Drafting Enforceable Noncompetition Agreements in Illinois

Though Illinois courts are unfriendly to post-employment noncompetition agreements, you can increase the odds that your employer-client's noncompete will pass judicial muster in a challenging legal environment. Here's how.

By Peter A. Steinmeyer

To protect their human capital, employers increasingly require employees to sign post-employment noncompetition agreements, even though many states, including Illinois, are unfriendly to such agreements. With careful drafting, however, even Illinois employers can have enforceable noncompetition agreements that meet their needs, if not their wants.

Noncompetition agreements stem from a variety of motives. Some are recognized by Illinois courts as legitimate (e.g., protection of trade secrets and "near permanent" client relationships), while others are not (e.g., limiting competition).

Although a desire to stifle competition is understandable, a noncompetition agreement that goes too far may be deemed unenforceable – even if it contains a contractual clause authorizing the court to modify the agreement as needed to render it enforceable. Accordingly, the preparation of any noncompetition agreement should begin with a realistic assessment of what restrictions are likely to be enforced by a court and what protections are really needed.

Legitimate, protectible interests – trade secrets, near-permanent relationships

Generally speaking, there are two situations in which an Illinois employer

Peter A. Steinmeyer is a member of the Chicago office of Epstein Becker & Green, PC, where he concentrates on employment litigation and advising clients about employment issues. He is co-chair of the firm's Non-Competes, Unfair Competition and Trade Secrets Practice Group.

will be found to have a legitimate, protectible interest sufficient to justify a post-employment covenant not to compete:

> [W]here, by the nature of the business, an employer has a near-permanent relationship with its customers and, but for his association with his employer, an employee would have had no contact with them; or where the former employee learns trade secrets or acquires other confidential information during his employment and subsequently attempts to use it for his own benefit.[1]

Illinois courts apply one of two alternative tests when determining whether an employer has a "near permanent relationship" with its customers. Some courts apply a "nature of the business" test, while others apply a seven-factor, objective test.[2]

Under the "nature of the business test," a court looks to the nature of the employer's business to determine whether its client relationships are near permanent.[3] A near-permanent relationship with clients is deemed "inherent in the provision of professional services."[4]

In contrast, "a near permanent relationship is generally absent where the nature of the plaintiff's business does not engender customer loyalty by providing a unique product or personal service and customers utilize many suppliers simultaneously to meet their needs."[5] Thus, "a near permanent relationship with customers is generally absent from businesses engaged in sales."[6]

Meanwhile, the objective seven-factor test for "near permanent customer relationships" has been summarized as follows:

> To determine whether an employer has a near-permanent relationship with its customers, Illinois courts consider the following factors: "(1) the length of time required to develop the clientele; (2) the amount of money invested to acquire clients; (3) the degree of difficulty in acquiring clients; (4) the extent of personal customer contact by the employee; (5) the extent of the employer's knowledge of its clients; (6) the duration of the customer's association with the employer; and (7)

Some employer motives – like protecting trade secrets and "near-permanent" client relationships – are protectible, while others – like limiting competition – are not.

1. *Arpac Corp v Murray*, 226 Ill App 3d 65, 72-73, 589 NE2d 640, 647 (1st D 1992).
2. *Lawrence and Allen, Inc v Cambridge Human Resource Group, Inc*, 292 Ill App 3d 131, 142, 685 NE2d 434, 443 (2d D 1997).
3. Id.
4. Id.
5. Id at 142, 685 NE2d at 444.
6. Id.

the continuity of the employer-customer relationships."[7]

Given the practical difficulty of establishing "near-permanent customer relationships," most employers seeking to enforce a post-employment, noncompetition agreement will need to establish that a former employee learned trade secrets or acquired other confidential information during his employment and subsequently attempted to use it for his own benefit.

Employers should be realistic about the duration of the agreement. One year will likely pass muster. Three years might not.

Bolstering the claim to a protectible interest

Whether an employer has a protectible interest is a factual inquiry. Still, it's a good idea to recite in the agreement what it is intended to protect (to include, e.g., an acknowledgement by the employee that by virtue of his employment he has obtained, or will obtain, access to confidential information and/or trade secrets of the employer, in addition to special knowledge and familiarity with the needs and requirements of the employer's customers).[8]

Improving the odds the agreement will be enforced

Under Illinois law, once a protectible interest is established, irreparable injury for purposes of injunctive relief "is presumed to follow if the interest is not protected."[9] Indeed, the mere fact of ongoing competition is enough for injunctive relief, and it is not necessary to prove "any customer defection and monetary loss."[10]

Nevertheless, when deciding whether to issue injunctive relief, a court will also look to whether the restriction on competition is "reasonable" – an inquiry that will entail examination of the "hardship to the employee, its effect upon the general public, and the reasonableness of the time, territory, and activity restrictions."[11]

There are several practical steps you can take to improve the odds that a court will enforce a noncompetition agreement.

First, because Illinois law is, in the words of seventh circuit Judge Richard A. Posner, "hostile to covenants not to compete found in employment contracts,"[12] think about including a choice of law provision specifying the law of a state *other than Illinois*. While there is a risk that an Illinois court would not enforce such a provision, it's worth considering if there is a legitimate relationship between the parties and the designated state (e.g., where the employer maintains its headquarters in the designated state).

Second, any restriction on a former employee's activities should be no broader than necessary. If an employer does not do business in Alaska, it should not prohibit a former employee from working there. Likewise, "Courts are hesitant to enforce prohibitions against employees servicing not only customers with whom they had direct contact, but also customers they never solicited or had contact with."[13]

Third, employers should be realistic about the duration of the agreement. One year will likely pass muster; three years might not.

Fourth, because a covenant not to solicit customers will be subject to lesser judicial scrutiny than a covenant not to work for any competitor, employers should consider separate "nonsolicitation" and "noncompetition" clauses with different durations (e.g., a 12-month customer solicitation ban, but only a six-month ban on working for a competitor).[14]

Fifth, every noncompetition agreement should include a severability clause providing that the invalidity of one provision shall not affect the validity of any other.

Finally, every noncompetition agreement should include a "blue pencil" provision requesting a reviewing court to revise an otherwise overbroad restriction to make it as restrictive as possible under applicable law. Such provisions are enforceable under Illinois law, unless the original agreement was so unreasonable as to be unfair.[15] For purposes of this analysis, "[a] restrictive covenant is unfair where its terms 'clearly extend far beyond those necessary to the protection of any legitimate interest' of the employer or, in other words, amount to 'unrealistic boundaries in time and space.'"[16]

Trade-secret, anti-raiding provisions

Although Illinois law is unfriendly to noncompetition agreements, it is very protective of an employer's trade secrets and confidential information. Disclosure is viewed no differently than other theft of employer property.[17]

Accordingly, every noncompetition agreement should also include a provision requiring the return, at termination, of all employer property and information (in any and all forms, including electronically stored information), and a *permanent* prohibition on the use or disclosure of employer trade secrets or other confidential information, as defined in the agreement.[18]

Similarly, Illinois employers have a protectible interest in maintaining a stable workforce, which justifies restrictions on a former employee's ability to recruit former co-workers.[19] Accordingly, every noncompetition agreement also should include an "anti-raiding" clause with a

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7. *Hanchett Paper Co v Melchiorre*, 341 Ill App 3d 345, 352, 792 NE2d 395, 401 (2d D 2003), quoting *Audio Properties, Inc v Kovach*, 275 Ill App 3d 145, 148-49, 655 NE2d 1034, 1037 (1st D 1995).
8. See, e.g., *Arpac* at 77, 589 NE2d at 650.
9. *McRand, Inc v van Beelen*, 138 Ill App 3d 1045, 1054, 486 NE2d 1306, 1313 (1st D 1985).
10. *Armour & Company v United American Food Processors, Inc*, 37 Ill App 3d 132, 137, 345 NE2d 795, 799 (1st D 1976).
11. *Lawrence and Allen* at 138, 685 NE2d at 441.
12. *Outsource International, Inc v Barton*, 192 F3d 662, 669 (7th Cir 1999) (Posner dissenting).
13. *Lawrence and Allen* at 138, 685 NE2d at 441. See also *Morrison Metalweld Process Corp v Valent*, 97 Ill App 3d 373, 379-380, 422 NE2d 1034, 1039 (1st D 1981) (enforcing two-year restriction barring defendant from doing business with the specific customers with whom he came in contact while employed by plaintiff, regardless of their geographic location); and *McRand* at 1057, 486 NE2d at 1315 (holding that "no undue hardship will be suffered by defendants" because they "are only restricted from selling to certain McRand customers"; "the rest of the field remains open to them for competition with McRand").
14. *Lawrence and Allen* at 139, 685 NE2d at 442.
15. *Eichmann v National Hosp and Health Care Services, Inc*, 308 Ill App 3d 337, 347, 719 NE2d 1141, 1149 (1st D 1999); *Kempner Mobile Electronics, Inc v Southwestern Bell Mobile Systems, LLC*, No 02 C 5403, 2003 WL 1057929 at * 19 (ND Ill 2003).
16. *Eichmann* at 347, 719 NE2d at 1149, quoting *House of Vision, Inc v Hiyane*, 37 Ill 2d 32, 39, 225 NE2d 21, 25 (1967). (This is yet another reason to narrowly draft a non-competition agreement at the outset!).
17. See *Illinois Trade Secrets Act*, 765 ILCS 1065/1 et seq.

time duration consistent with the underlying noncompetition provisions.

Overbroad noncompete as deterrent

One school of thought is that a broadly drafted noncompete, while unlikely to be enforced, will make current employees (and their future employers) think twice before violating the agreement. There is undoubtedly some merit to this view. However, if an employer hopes actually to enforce a noncompetition agreement, it should err on the side of narrow drafting.

Conclusion

The bottom-line in Illinois is that no matter how carefully you draft a noncompetition agreement, it might not be enforceable – even with a blue-pencil provision. However, by focusing narrowly on your employer's needs and not creating an overbroad agreement, you can significantly improve the odds that it will stand up in court. ■

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18. The need to protect trade secrets may also allow an employer to seek an injunction barring a former employee from working in certain positions in which he would inevitably use or disclose the prior employer's trade secrets. See 765 ILCS 1065/3; *PepsiCo, Inc v Redmond*, 54 F3d 1262, 1267 (7th Cir 1995). Indeed, in litigation intended to restrict the activities of a former employee, the battle is frequently won, lost, or settled based on issues related to trade secrets. Accordingly, when contemplating enforcement action against a former employee, an employer should focus on the need to protect its trade secrets and also look for any indicia of trade secret theft (e.g., unusual computer or e-mail activity shortly before an employee's departure).

19. *Arpac* at 75, 589 NE2d at 649.