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Alert

New Jersey Appellate Court Provides Some Clarity on the Scope and Use of Employment Restrictive Covenants

By: Joshua L. Weiner
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The New Jersey Appellate Division has clarified the analysis required to determine the effect of restrictive covenant agreements (RCAs) and offered guidance to practitioners drafting RCAs under New Jersey law in a decision on six consolidated actions. *ADP, LLC v. Kusins*, No. A-4664-16T1 (N.J. Super. Ct. App. Div. July 26, 2019).

Background

In *Kusins*, the employer had a two-tiered system of restrictive covenants. In the first-tier, each sales representative, upon hire, executed agreements containing general non-compete and non-solicitation provisions limited to the geographic regions in which the representative worked and tailored to the clients the representative contacted while employed.

In the second-tier, however, each representative executed "click-wrap" agreements that, in exchange for participation in a stock award incentive program, included restrictions on soliciting *any* actual or prospective client without regard to the representative's geographic location or personal contact with the client or prospective client.

Generally, representatives worked for the company in specific geographic territories and markets, received extensive training, maintained lists of clients and prospects, and received access to the company's pricing information.

The defendants voluntarily resigned their respective employments with the company to accept positions with a competitor. Thereafter, the defendants allegedly engaged in activities that violated the terms of their RCAs to varying degrees and the company sued to enforce the agreements.

Appellate Court Decision

The appeals court first reaffirmed New Jersey's recognition of the enforceability of RCAs designed to protect the legitimate interests of an employer, as long as the restrictions "impose[] no undue

hardship on the employee, and [are] not injurious to the public." The Court noted that any such restrictions must be reasonable in "duration, area, and scope of activity." It also noted that a company may properly protect its trade secrets, proprietary information, and customer relationships through RCAs.

The Court approved the company's two-tiered system, which utilized heightened restrictions for upper-level employees. It said such an approach reflected "the greater damage those employees could inflict" on the company upon departure. The Court noted the additional training provided to such employees, the investment in such employees, and their access to proprietary information justified the heightened restrictions. Indeed, the Court said these factors made the representatives attractive to competitors.

The Court, however, found the non-compete and non-solicitation clauses in the second-tier RCAs unreasonable as written. It therefore modified (or "blue-penciled") those provisions to make them enforceable.

First, the clauses applied to any and all company clients, not just the existing clients the representative actively worked on or whose identity the representative learned of while employed by the company. The Court found this restriction unreasonable, explaining that where a representative could not possibly know all of a company's actual clients, such a broad restriction is unenforceable. Therefore, the Court upheld the modification of the provision to the extent it is limited to clients the former employees worked on or whose identity the employee learned of while employed by the company.

Second, the non-solicitation clause applied to any prospective client. The Court likewise held this restriction to be unreasonable, explaining that, to be enforceable, a non-solicitation clause as to prospective clients must be limited to prospective clients the representative gained knowledge of while employed by the company. The Court upheld the modification to that provision, as well, to reflect its limitations as to prospective clients the former employee gained knowledge about during employment.

Third, the Court upheld the non-competition restriction and its geographic limitation, but rejected the lower court's further narrowing of the restriction to the former employee's specific market segment.

Impact of *Kusins*

In *Kusins*, the New Jersey Appellate Division clarified that, notwithstanding news reports and legislation aimed at limiting the use and enforceability of non-competition agreements, such restrictive covenants remain enforceable in New Jersey.

New Jersey companies or companies with a New Jersey choice-of-law provision in their RCAs should review existing non-competition and non-solicitation agreements to determine compliance with *Kusins*. Moreover, with the Court's express approval of a two-tiered restrictive covenant system,

companies may want to explore implementing a similar protocol to ensure that the level of limitations reflects an employee’s position with the company. The attorneys at Coughlin Midlige & Garland are prepared to assist you in reviewing, modifying and/or drafting non-disclosure and other employment agreements containing restrictive covenants.