drafted agreements come before trial courts on motions to enjoin employees and are then struck down as unenforceable.

Faced with this challenge, the General Assembly proposes to exempt agreements that are consistent with the new law (House Bill 173) from the kinds of contracts that are illegal and void against public policy. Freely negotiated employment agreements designed to protect trade secrets, confidential information and customer relationships would no longer be categorized with "contracts tending to corrupt the legislation or the judiciary" or, perhaps more common "wagering contracts."

If approved by the voters, the new law will replaces the rigid "geographic scope" test, thereby modernizing restrictive covenant enforcement. Instead of trying to define an employee's territory based on where the employee physically has done business for the employer, the new law permits a court to accommodate not just geography, but the area where activities are actually conducted. House Bill 173 alternatively allows employers to simply list prohibited competitors instead of a prohibited geographic territory. Thus, employers and employees have more flexibility in negotiating what kinds of post-employment conduct is prohibited, and the employer does not have to worry about constantly having to update the agreement as the business relationship between the parties changes over time. At the same time, the employee is afforded more certainty in the protections negotiated in the event that the agreement has to be enforced.

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The proposed definition of "employee" in the new law would extend only to executives, persons with true access to confidential information (such as research and development personnel) and persons with specifically sensitive customer information that is generated from the employee's tenure with the employer—not every employee. In other words, House Bill 173 is targeted precisely to protect the entrusting of competitively sensitive information by the employer to the employee in exchange for the compensation and benefits attendant to the job.

Moreover, even defined "employees" subject to the new presumptions in favor of restrictive covenant agreements drafted in accordance with House Bill 173 have the legal ability to challenge particular agreements as being overbroad in fact. Unlike the current state of the law where agreements are "good" or "bad" as written and cannot be modified to balance competing interests, the new law gives the courts the ultimate ability to "blue pencil" or "modify" arguably overbroad agreements. Thus, the courts still serve as a check against an employer who has reached too far in fact, but the courts now have to account for the concerns of business as well in evaluating the scope of the restriction sought to be imposed by the employer. At present, lacking the ability to "blue pencil," courts can only invalidate a restrictive covenant that may reach just beyond what is reasonable.

Businesses drafting restrictive covenants, and the professionals assisting them, will find additional certainty in the bill. For all kinds of prospective restrictive covenants, the Georgia Assembly included presumptions as to the duration of covenants. For covenants provided in the employment context, House Bill 173 states that a period of up to two years is presumptively reasonable. For covenants executed in other situations, the length of the permissible restriction may increase, e.g., for up to three years in a franchise or licensing context and up to five years when covenants are provided in connection with the sale of a business.

If approved by in November, the new law will apply prospectively, that is, to agreements entered after the effective date of HB 173. To read the text of Georgia House Bill 173, please click here.[1] To read some further discussion of its implications, please click here.[2]

1 http://www.legis.ga.gov/legis/2009_10/versions/hb173_HB_173_AP_7.htm
2 http://www.agg.com/media/interior/publications/AGG_White_Paper-Georgia_House_Bill_173.pdf