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THE ENFORCEABILITY AND ADVISABILITY OF NONCOMPETITION, NONSOLICITATION AND CONFIDENTIALITY AGREEMENTS IN COLORADO

Christopher L. Ottele, Esq.
Emma L. Savory, Esq.
Husch Blackwell LLP
chris.ottele@huschblackwell.com
emma.savory@huschblackwell.com

I. Introduction to Colorado Noncompetition Covenant Law

A. Colorado Law and Its Exceptions

Like many states, Colorado balances competing public policy goals when determining the enforceability of noncompetition covenants. On the one hand, Colorado acknowledges the legitimate business interests of protecting a company's trade secrets and preventing nonpublic information from falling into the hands of a competitor. Courts also recognize that noncompetition covenants may be a restraint of trade or infringe an individual's right to make a living and are therefore disfavored. *Saturn Sys., Inc. v. Militare*, 252 P.3d 516, 526 (Colo. App. 2011).

The Colorado noncompetition covenant statute provides: "[a]ny covenant not to compete which restricts the right of any person to receive compensation for performance of skilled or unskilled labor for any employer shall be void." COLO. REV. STAT. § 8–2–113(2) (2015). The statute lays out four narrowly construed exceptions. *Nat'l Propane Corp. v. Miller*, 18 P.3d 782, 787 (Colo. App. 2000):

(1) Any contract for the purchase and sale of a business or the assets of a business;

(2) Any contract for the protection of trade secrets;

(3) Any contractual provision providing for recovery of the expense of educating and training an employee who has served an employer for a period of less than two years; and

(4) Executive and management personnel and officers and employees who constitute professional staff to executive and management personnel.

C.R.S. § 8-2-113(2)(a)-(d). Courts void covenants that do not meet one of the statutory exceptions. *Mgmt. Recruiters of Boulder, Inc. v. Miller*, 762 P.2d 763, 765 (Colo. App. 1988). A noncompetition provision must be enforceable at the time the parties form the agreement.

Phoenix Capital, Inc. v. Dowell, 176 P.3d 835, 840 (Colo. App. 2007). Even where a noncompetition covenant fits a statutory exception, it must still be reasonable in duration and scope. *Nat'l Graphics Co. v. Dilley*, 681 P.2d 546, 657 (Colo. App. 1984); *see infra* Section IV.

II. Statutory Exceptions

A. Purchase or Sale of a Business

The first exception allows for a noncompetition covenant in connection with the purchase and sale of a business or the assets of a business. When in conjunction with the sale of a business, such covenants protect the buyer's right to enjoy the goodwill purchased. *Gibson v. Eberle*, 762 P.2d 777, 779 (Colo. App. 1988). The rationale behind this exception is that goodwill "is an incident of a continuing business having a particular locality or name," and includes "the expectation of continued and repeated public patronage." *Nat'l Propane Corp. v. Miller*, 18 P.3d 782, 786 (Colo. App. 2000).

Even in the context of the sale or purchase of a business, the noncompetition covenant must still be "reasonable," which depends on whether the restraint on competition provides fair protection to the buyer's purchase of goodwill, while imposing restrictions no greater than necessary to protect the value of that goodwill." *See Barrows v. McMurtry Mfg. Co.*, 131 P. 430 (Colo. 1913).

Recognizing the diminished public policy concerns of restricting a former business owner from competing with the purchaser of its business or its assets, Colorado courts apply a less restrictive "reasonableness" standard to noncompetition covenants connected to the sale or purchase of a business than those in the strictly employment context. For example, a covenant not to compete ancillary to the sale of a business may be enforceable even when a covenant of similar breadth in the employment context would not be. *See Nat'l Propane Corp*, 18 P.3d at 786-87 (finding that a noncompetition covenant which was enforceable as a covenant ancillary to the sale of a business could be interpreted more liberally than an employer-employee noncompetition covenant). In making this distinction, Colorado courts cite to *Rent-A-Center, Inc. v. Canyon Television*, 944 F.2d 597, 600-01 (9th Cir. 1991):

> When deciding what is reasonable, courts give greater deference to restrictions that are part of the sale of a business than to restrictive covenants between employers and employees. This is because the seller of a business is more likely to have equal bargaining power in negotiating such covenants, and is presumably compensated by an increase in the selling price, while an employee merely receives the opportunity for continued employment.

Still, noncompetition covenants ancillary to the purchase or sale of a business must be reasonable as to scope and duration. *See Haggard v. Spine*, No. 09-CV-00721CMAKMT, 2009 WL 1655030, at *10 (D. Colo. June 12, 2009); *Reed Mill & Lumber Co.*, 165 P.3d at 735.

Noncompetition covenants generally do not survive the closure of that business. *See National Propane Corp. v. Miller*, 18 P.3d at 785-86 (finding that a noncompetition covenant in a contract for the purchase of a company was unenforceable after the purchaser ceased to exist as a separate

business entity, its office was closed, and its operations were merged into a successor corporation's operations).

B. Protection of Trade Secrets

The second statutory exception allows for noncompetition covenants that protect trade secrets. For a covenant to fit within the trade secrets exception, "the purpose of the covenant must be the protection of trade secrets, and the covenant must be reasonably limited in scope to the protection of those trade secrets." *Cocona, Inc. v. Singtex Indus. Co.*, No. 14-CV-01593-MJW, 2014 WL 5072730, at *4 (D. Colo. Oct. 9, 2014) (citing *Gold Messenger, Inc. v. McGuay*, 937 P.2d 907, 910–11 (Colo. App. 1997)).

Employers often mistakenly assert that day-to-day information constitutes a "trade secret." Litigation over the noncompetition clauses under this exception thus often focuses on whether an employee has access to a company's trade secrets. Courts evaluate the following factors to determine whether the information constitutes a trade secret:

(1) the extent to which the information is known outside the business;

(2) the extent to which it is known to those inside the business, *i.e.*, by the employees;

(3) the precautions taken by the holder of the trade secret to guard the secrecy of the information;

(4) the savings effected and the value to the holder in having the information as against competitors;

(5) the amount of effort or money expended in obtaining and developing the information; and

(6) the amount of time and expense it would take for others to acquire and duplicate the information.

Porter Indus., Inc. v. Higgins, 680 P.2d 1339, 1341 (Colo. App. 1984). Courts take a practical approach, attempting to determine whether the information alleged to be a trade secret gives the employee an opportunity to obtain an advantage over competitors who do not know or use it. *Gold Messenger*, 937 P.2d at 911.

A trade secret may consist of a number of different components, all of which are publicly known, if the specific combination of information could lead to a competitive advantage. *See e.g., Harvey Barnett, Inc. v. Shidler*, 338 F.3d 1125, 1130 (10th Cir. 2003); *Doubleclick Inc. v. Paikin*, 402 F. Supp. 2d 1251, 1257-58 (D. Colo. 2005). Knowledge of what a former employer plans to bid on a future contract can also be a trade secret. *Ovation Plumbing, Inc. v. Furton,* 33 P.3d 1221, 1224 (Colo. App. 2001).

An employer must take steps to protect its trade secrets. COLO. REV. STAT. § 7–74–102(4) (2015) (the owner of a trade secret "must have taken measures to prevent the secret from

becoming available to persons other than those selected by the owner…"). These precautions must be more than normal business procedures. *See Colo. Supply Co. Inc. v. Stewart*, 797 P.2d 1303, 1306 (Colo. App. 1990). For example, these efforts may include advising employees of the existence of a trade secret, limiting access to a need-to-know basis, and controlling access to locations where the information may be learned. *See Harvey Barnett, Inc. v. Shidler*, 143 F. Supp. 2d 1247, 1252 (D. Colo. 2001).

Like the business exception above, a noncompetition covenant designed to protect trade secrets must also be reasonably limited in scope to the protection of those trade secrets, and the reasonableness is determined on a case-by-case basis. *Gold Messenger*, 937 P.2d at 910. For example:

- In *Management Recruiters of Boulder, Inc. v. Miller*, the court found that a one-year restriction prohibiting a former employee from contacting any candidate with whom he had actual contact during his final year of employment was properly tailored to prevent the misappropriation of trade secrets. 762 P.2d at 766.

- In *Nutting v. RAM Southwest, Inc.*, the court determined that a noncompetition covenant between a manufacturer of artificial vampire fangs and an independent distributer, which also manufactured and sold its own line of fangs, was void because the worldwide, perpetual agreement was unreasonable in geographical scope and duration. 106 F. Supp. 2d 1121 (D. Colo. 2000).

C. Recovering Expenses of Education and Training

The third statutory exception allows for noncompetition covenants in the context of training and education expense recovery. An employer may enforce a noncompetition covenant against a former employee to recover expenses incurred for the education or training of the employee if the employee has served the employer for less than two years. COLO. REV. STAT. § 8-2-113(2)(c) (2015). However, this exception is inapplicable if the employment agreements do not contain a provision requiring reimbursement. *Dresser Indus., Inc. v. Sandvick*, 732 F.2d 783, 788 (10th Cir. 1984) (finding exception inapplicable where the employer incurred expenses in training employees who left after about eighteen months of employment, because their employment agreements contained no provision requiring reimbursement of training expenses).

D. Executive, Management and Professional Staff

1. *Executive and Management Personnel*

The fourth statutory exception applies to noncompetition covenants with "executive and management personnel and officers and employees who constitute professional staff to executive and management personnel." COLO. REV. STAT. § 8-2-113(2)(d). Courts analyze the following factors to determine if an employee is "executive and management personnel":

- Whether the employee is "in charge" of a significant portion of the plaintiff's business or other employees;

- Whether the employee acts in an unsupervised capacity; or

- Whether the employee has significant responsibility for the business and does more than transact business for the company.

See Doubleclick Inc. v. Paikin, 402 F. Supp. 2d 1251, 1258 (D. Colo. 2005); *Porter Indus., Inc. v. Higgins*, 680 P.2d 1339, 1342 (Colo. App. 1984); *Alexander & Alexander, Inc. v. Frank B. Hall & Co.*, No. CIV. A. 88-A-1621, 1990 WL 8028, at *5 (D. Colo. Jan. 31, 1990); *see also* John F. Reha, *The Law of Trade Secrecy and Covenants Not to Compete in Colorado-Part II*, 30 COLO. LAW. 5, 6 (2001).

Some examples illustrate the scope of this exception:

- A corporate stockholder who "was the only person who possessed the knowledge, skills, and the licenses to make the business a possible success" was executive or management personnel. *Harrison v. Albright*, 577 P.2d 302, 304 (Colo. App. 1977).

- A mid-level manager who supervised fifty employees, was at the top of the compensation scheme, was employed in a decision-making capacity, and had a certain level of autonomy was executive or management personnel. *DISH Network Corp. v. Altomari*, 224 P.3d 362, 368 (Colo. App. 2009).

- A defendant who supervised fifty employees, had only three levels of management above her, was in charge of a significant part of the company's business, and was at least partially involved in setting company strategy was executive or management personnel. *Doubleclick Inc. v. Paikin*, 402 F. Supp. 2d 1251, 1258-59 (D. Colo. 2005).

- An employee was not management personnel even though his title was Regional Account Manager. The court noted that the employee supervised two people, but had no hiring or firing authority. His duties involved contacting mortgage brokers and other entities in the lending industry who might potentially refer credit repair customers to the employer. *Cont'l Credit Corp. v. Dragovich*, No. 13-CV-01349-WYD-MJW, 2013 WL 3303976, at *4 (D. Colo. July 1, 2013).

- Account executives who were primarily information gatherers were not management personnel. *Mgmt. Recruiters of Boulder, Inc. v. Miller*, 762 P.2d 763, 765 (Colo. App. 1988).

- An employee whose job title was company representative and whose duties were to negotiate and sell contracts, make sales calls, keep updated contracts filed, and promoted the employer's business, was not "in charge" of the business's existing contracts and so was not executive or management personnel. *Porter Indus., Inc. v. Higgins*, 680 P.2d 1339, 1342 (Colo. App. 1984).

2. *Professional Staff*

The fourth statutory exception also accounts for "professional staff to executive and management personnel." COLO. REV. STAT. 8-2-113(2)(d). The General Assembly did not define the phrase "professional staff to executive and management personnel."

Some examples of this exception:

- Physicians are professional staff. *Boulder Med. Ctr. v. Moore,* 651 P.2d 464, 465 (Colo. App. 1982).

- A dentist, however, was not "professional staff" because, under the terms of his contract, he was an independent contractor and therefore not a member of the employer's staff. *Smith v. Sellers*, 747 P.2d 15, 17 (Colo. App. 1987).

- An employee, who managed the employer's analytics division, was not "professional staff" because eighty to ninety percent of his work was in a sales support role rather than support of executive or management functions. *Phoenix Capital, Inc. v. Dowell*, 176 P.3d 835, 841-43 (Colo. App. 2007).

E. Physicians

Colorado prohibits covenants not to compete purporting to cover physicians, but does permit a liquidated damages provision. Colo. Rev. Stat. § 8-2-113(3). In other words, a physician cannot be restricted from the practice of medicine, but a physician may be required to pay a fixed amount to her previous employer or partnership if she does compete.

The amount of liquidated damages must be reasonably related to the injury suffered by the termination of the agreement. *Id.* In *Wojtowicz v. Greeley Anesthesia*, 961 P.2d 520 (Colo. Ct. App. 1998), the Colorado Court of Appeals struck down such a liquidated damages provision. The *Wojtowicz* court reasoned that a damage provision could not be based on speculation or conjecture, and that damages for lost profits are measured by loss of net profits. *Id.* at 522. Ultimately, the court concluded that the liquidated damages provision that required the physician to pay 50 percent of his fees to the former employer for two years, was not reasonably related to the injury suffered where the evidence did not show a loss of profits. *Id*. at 523. The court concluded that the "fee percentage set as liquidated damages in the noncompetition provision [was] disproportionate to any possible loss incurred" by the employer. *Id.* The court also struck down a liquidated damages provision related to damage to the goodwill of the employer because there was no evidence of actual harm. *Id.*

III. Federal Law Update: The Defend Trade Secrets Act

In April 2016, the Defend Trade Secrets Act (DTSA) passed the U.S. House of Representatives by a vote of 410-2 and the U.S. Senate by a vote of 87-0. President Obama signed the bill into law on May 11, 2016.

The DTSA permits the owners of a trade secret to file lawsuits in federal district court for trade secret theft. In the past, only state courts have enforced trade secrets. While most states (48) have adopted some version of the Uniform Trade Secrets Act, companies struggled to obtain consistent, nation-wide relief. DTSA provides some other notable provisions.

- The DTSA grants whistleblowers protection from retaliation and immunity to turn a company's trade secrets over to the government to investigate potentially illegal activity. Whistleblowers are also permitted to turn a trade secret over to their personal attorney.

- Employers must disclose to employees in confidentiality agreements or policies this immunity. If not, they will not be eligible to receive punitive damages or attorneys' fees in an action against an employee to protect against the disclosure of the employer's trade secrets.

- A court may issue an *ex parte* order to seize property and prevent the dissemination of the trade secret.

- The DTSA does not preempt state laws.

See H.R. 3326 114th Cong. (2015-2016).

IV. The Covenant Must Also Be Reasonable in Duration and Scope

In addition to falling within one of the four statutory exceptions, a noncompetition covenant must be reasonable in duration, geographical scope and the scope of the restricted activities. *Energex Enters., Inc. v. Anthony Doors, Inc.*, 250 F. Supp. 2d 1278, 1283 (D. Colo. 2003). "These agreements must not impose undue hardship and must be no wider than necessary to afford the required protection." *Knoebel Mercantile Co. v. Siders*, 439 P.2d 355, 358 (Colo. 1968).

A. Duration

A noncompetition covenant in Colorado must specify at least the time and location limits. *Nat'l Graphics Co. v. Dilley*, 681 P.2d 546, 547 (Colo. App. 1984) (finding a noncompetition covenant with no time or geographic limits void as unreasonable, despite the employer's contention that the clause was reasonable because it was limited in terms of customer accounts acquired by the employee during the term of employment). A Colorado court will not create reasonable limits where a contract is silent on those issues. *See id.* There is no general rule regarding what is "reasonable" in noncompetition covenants. *Nutting*, 106 F. Supp. 2d at 1126.

The central inquiry is whether the restrictive provision is necessary to safeguard the plaintiff's business. *See Mgmt. Recruiters of Boulder, Inc. v. Miller*, 762 P.2d 763, 766 (Colo. App. 1988); *see also Nutting*, 106 F. Supp. 2d at 1127.

Colorado courts applying this fact-driven test have enforced noncompetition covenants with durations extending from six months to perpetuity. *See Energex*, 250 F. Supp. 2d at 1283; *see also Axelson v. Columbine Laundry Co.*, 254 P. 990 (Colo. 1927) (finding six month provision enforceable); *see also Weber v. Nonpareil Baking Co.*, 274 P. 932 (Colo. 1929) (finding perpetual covenant enforceable) *and Nutting v. RAM Southwest, Inc.*, 106 F. Supp. 2d at 1127 (striking down a perpetual restriction because there was no evidence that an unlimited time restraint was necessary to protect the employer and his product.).

A noncompetition clause with a maximum term of 18 months has been described as being "well within terms approved by Colorado courts." *Doubleclick Inc. v. Paikin*, 402 F. Supp. 2d 1251, 1259 (D. Colo. 2005).

B. Geographical Scope

Colorado courts have enforced a range of restrictions, ranging from county-wide to nationwide. *Gibson v. Angros*, 491 P.2d 87 (Colo. App. 1971) (finding five-year, countywide provision enforceable); *Harrison v. Albright*, 577 P.2d 302 (Colo. App. 1977) (finding five-year, 50 mile clause voluntarily supplied by employee as reasonable).

Still, the geographic limitation should relate to the location in which the employer actually does business because it would be unreasonable to prevent a former employee from pursuing a career in a place where the employer has no customers. *See Sprague's Aetna Trailer Sales, Inc. v. Hruz*, 474 P.2d 216, 218 (Colo. 1970) (finding reasonable a one-year noncompetition covenant for a former employee which had a seventy-five mile radius); *see also* John R. Paddock Jr., *Noncompetition agreements—Reasonable activity, time and geographic restrictions*, 16 Colo. Prac., Employment Law & Practice § 5.30 (2d ed.).

- In *Trans-American Collections, Inc. v. Continental Account Servicing House, Inc.*, the court upheld a two-year, nationwide competition restriction in the "flat-rate account collection letter business," even though the employee operated in only nine states. 324 F. Supp. at 1306. The court reasoned that the employee's influence extended far beyond his own territory and that the covenant was a reasonable restriction on his right to employment since he was a career salesman with skills and experience that could effectively apply in the sale of another service or product. *Id*.

- In *Energex Enterprises, Inc. v. Anthony Doors, Inc.*, the court upheld a noncompetition clause that extended for ten years and prohibited the employee from engaging in the sale of a product substantially similar to the employer's in all areas where any of the employer's products were sold. *Energex Enterprises, Inc. v. Anthony Doors, Inc.*, 250 F. Supp. 2d 1278, 1283 (D. Colo. 2003).

- In *Doubleclick Inc. v. Paikin*, the court granted a preliminary injunction enforcing an eighteen-month restriction that did not set a geographical limit for an "executive and management" employee. 402 F. Supp. 2d 1251, 1259 (D. Colo. 2005). The employee's former title was "Senior Vice President of Merchandise Services," she supervised nearly fifty employees and had only three levels of management above her in a multinational corporation. *Id*. She was also in charge of a significant amount of the company's business and played a role in setting company strategy. *Id*. The court reasoned that even though no geographic limitation existed, Colorado courts have approved nationwide restrictions. *Id*. (citing *Energex Enters., Inc. v. Anthony Doors, Inc.*, 250 F. Supp. 2d 1278, 1283 (D. Colo. 2003)).

- In *Nutting v. RAM Southwest, Inc.*, the court struck down a global restriction in a noncompetition covenant prohibiting the sale of "Dracula Fangs" because the employer offered no evidence that he required a worldwide restriction in order to protect his niche in the market. 106 F. Supp. 2d at 1127. Although the employer took some orders at a trade show, there were no allegations that the employer's business was worldwide or that the Dracula Fangs were ever sold in any country outside the United States. *Id*.

- Similarly, in *Harvey Barnett, Inc. v. Shidler*, the court struck down a limitless geographic restriction prohibiting employees from ever disclosing the employer's "specialized methods" of teaching children to swim. 143 F. Supp. 2d 1247, 1254-55 (D. Colo. 2001).

C. Scope of Restricted Activities

The reasonableness of a noncompetition restriction must not be broader than necessary to protect the employer's legitimate interests, and it must not impose hardship on the employee. *See Reed Mill & Lumber Co. v. Jensen*, 165 P.3d 733, 736 (Colo. App. 2006); *see also Saturn Sys., Inc. v. Militare*, 252 P.3d 516, 526–28 (Colo. App. 2011) (comparing trade-secret cases). A noncompetition restriction must not prevent the employee from being able to make a living. *See Saturn Sys.*, 252 P.3d at 526 (citing *Phoenix Capital, Inc. v. Dowell*, 176 P.3d 835, 844 (Colo. App. 2007)).

For example:

- In *Cocona, Inc. v. Singletex Indus. Co*., the court found that a noncompetition clause was reasonable in its scope of restricted activities because it did not prohibit a manufacturer from creating or selling fabrics that did not incorporate the distributor's "active particles," or trade secrets. No. 14-CV-01593-MJW, 2014 WL 5072730, at *3 (D. Colo. Oct. 9, 2014).

- In *Reed Mill & Lumber Co. v. Jensen*, the court found that a noncompetition covenant entered into between the buyer of a lumber company and a company employee, which prevented the employee from competing with the company for three years after the employee's termination, was unreasonable and unenforceable. 165 P.3d 73, 737-38 (Colo. App. 2006), *as modified on denial of reh'g* (Feb. 15, 2007). The covenant restricted the employee's right to because the employee's termination occurred six years after the sale of the company and restricted more than was necessary to protect the value of buyer's purchase of goodwill. *Id*.

V. Consideration for Noncompetition Covenants

Colorado noncompetition covenants require consideration. *Freudenthal v. Espey*, 102 P. 280, 283–84 (Colo. 1909). Colorado courts are hesitant to assess the adequacy of consideration. *Id*. (citing *Freudenthal*, 102 P. at 284).

Consideration may take the form of forbearance by one party to refrain from doing something that it is legally entitled to do. *Lucht's Concrete Pumping, Inc. v. Horner*, 255 P.3d 1058, 1061 (Colo. 2011). For example, forbearance of terminating an at-will employee at any time constitutes adequate consideration to support a noncompetition covenant. *Lucht's*, 255 P.3d at 1061. However, a noncompetition covenant may lack consideration where an employer enters into the agreement with the intention of terminating the employee immediately afterwards. *Id*. at 1063. Thus, employers may not act in bad-faith when entering into noncompetition covenants with employees.

VI. Nonsolicitation Agreements

Another method that employers may use to protect their legitimate business interest is to enter into nonsolicitation agreements with employees. These agreements prevent employees from soliciting coworkers or customers after employment termination.

A. Coworkers

A nonsolicitation agreement limited to prohibiting only active solicitation of former coworkers is enforceable with any employee, even if an accompanying noncompetition provision is void. *See Atmel Corp. v. Vitesse Semiconductor Corp*., 30 P.3d 789, 796 (Colo. App. 2001) *abrogated in part on other grounds by Ingold v. AIMCO/Bluffs, L.L.C. Apartments*, 159 P.3d 116, 124 (Colo. 2007); *see also Phoenix Capital, Inc. v. Dowell*, 176 P.3d 835, 844 (Colo. App. 2007).

Two cases address the issue of nonsolicitation agreements prohibiting a former employee's solicitation of former coworker:

- In *Atmel Corp. v. Vitesse Semiconductor Corp*., the court found that a nonsolicitation agreement can prevent a former employee from initiating contacts or "actively" soliciting former colleagues. 30 P.3d at 794-96. But, the *Atmel* court also held that a nonsolicitation agreement cannot prohibit a former employee from communicating with former coworkers who initiated such contact on their own. *Id.*

- Six years later, in *Phoenix Capital, Inc. v. Dowell*, the court held that where a nonsolicitation provision is limited to prohibiting only initiating contacts or "active" solicitation of the employer's employees, it is enforceable despite the invalidity of an accompanying noncompetition provision. 176 P.3d at 844.

B. Customers

Colorado courts analyze nonsolicitation agreements covering an employer's customers under C.R.S. § 8-2-113(2) because an agreement not to solicit customers is a form of an agreement not to compete. *Saturn Sys., Inc. v. Militare*, 252 P.3d 516, 526 (Colo. App. 2011) (citing *Phoenix Capital*, 17 P.3d at 844). Colorado courts will not enforce an agreement not to solicit customers unless it falls under one of the statutory exceptions of C.R.S. § 8-2-113(2). *See Phoenix Capital*, 17 P.3d at 844; *see also Mgmt. Recruiters of Boulder, Inc. v. Miller*, 762 P.2d 763, 764-65 (Colo. App. 1988) (invalidating under C.R.S. § 8-2-113(2) a nonsolicitation clause prohibiting contact with customers because "it would have the effect of restricting [the former employee] from working for another employer in the recruiting business.").

In contrast to the prohibition on actively soliciting an employer's employees, the *Phoenix Capital* court came to a different conclusion regarding nonsolicitation agreements restricting contact with customers, reasoning that in order to make a living, a former employee needs to be free to solicit—actively or passively—former customers, so long as he or she does not use the employer's trade secrets in doing so. 176 P.3d at 84.

An agreement not to solicit an employer's customers is enforceable when its purpose is to protect the employer's trade secrets and is reasonably limited in time and geographic scope. *Saturn*

Systs., Inc. v. Militare, 252 P.3d 516, 526 (Colo. App. 2011) (fining a nonsolicitation clause restricting an employee's ability to solicit the employer's clients for one year was necessary to protect the employer's confidential client and debtor information that could only be accessed via a password-protected website was narrowly tailored to restrict the employee only from soliciting the employer's customers as a way of protecting trade secrets and confidential information).

VII. Confidentiality Agreements

Well-drafted confidentiality agreements inform the employee of what the employer considers to be confidential, demonstrate the employer's steps to maintain secrecy of this information, and provide the employer with a breach of contract claim against an employee in violation of the agreement.

Under Colorado law, a confidentiality agreement is enforceable only to the extent that confidential information is acquired during the course of employment. *Mulei v. Jet Courier Service, Inc.*, 739 P.2d 889, 892–93 (Colo. App. 1987). General knowledge of a business operation and information already known to competitors or readily ascertainable elsewhere is not confidential. *Id.* Moreover, "confidential information" does not include the general ability that an individual brings into employment, or the skill and experience acquired by the individual during employment because "the right to use and expand this knowledge remains the employee's." *Id.*

Some recent examples of enforceable confidentiality agreements in Colorado include:

- Former employees breached their confidentiality agreements when they retained thousands of the employer's proprietary files, distributed copies of the employer's software programs, retained hard drive copies of test reports and test plans, and distributed copies of the software to a competitor's employee. *L-3 Commc'ns Corp. v. Jaxon Eng'g & Maint., Inc.*, No. 10-CV-02868-MSK-KMT, 2015 WL 5117792, at *19-20 (D. Colo. Sept. 1, 2015).

- An employee breached his confidentiality agreement, and the court entered a temporary restraining order requiring the return of confidential information, when the employee emailed a large volume of the employer's confidential documents to his personal email address including customer lists, supplier agreements and surveys, a quality control manual, organizational chart, contract manufacturing statement, product analytical information, as well as forms of non-disclosure agreements, product brochures, and software login information. *Atlas Biologicals, Inc. v. Kutrubes*, No. 15-CV-00355-CMA-MEH, 2015 WL 996368, at *1-2 (D. Colo. Mar. 3, 2015).

- An employee surreptitiously downloaded proprietary software information, pricing information, sales history and senior management reports onto portable CDs with the intention of taking them to his new employment with a competitor. The court determined that the documents constituted confidential information because: 1) the information was not known outside of the employer and was known only by a limited number of employees; 2) the employer took reasonable precautions to guard the secrecy of the materials, including limiting the number of people who had access to the information and

requiring those with access to sign confidentiality agreements, non-compete and non-disclosure agreements; and 3) the information contained in the documents took thousands of man-hours to prepare. *SBM Site Servs., LLC v. Garrett*, No. 10-CV-00385-WJM-BNB, 2011 WL 7563785, at *3 (D. Colo. June 13, 2011).

VIII. Practical Considerations in Drafting

A. Modification of Noncompetition Covenants: "Blue Lining"

Where a noncompetition covenant falls within a statutory exception but is unreasonable in terms of duration or scope, Colorado courts may exercise discretion and modify the covenants to conform with Colorado law. *See Nat'l Graphics Co. v. Dilley*, 681 P.2d 546, 547 (Colo. App. 1984) (citing *Whittenberg v. Williams*, 135 P.2d 228 (Colo. 1943) "[a] trial court has discretion to reform an unreasonable territorial restriction set forth in a covenant not to compete in order to make the scope of the geographic area reasonable."). *Energex Enter., Inc. v. Anthony Doors, Inc.*, 250 F. Supp. 2d 1278, 1283 (D. Colo. 2003) ("[i]f the trial court finds a particular noncompetition agreement unreasonable in either duration or scope, it has discretion to modify the terms of the agreement to render it reasonable and enforceable," citing *Gulick v. A. Robert Strawn & Assocs., Inc.*, 477 P.2d 489, 493 (Colo. App. 1970)); *Doubleclick*, 402 F. Supp. 2d at 1259. The court had "authority to modify the agreement to cure any unreasonable provision."

IX. Multistate Issues

A. Other States Laws

State law governs the enforceability of noncompetition agreements. Here are a few examples of how state laws differ from Colorado's law:

- California restricts noncompetition covenants in almost every circumstance. Generally "every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void." Cal. Bus. & Prof. Code § 16600. California does grant an exception to this general rule if it involves the sale of the goodwill of a business. Cal. Bus. & Prof. Code § 16601. California federal courts recognize a narrow exception to § 16600 if the agreement is necessary to protect an employer's trade secrets, but California state courts have not clearly adopted such exception. *Comp. Asset Marketing Systems v. Gagnon*, 542 F.3d 748, 758 (9th Cir. 2008); *with Edwards v. Arthur Anderson LLP*, 189 P.3d 285 (Cal. 2008).

- In Oregon, a noncompetition agreement entered into between an employer and employee is voidable and may not be enforced by a court unless:

    - The employee is informed in a written employment offer that a noncompetition agreement is required at least two weeks before or that noncompetition agreement is entered into upon a subsequent bona fide advancement of the employee by the employer;

    - The employee is an administrative, executive or professional employee;

- The employer has a protectable interest, *i.e.* the employee has access to trade secrets, confidential information, or the employee is employed as on-air talent; and

- The total amount of the employee's annual gross salary and commissions, calculated on an annual basis, at the time of the employee's termination exceeds the median family income for a four-person family. *See* O.R.S. § 653.295.

- In Montana, contacts which restrain people from exercising a lawful profession, trade, or business of any kind are void. There are two exceptions to this general rule: (1) a person who sells the goodwill of the business may agree with the buyer to refrain from business within the same and/or adjacent county, so long as the buyer continues the business; or (2) dissolution of a partnership. Mont. Code Ann. §§ 28-2-703 to 28-2-705.

- In Missouri, employers may have the limited restrictive covenants. V.A.M.S. § 431.202. The following are acceptable:

  - An agreement made between two entities is in connection to the acquisition of the corporation or entities during and for a reasonable period following the acquisition;

  - An agreement made between two or more entities in a joint venture or other business arrangement where such covenant seeks to protect against possible misuse of confidential or trade secret business information shared or to be shared between or among such entities;

  - An agreement between an employer and an employee seeking on the part of the employer to protect:

    - Confidential or trade secret business information; or

    - Customer or supplier relationships, goodwill or loyalty, which shall be deemed to be among the protectable interests of the employer; or

  - An agreement between an employer and employee, notwithstanding the absence of the protectable interests described above, so long as such covenant does not continue for more than one year following the employee's employment. This does not apply to agreements signed by employees who provide only secretarial or clerical services.

- In, Arizona, a restrictive covenant is unreasonable and will not be enforced "(1) if the restraint is greater than necessary to protect the employer's legitimate interest; or (2) if that interest is outweighed by the hardship to the employee and the likely injury to the public." *Valley Med. Specialist v. Farber*, 982 P.2d 1277, 1283 (Ariz. 1999).

- In Texas, a covenant not to compete is enforceable if it contains limitations as to time, geographical area, and scope of activity to be restrained that are reasonable and do not

impose a greater restraint than is necessary to protect the goodwill or other business interest of the promisee. The statute has special requirements for physicians. Tex. Code Ann. §§ 15.50

B. Choice of Law

Many noncompetition agreements contain a choice of law provision to attempt control what state's law governs the enforceability of the agreement. These provisions, however, are not always controlling.

In Colorado, courts will apply the law of the state chosen in the form forum selection clause unless the application of that state's law would be contrary to a fundamental policy of a Colorado and Colorado has a materially greater interest than state in the choice of law provision. *Haggard v. Spine*, No. 09-cv-00721, 2009 WL 1655030, *3 (D. Colo. June 12, 2009). Colorado has a strong public policy regarding covenants not to compete, as reflected in Colo. Rev. Stat. § 8-2-113(2). *Id.* at *4. The court then turns to the facts of the case to determine whether Colorado will have a materially greater interest than the state named in the agreement by considering factors such as, whether the employee is located, where the employee worked, where the company is located, and where the agreement was signed. *Id.*; *see also In re Hruby*, 512 B.R. 262 (D. Colo. 2014).