

**The New Restrictive Covenants Act:
Sloppy Draftsmanship May Soon Be Forgiven**

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On April 29, 2009 Governor Perdue signed a bill fundamentally altering the treatment of restrictive covenants in Georgia. Assuming the required constitutional amendment is ratified as discussed below, Georgia General Assembly Act 64 (formerly HB-173) will have a dramatic effect on the legality of non-compete, non-solicitation, and non-disclosure covenants.

Background

Georgia courts are among the most hostile in the nation to restrictive covenants due to Georgia's strong public policy against contracts in partial restraint of trade. This policy is reflected in ART. III, SEC. VI, PARA. V(c) of the Georgia Constitution of 1983, which prohibits the General Assembly from authorizing any contract "which may have the effect of or which is intended to have the effect of defeating or lessening competition, or encouraging a monopoly" Based on this prohibition, Georgia courts traditionally strike down post-employment covenants deemed overly broad instead of "blue penciling" the agreements to make them reasonable as is done in most other states. W.R. Grace & Co. v. Mouyal, 262 Ga. 464, 465, 422 S.E.2d 529 (1992).

Generally, Georgia courts will enforce restrictive covenants if they are: (1) reasonable in scope; (2) supported by consideration; (3) reasonably necessary to protect the restraining party's interests; and (4) not unduly prejudicial to the interests of the public. Id. Given Georgia Courts' tendency to analyze restrictive covenants on a case-by-case basis and to construe these agreements against the employer, this is a particularly difficult area for employers to navigate.

The Act

Georgia General Assembly Act 64 ("Act 64") is the legislature's most recent attempt to expand the permissible contours of restrictive covenants. A substantially similar law was passed in 1990, codified at O.C.G.A. § 13-8-2.1 *et seq.* The Georgia Supreme Court found that section unconstitutional because it may have the effect of or was intended to have the effect of defeating or lessening competition or encouraging monopoly in violation of ART. III, SEC. VI, PARA. V(c) of the Georgia Constitution of 1983. See Jackson & Coker v. Hart, 261 Ga. 371, 405 S.E.2d 253 (1991).

The stated purpose of Act 64 is to "provide statutory guidance so that all parties to such agreements may be certain of the validity and enforceability of such provisions and may know their rights and duties according to such provisions." Act 64, Art. 4. In response to the Jackson

decision, Act 64 only becomes effective "on the day following the ratification at the time of the 2010 general election an amendment to the Constitution of Georgia providing for the enforcement of covenants in commercial contracts that limit competition." Act 64 legislates presumptively reasonable time, territory, and scope of activity restrictions for non-compete, non-solicitation, and non-disclosure covenants.

Targeted Employees

Act 64 only applies to non-competition and non-disclosure covenants against certain employees, namely those who:

- Customarily and regularly solicit for the employer customers or prospective customers;
- Customarily and regularly engage in making sales or obtaining orders or contracts for products or services to be performed by others;
- Have a primary duty of managing the enterprise in which the employee is employed or a customarily recognized department or subdivision thereof;
- Customarily and regularly direct the work of two or more other employees; and
- Have the authority to hire or fire other employees or have particular weight given to suggestions and recommendations as to the hiring, firing, advancement, promotion, or any other change of status of other employees; or
- Perform the duties of a key employee or of a professional.

Non-solicitation covenants, in contrast, are enforceable against any employee, but they may only prevent an employee from soliciting for competitive services those actual or prospective customers of the employer with whom the employee had material contact during his employment.

Magic Language

Act 64 eliminates all "magic language" requirements and instructs courts to narrowly construe certain terms to make covenants enforceable. Any reference to a prohibition against "soliciting or attempting to solicit business from customers" is sufficient in the context of a non-solicitation covenant. Activities, products, or services shall be considered sufficiently described if a reference to them is provided and qualified by the phrase, "of the type conducted, authorized, offered, or provided within two years prior to termination," or similar language containing the same or a shorter time period. Similarly, the phrase, "the territory where the employee is working at the time of termination," or similar language shall be considered sufficient as a description of geographic areas if the person or entity bound by the restraint can reasonably determine the maximum reasonable scope of the restraint at the time of termination.

Presumptively Reasonable Time Periods

Courts are instructed to presume a post-employment restrictive covenant is reasonable in time if it lasts for two years or less in an employment relationship, three years or less in a dealer/distributor/licensee relationship, and five years or less in the sale of a business. During the employment relationship, a restrictive covenant for the entire employment period and a geographic territory including all areas in which the employer does business during the relationship are reasonable, provided that the total distance encompassed is reasonable, and/or specific competitors are enumerated for which the employee may not work during a limited period of time after the employment ends.

Blue Penciling

Act 64 provides that “a court may modify a covenant that is otherwise void and unenforceable so long as the modification does not render the covenant more restrictive with regard to the employee than originally drafted by the parties.” While this provision is permissive, the Act further provides that “[a] court shall construe a restrictive covenant with the reasonable intent and expectations of the parties to the covenant and in favor of providing reasonable protection to all legitimate business interests established by the person seeking enforcement.” Read in conjunction, these sections appear to render blue penciling mandatory.

Burden Shifting

The initial burden is cast on the party seeking enforcement to “plead and prove the existence of one or more legitimate business interests justifying the restrictive covenant.” Once a prima facie showing has been made that the restraint is in compliance with Act 64, the burden shifts to the party opposing enforcement to establish noncompliance or that the covenant is unreasonable.

Remedies

Act 64 requires that courts “shall” enforce restrictive covenants by “appropriate and effective” remedies, including but not limited to temporary and permanent injunctions. In determining the appropriate remedy, courts may consider economic hardship imposed on an employee, but economic hardship may not be considered for agreements between distributors and manufacturers, lessors and lessees, partnerships and partners, franchisors and franchisees, sellers and purchasers of a commercial enterprise, or two or more employers.

Conclusion

If the constitutional amendment is passed, Act 64 will provide employers with significantly more protection from departing employees than they currently have. Act 64 may have the unintended effects of increasing litigation in this area and casting the ultimate responsibility for drafting enforceable restrictive covenants on the courts.