Ill. Noncompete Reform Balances Employee And Biz Interests

By **Peter Steinmeyer and Brian Spang** (June 2, 2021)

Peter Steinmeyer

Brian Spang

Over Memorial Day weekend, the Illinois Legislature accomplished something truly remarkable: a comprehensive reform of noncompete and nonsolicit law that was passed unanimously by the Illinois Senate and House of Representatives.

The reform bill[1] is not a complete ban, as some competing bills and employee advocates originally sought. And the bill is certainly not pro-enforcement, as many employers would prefer. Instead, it is that increasingly rare political creature: a compromise.

Why Is the Illinois Compromise Significant?

Attitudes toward restrictive covenants do not fit neatly into a red or a blue political litmus test, as there are competing interests recognized by persons on both sides of the political aisle. On the one hand, post-employment restrictive covenants are one of the most effective tools to protect confidential information, customer relationships, and a business's investment in itself and its employees.

Businesses in both red and blue states see the same color when it comes to protecting these interests: green. On the other hand, post-employment restrictive covenants impede employee mobility, and thereby clash with fundamental notions of individual liberty.

Forty-seven states permit post-employment noncompetition agreements to varying degrees, while three states and Washington, D.C., ban them. Two of the states that ban them — North Dakota and Oklahoma — are among the politically reddest of the red, while the third — California — is among the bluest of the blue.[2]

In recent years, abusive uses of noncompetes have received wide media attention,[3] which has led to an active debate across the country about the appropriate uses of post-employment restrictive covenants.[4] Should there be minimum income thresholds? If so, at what level?

In recent years, states have answered that question with widely varying answers, from New Hampshire on the low end at $30,160 per year,[5] to Washington state and Oregon on the high end at $100,000 per year.[6] Maryland, Rhode Island, Massachusetts, Maine and Virginia all fall in between.

Should customer or co-worker nonsolicits be treated differently than noncompetes? The Massachusetts, Washington state and Oregon statutes expressly carve out nonsolicits, but the Washington, D.C., ban does not.[7] Should employers be required to pay an employee not to compete, either via a paid post-employment restricted period, or via a required advance notice of resignation or termination — i.e., a mandatory garden leave period?

Massachusetts and Oregon have said yes, while Washington state requires payment during the restricted period in the event of a layoff.[8]

All of these issues, and many more, were debated, negotiated and hashed out in Illinois over the past year. The resulting Illinois compromise may prove to be a model for other states given its comprehensiveness and balancing of interests.

What Is the Illinois Compromise?

At its core, the Illinois compromise balances due process protections for employees — by imposing compensation thresholds and providing various procedural protections — while still preserving for employers an effective tool to protect their confidential information, customer relationships and the stability of their workforces.

The Illinois compromise also attempts to clarify the law about what constitutes adequate consideration and what qualifies as a legitimate business interest sufficient to warrant a restrictive covenant. If, as expected, Gov. J.B. Pritzker signs the bill into law, it should result in fewer traditional noncompete agreements, and potentially less litigation over noncompetes, but a greater likelihood of enforceability when a noncompete dispute actually ends up in court.

Highlights of the Illinois Bill

Effective Date

The bill applies to noncompetes and nonsolicits entered into after Jan. 1, 2022. It is not retroactive, and therefore does not apply to covenants executed before that date.

Prohibitions

The bill bans noncompetes for employees earning $75,000 per year or less, and bans customer and co-worker nonsolicits for employees earning $45,000 per year or less. Both of these salary thresholds are roughly indexed for inflation in future years.

The bill also prohibits noncompetes and nonsolicits for construction tradespeople and public employees.

Due Process Protections for Employees

The bill mandates that individuals be permitted at least 14 days to review the agreement and decide whether to sign, although an employee is free to sign in less than 14 days should they elect to do so. The bill also requires that individuals be advised in writing to consult with an attorney before signing.

And, importantly, the bill authorizes an employee to recover attorney fees, as well as appropriate relief, if the employee prevails on a claim filed by an employer seeking to enforce a noncompete or nonsolicit.

Clarification of Certain Ambiguities in the Common Law

The bill clarifies a number of ambiguities in Illinois' common law.

First, it reiterates that when determining whether an employer has a legitimate business interest sufficient to warrant a post-employment restrictive covenant, "the totality of the facts and circumstances of the individual case shall be considered," and "[e]ach situation must be determined on its own particular facts." Moreover, the bill reiterates that:

"Reasonableness is gauged not just by some, but by all of the circumstances."

Second, the bill clarifies that while a court "may refrain from wholly rewriting contracts ... [i]n some circumstances, a court may, in its discretion, choose to reform or sever provisions of a covenant not to compete or a covenant not to solicit rather than hold such covenant unenforceable."

Moreover:

> Factors which may be considered when deciding whether such reformation is appropriate include the fairness of the restraints as originally written, whether the original restriction reflects a good-faith effort to protect a legitimate business interest of the employer, the extent of such reformation, and whether the parties included a clause authorizing such modifications in their agreement.

Finally, the bill provides some clarification as to what constitutes "adequate consideration" sufficient to support a restrictive covenant. Specifically, the bill provides that:

> "Adequate consideration" means (1) the employee worked for the employer for at least 2 years after the employee signed an agreement containing a covenant not to compete or a covenant not to solicit or (2) the employer otherwise provided consideration adequate to support an agreement to not compete or to not solicit, which consideration can consist of a period of employment plus additional professional or financial benefits or merely professional or financial benefits adequate by themselves.

While this provision provides a clear safe harbor of two years of employment in terms of what is adequate consideration, it also clarifies that less than two years of employment may be sufficient if coupled with additional professional or financial benefits or merely "professional or financial benefits adequate by themselves."

Although it will be up to the courts to flesh out the meaning of these terms, such professional or financial benefits are anticipated to include consideration such as a raise, a promotion, training, professional exposure and marketing, incentive compensation such as stock options or restricted stock, bonuses, separation pay, or other employee benefits.

In other words, while on one hand this provision codifies to some extent the controversial Fifield rule that requires at least two years or more of continued employment, on the other hand this provision reinforces judicial and equitable flexibility.[9]

Key Exceptions in the Bill

The bill contains a number of critical exceptions.

First, the bill expressly carves out confidentiality, trade secret and invention assignment agreements from the definition of a covered noncompete.

Second, the bill also expressly exempts garden leave clauses — i.e., clauses or agreements requiring advance notice of termination of employment, during which notice period the employee remains employed by the employer and receives compensation — from the definition of a covered noncompete.

Third, the bill expressly exempts agreements entered into in connection with the acquisition

or disposition of an ownership interest in a business. As a result, noncompetes in purchase or sale agreements, or even agreements by which an employee acquires any ownership interest in a business, are not covered.

Fourth, the bill exempts "no reapplication" clauses in separation agreements.

Finally, although the protections in the bill apply to "no moonlighting" provisions in employment agreements, they do not apply to no moonlighting policies in employee handbooks.

State Attorney General Enforcement

In recent years, the Illinois Attorney General's Office has played an active and highly publicized role in policing certain situations involving form noncompete agreements that low-wage employees were compelled to sign. The bill codifies the state attorney general's power to protect the public in this area. Specifically, when the attorney general has "reasonable cause to believe than any person or entity is engaged in a pattern and practice prohibited" by the law, it may initiate or intervene in litigation.

Likewise, the bill also authorizes the attorney general to initiate an investigation of potential violations, and in an action brought under the bill, the attorney general may, but is not required to, request a civil penalty payable to the state, but the court has discretion whether to award any such penalty.

COVID-19-Related Terminations

The bill also contains an express exception for employees who lose their jobs because of the COVID-19 pandemic or under circumstances that are similar to the COVID-19 pandemic.

Namely, in that situation, the employer is barred from entering into a restrictive covenant with such persons

> unless enforcement of the covenant not to compete includes compensation equivalent to the employee's base salary at the time of termination for the period of enforcement minus compensation earned though subsequent employment during the period of enforcement.

What Should Employers Do Now?

In advance of the Jan. 1, 2022, statutory effective date, there are a number of steps that Illinois employers should take now.

First, employers should consider updating their existing agreements and having new ones executed before the law goes into effect on Jan. 1, 2022.

Second, for all form agreements to be executed on or after Jan. 1, 2022, employers must revise their agreements and comply with the due process provisions of the law — i.e., the 14-day review period and written advice to seek counsel from an attorney before signing.

Third, given the salary thresholds and consideration requirements, employers should use this as an opportunity to reassess which employees truly warrant post-employment noncompetition and/or nonsolicitation restrictions.

Fourth, employers need to reassess the consideration provided to employees in exchange for signing. Is it adequate? Should the employer change its practices with respect to promotions, bonuses, training, or participation in severance plans or stock option plans in order to ensure that it is providing adequate consideration?

Finally, all employers should consider moving to garden leave agreements rather than traditional noncompetes.

Peter Steinmeyer and Brian Spang are members, and co-chairs of the trade secrets and employee mobility practice group, at Epstein Becker Green.

Disclosure: Steinmeyer and Spang advised the Illinois Chamber of Commerce in its negotiations over this legislation, and Steinmeyer testified on behalf of the Illinois Chamber of Commerce in support of the bill before the Illinois House of Representatives.

[1] https://www.ilga.gov/legislation/102/SB/PDF/10200SB0672ham001.pdf.

[2] N.D. Cent. Code § 9-08-06; Cal. Bus & Prof. Code § 16600; N.D Cent. Code 9-08-06.

[3] See, e.g., Daniel Wiessner, Jimmy Johns settles Illinois lawsuit over non-compete agreements, Reuters (Dec. 7, 2016), https://www.reuters.com/article/us-jimmyjohns-settlement/jimmy-johns-settles-illinois-lawsuit-over-non-compete-agreements-idUSKBN13W2JA.

[4] Indeed, in a classic example of noncompete overreach, one of the authors of this article was required to sign a noncompete in order to work as a house painter as a college kid over summer break.

[5] N.H. Rev. Stat. Ann. § 275:70-a(b) (prohibiting non-competes for "low-wage" employees, defined as "an employee who earns an hourly rate less than or equal to 200 percent of the federal minimum wage").

[6] Wash. Rev. Code Ann. § 49.62.020(b).

[7] Compare Mass. Gen. Laws Ann. ch. 149, § 24L(a), Or. Rev. Code Ann. § 653.295(4)(b), and Wash. Rev. Code Ann. § 49.62.005(4), with D.C. Code Ann. § 32-581.01(5).

[8] See Mass. Gen. Laws Ann. ch. 149, § 24L(b)(vii); Or. Rev. Code Ann. § 653.295(6); and Wash. Rev. Code Ann. § 49.62.020(c).

[9] See Fifield v. Premier Dealer Services, Inc. , 2013 IL App (1st) 120327, ¶ 19 ("Illinois courts have repeatedly held that there must be at least two years or more of continued employment to constitute adequate consideration in support of a restrictive covenant. This rule is maintained even if the employee resigns on his own instead of being terminated.") (internal citations omitted).