ENFORCING RESTRICTIVE COVENANTS AGAINST EMPLOYEES DISCHARGED WITHOUT CAUSE

Can an employer enforce post-employment restrictive covenants (including agreements not to compete and not to solicit customers and employees) against an employee discharged without cause? According to two recent court decisions: yes and no.

The traditional view had been that employers could not enforce post-employment restrictive covenants against employees discharged without cause. In 2012, however, the U.S. Court of Appeals for the Second Circuit in *Hyde v. KLS Prof'l Advisors Group, LLC* suggested that even when an employer discharged an employee without cause, the enforceability of a restrictive covenant should be analyzed under *BDO Seidman's* reasonableness test which courts apply in determining the enforceability of restrictive covenants against employees who voluntarily resigned or were terminated for cause. Under that test, restrictive covenants are "reasonable" and therefore enforceable, where they: (1) are no greater than necessary to protect the legitimate interest of the employer; (2) do not impose undue hardship on the employee; and (3) are not injurious to the public.

A recent decision from the New York Appellate Division – New York State's intermediary appellate court – indicates that New York courts might be gravitating back to the original bright-line rule that an employer may not enforce any restrictive covenants against an employee terminated without cause. In *Buchanan Capital Markets, LLC v. DeLucca*, the court held that covenants not to compete in employment agreements are not enforceable if the employer "does not demonstrate continued willingness to employ the party covenanting not to compete."

Another recent case, however, illustrates how employers can seek to secure enforceable restrictive covenants when they are terminating an employee without cause. In *U.S. Security Assoc., Inc. v. Cresante*, the employee (Douglas Cresante) had signed an employment agreement which contained post-employment restrictive covenants. The day after U.S. Security terminated Cresante's employment, the parties entered into a separation agreement. In that agreement, U.S. Security agreed to pay Cresante seven weeks of severance that it was not otherwise obligated to pay as consideration for Cresante agreeing to adhere to the non-compete and non-solicitation provisions in his employment agreement. The New York trial court held that, even if U.S. Security had terminated Cresante's employment

THE BOTTOM LINE

A bright-line rule that an employer may not enforce restrictive covenants against an employee terminated without cause appears to be re-emerging in New York. But there are potential strategies for employers to secure enforceable post-employment restrictions against an involuntarily discharged employee, such as defining "cause" broadly in an employment agreement or agreeing to provide the employee benefits following termination to which the employee would not otherwise be entitled in exchange for the employee's agreement to adhere to reasonable restrictions.

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without cause, the restrictive covenants were enforceable if they were otherwise reasonable under the *BDO Seidman* analysis because the separation agreement constituted a contract independent of Cresante's previous employment agreement and Cresante was receiving benefits in addition to those to which he was entitled under his employment contract.

While employers should be mindful of the apparent re-emergence of the bright-line rule against enforcing restrictive covenants against employees discharged without cause, employers do have potential strategies for securing enforceable restrictive covenants. They can define "cause" broadly in an employment agreement, making it harder for the employee to argue that the termination was without cause. They can also provide the employee with new consideration to which he or she was not otherwise entitled in exchange for the employee's agreement to adhere to reasonable restrictive covenants.

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