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Are Non-Compete Agreements Right for Your Construction Company?

Non-compete agreements, or non-competition agreements, are contracts into which an employer and an employee enter that restricts the work the employee can perform for another company when the employee's tenure at the employer company ends. Typically, it's illegal to intentionally restrain trade; however, some states allow employers and employees to voluntarily enter into agreements with future employment restrictions. Contractors have several reasons to require that their high-level employees (e.g., C-Level) enter non-compete agreements.

While these contracts are often used to protect trade secrets or unique software, valid and enforceable non-compete agreements are also a powerful employee retention tool. Given the current labor shortage, ensuring qualified field employees do not leave your company for the competition is more critical than ever. Protecting positions such as PMs, estimators, or field superintendents with a non-compete agreement can help retain experienced employees, thereby maintaining your company's ability to perform.

However, it is important to consider whether non-compete agreements are the best means for your company to achieve this goal, so be sure to define what your company is trying to protect. Think beyond the common assumption that non-compete agreements are required as a matter of policy: Does your construction company have actual trade secrets that it needs to protect? Does your company have unique, proprietary software that could jeopardize the company's ability to out-bid competition if disclosed?

If you've determined the need for a non-compete agreement, then it's important to understand how it works, the costs of drafting the agreement, the manner and the costs of enforcement, and the potential benefit or negative impact on your company and its employees.

Know Your Jurisdiction

To determine if such an agreement would be a good fit, start with some basic legal considerations. From the outset, you'll need to know whether or not your company operates in a

jurisdiction that favors or even allows non-compete agreements. Some states like California do not allow the enforcement of non-compete agreements.¹ Other states like Florida have very distinct statutes defining the circumstances under which a company can restrict the future employment of one of its employees.²

Also in some states like Florida, the length and type of restriction varies depending on the seniority of the employee subject to the non-compete agreement and the exposure of the departing employee to company-sensitive materials or to trade secrets. Other states view non-compete agreements on a case-by-case basis.

Costs of a Non-Compete Agreement

Sometimes your company can have difficulty ascertaining the costs associated with initiating and enforcing non-compete agreements. However, it's important not to disregard this step. Your company's concerted attention is required when evaluating whether it makes sense to require non-compete agreements for certain employees.

Drafting the Contract

The initial drafting and enforcing of the document each have their own procedures and associated costs. A non-compete agreement is a legal contract and should involve the expertise of an attorney. A non-compete agreement can exist within an employment contract or as a separate non-compete contract. Some states require that an employee actually works at the company at the time the non-compete agreement is executed, so the timing of the agreement is crucial.

Your attorney should ensure that the non-compete agreement is valid in the jurisdiction in which you seek enforcement, and that the company takes all of the required steps in order to best pursue its remedies in the event of the employee's breach of the agreement. Presuming that the agreement is valid, there is a cost associated with your counsel's drafting and annual review of an agreement that is appropriate not only for your company, but also for the particular situation that complies with any existing statutes or the case law in your jurisdiction.

Although the costs might vary depending on the amount of time it takes to draft the contracts, they are typically manageable and easily budgeted for upfront. Of greater concern are the potential costs associated with the required enforcement of a non-compete agreement, which are more difficult to assess.

Enforcing the Contract

Non-compete agreements are not self-executing. If an employee leaves your company to take a job with a competitor (seemingly in direct violation of his non-compete agreement), then your company must take action to enforce its contractual rights.

Usually, the first step is a letter from counsel to both the departed employee and the new company requesting that the parties “cease and desist” the new employment, along with a copy of the executed non-compete agreement to the cease and desist letter. If the contractual language of the non-compete agreement allows, then the letter should state that the departed employee will have to pay the former employer (your company) the fees and costs associated with any further legal action that results in enforcement of the agreement.

In most circumstances, this letter will also inform the current employer that if the employment continues to violate the non-compete agreement, then the current employer will be included in any legal proceedings that result from its intentional and tortious interference with the non-compete contract.

Sometimes those letters are enough to either stop the employment or initiate negotiations for how to avoid further legal action (typically in the form of payment to your company). However, if the current employer and the departed employee challenge the agreement, enforcement proceedings will take place as set forth in the non-compete agreement.

If the agreement does not include the venue or the choice of law (i.e., which state’s law to use – commonly the home state of the employer), then the enforcement action is almost always filed in the state courts of the jurisdiction where the departed employee resides. However, if you and your counsel prefer to resolve disputes in arbitration, be sure to express this in the non-compete. At this point, the costs are almost impossible to predict.

The enforcement process begins with a complaint and a motion for issuance of an injunction to keep the employee from working with the new employer. If the court requires a hearing on this issue, it will take place at a time when the court is available to facilitate such a hearing. Some matters proceed quickly; others can occur months after the initial court filing.

If the court holds a hearing and enters the requested injunction, then the prevailing party must post an injunction bond. The court can set a bond as high or low as it deems reasonable given the facts in a particular case.

In many instances, these hearings involve few witnesses and are resolved relatively quickly. In other circumstances, hearings can take days or even weeks of court time, and the costs can easily outpace your company’s anticipated legal budget. And unlike many construction defect matters that have associated insurance coverage, action to enforce a non-compete agreement is a cost that the company bears.

As mentioned previously, the agreement should typically include prevailing party legal fees and costs in the event that enforcement of a contractual breach requires legal proceedings. However, this doesn’t necessarily mean that the employee may not have the means to reimburse your company for these fees and costs. If you win, you may end up with a large judgment against the former employee, but it does not always translate into a return of your company’s investment. This is especially true if the departed employee either lacks the funds to pay back your company or takes other legal tactics to avoid paying the judgment (e.g., restructuring assets or declaring bankruptcy).

In addition, even if you prevail against the new employer, there is no reason for that company to reimburse your company’s legal fees and costs if it is not contractually obligated to do so.

Benefits & Risks

The benefits of a carefully drafted and enforced non-compete agreement are clear. First, the knowledge that an employee has executed a non-compete agreement is often enough for that employee not to explore opportunities with competitors. In addition, if a departed employee becomes involved in a lawsuit or loses his or her job due to a non-compete agreement, then your current employees may reconsider moving to a competitor upon learning of the repercussions.

However, non-compete agreements can have a potentially negative impact on your company’s culture. Will a non-compete agreement make employees feel “trapped” or “forced” to stay? Or does your company treat its employees in a way that eliminates any incentive for a key employee to leave?

Some companies prefer to have non-compete agreements and enforce them at every instance. While this can improve retention, it doesn’t always improve morale or motivate a company’s key employees. Some companies prefer to incentivize employees so that few reasons exist for valuable employees to leave the company for the competition.



And, keep in mind that each of these approaches has an associated cost to consider when weighing your options. Defining or understanding your company's culture as well as the costs to incentivize will help aid in the decision of enforcing a non-compete.

Finally, you must address whether your company has not only the financial capability, but also the emotional stamina to endure litigation to enforce your non-compete agreements. While a letter from your counsel can usually persuade a new employer to terminate or agree not to employ a departing employee subject to a non-compete agreement, some companies will pursue litigation.

Some new employers will cover all litigation expenses for the departed employee in order to acquire him or her. If the new company has significant financial assets and drives up litigation expenses, can your company go toe-to-toe in a prolonged legal battle?

Conclusion

If the benefits of a non-compete agreement outweigh the possible morale risks and potential enforcement costs, then it's time to take the next step. Find counsel experienced in

this area of the law to help you draft a non-compete agreement that addresses your company's needs and complies with jurisdictional laws, and remember to schedule annual reviews to ensure that the agreements remain compliant with any changes in the law. ■

Endnotes

1. Section 16600 of the California Business and Professions Code.
2. Florida Stat. Section 542.335.

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