DELAWARE
EMPLOYMENT LAW LETTER
Part of your Delaware Employment Law Service

William W. Bowser, Editor; Scott A. Holt and Adria B. Martinelli, Associate Editor
Young, Conaway, Stargatt & Taylor, LLP

Vol. 17, No. 2
February 2012

COVENANT NOT TO COMPETE

Less is more: Delaware courts crack down on expansive noncompetes

by Lauren E. Moak

The Delaware Court of Chancery has indicated that it is reconsidering a long-accepted policy called the blue-pencil rule, under which a court may modify a contract to address issues of fundamental fairness. Traditionally, the rule has been used in Delaware to restrict overly broad postemployment restrictions in employment contracts. Now, however, two judges on the court have stated that they are unlikely to modify a contract under those circumstances. The statement marks a significant change in Delaware law.

Two too many problems for employers

In March 2011, Vice Chancellor J. Travis Laster issued an opinion in a case involving an employee who knowingly violated the noncompetition and nonsolicitation provisions of his employment agreement. Under the terms of the agreement, he was prohibited from (1) competing with his former employer and (2) soliciting his former employer's customers for a period of 36 months following termination of his employment. The contract required the court to apply Maryland law.

Because the employee admitted engaging in conduct that violated the terms of the agreement, the only question before the court was whether the noncompete and nonsolicitation provisions of the contract were overly broad and therefore unenforceable. The court determined that a 36-month restriction was too long, so it had to decide whether it should remove or merely modify the offending provisions.

The court concluded that under the blue-pencil rule, Maryland law requires

modification. However, the court stated it would have handled the question differently under Delaware law. In particular, the court noted that modification under the blue-pencil rule "puts the employer in a no-lose situation." Simply put, if an agreement will be enforced to a lesser extent even if it's overly broad, an employer has no incentive to draft a reasonable provision in the first place. *Delaware Elevator, Inc. v. Williams,* C.A. No. 5596-VCL, March 16, 2011.

Different case, same outcome

During oral arguments in December 2011, Vice Chancellor John W. Noble echoed Laster's position, noting that he was reluctant to modify an overly broad 36-month postemployment restriction against competition and solicitation of a former employer's customers. The court recognized that "there is something of a divergence of opinion on that topic" between the court of chancery and the Delaware Supreme Court. Nevertheless, it indicated its intent to interpret the contract as written without modification. Thus, if the 36-month restriction was found to be unreasonable, the entire provision would be struck from the contract as unenforceable rather than be modified.

Both of these cases are significant because the employees involved were accused of real and intentional malfeasance with respect to their former employers. In other words, an objective onlooker would expect the court to be offended by the employees' conduct and hold them to their agreements. Despite those issues, the court of chancery has still expressed its reluctance to modify unreasonably broad postemployment restrictions. Moreover, the employee in this case was the president of the company and had an attorney during the negotiation of the contract. That fact did little to affect the court's position. *Chesapeake Insurance Advisors, Inc. v. Williams Insurance Agency, Inc., et al.,* C.A. No. 7126-VCN, December 29, 2011.

Bottom line

Given the warning statements from the Delaware court most often tasked with reviewing restrictive covenants, you should take the opportunity to consider whether your employment contracts contain enforceable postemployment restrictions. Among the issues to consider in determining a restriction's enforceability are:

1. the employee's relative position within the company;
2. the extent of the employee's business-related con- tacts;
3. the employee's establishment within the field of business and the surrounding community;
4. the realistic possibility of relocating or working outside the geographic area covered by the postemployment restriction; and
5. the overall length of the restriction.

If your company imposes postemployment restrictions on key employees, it may be time to consider getting counsel's review. Boilerplate clauses often don't take into account the recent nuances of the law discussed in this article.

DELAWARE EMPLOYMENT LAW LETTER does not attempt to offer solutions to individual problems but rather to provide information about current developments in Delaware employment law. Questions about individual problems should be addressed to the employment law attorney of your choice.