

Confidentiality, Non-Compete Agreements Unenforceable against Former Employee, Arizona Court Holds

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Striking four restrictive covenants in an employment agreement as overbroad, the Arizona Court of Appeals affirmed the dismissal of a breach of contract claim against the president of a public relations firm who set up a business competing with her former employer. *Orca Communications Unlimited, LLC v. Noder*, No. 12-0183 (Ariz. Ct. App. Oct. 17, 2013). However, the Court allowed claims for breach of the covenant of good faith and fair dealing, breach of the duty of loyalty, tortious interference, and unfair competition to proceed, finding they were not preempted by the Arizona Uniform Trade Secrets Act.

Background

Ann Noder served as the President of Orca Communications Unlimited. As a condition of her employment, Noder signed a Confidentiality, Non-Solicitation and Non-Competition Agreement that included four restrictive covenants: (1) a confidentiality provision, (2) a non-competition provision, (3) a customer non-solicitation provision, and (4) an employee non-solicitation provision.

Under the confidentiality provision, Noder was prohibited from directly or indirectly using any confidential information to compete with Orca. The Agreement defined confidential information as “knowledge or information not generally known to the public or in the public relations industry,” including any information Noder learned during her employment. Confidential information also included public information, but that “was only available through ‘substantial searching of published literature’ or that had to be ‘pieced together’ from a number of publications or sources.” The three other restrictive covenants prohibited Noder from competing with Orca and from soliciting any current, former, or potential Orca customer or current or former employee for a period of 18 months following termination.

In February 2009, Noder sought to purchase Orca from the owner, but no deal was reached. Thereafter, Noder began to solicit Orca’s potential customers, informing them that she was setting up a competing company.

After Noder resigned and formed her own public relations company, Orca sued her for breach of contract and various business torts. Noder asked the trial court to dismiss the case, arguing, among other things, that the restrictive covenants were unenforceable and the Arizona Uniform Trade Secrets Act (“AUTSA”) preempted the other claims. The trial court agreed and dismissed the lawsuit. Orca appealed.

Applicable Law

Under Arizona law, restrictive covenants that “tend to prevent an employee from pursuing a similar vocation after termination of employment are disfavored” and are strictly construed against the employer. *Amex Distrib. Co., Inc. v. Mascari*, 150 Ariz. 510, 724 P.2d 596 (App. 1986). 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*, 194 Ariz. 363, 369 ¶ 20, 982 P.2d 1277, 1283 (1999).

Further, under Arizona law, trade secrets are a legitimate protectable interest (*Calisi v. Unified Fin. Servs., LLC*, 232 Ariz. 103, 302 P.3d 628 (App. 2013)), as is customer information, if “truly confidential, and to a substantial degree inaccessible.... *Amex Distrib. Co., Inc.*, 150 Ariz. at 516, 724 P.2d at 602.” However, information available in trade journals, reference books, or published materials is public knowledge and not confidential. *Enter. Leasing Co. of Phoenix v. Ehmke*, 197 Ariz. 144, 3 P.3d 1064 (App. 1999).

Agreement Overbroad

The former employer argued that the Agreement’s confidentiality provision was enforceable because it protected “information not generally known in the public relations industry.” Calling this position “untenable,” the Court pointed out the provision covered public information that was derived through research. The Court found such information was not protectable even if an individual would need to spend substantial time to gather it and comprehend its significance. Further, the confidentiality provision applied to any information that Noder learned during her employment and contained no geographic restriction. Thus, the Court ruled, the confidentiality provision acted as a non-compete, effectively barring Noder from working anywhere in the public relations industry for one year. Accordingly, the Court found the confidentiality provision was unenforceable as a geographically unrestricted non-competition agreement.

Next, the Court found that the non-competition provision covered more than Orca’s legitimate business interests. Rather, the provision prevented Noder from “pursuing any type of work in the public relations industry, even work that would be based on her skill and talents and not merely on confidential information or customer relationships.” As such, the Court ruled, the provision acted as restraint on competition *per se* and was overbroad. Likewise, the non-solicitation provisions were overbroad, the Court determined, because they applied to Orca’s former and potential clients and employees, in which Orca had no protectable interests. Accordingly, the Court found the non-competition and non-solicitation provisions were unenforceable and overbroad.

The Court, however, allowed claims for breach of the covenant of good faith and fair dealing, breach of the duty of loyalty, tortious interference, and unfair competition to proceed, finding they were independent of the breach of contract claims and not preempted by the AUTSA.

Arizona courts carefully scrutinize restrictive covenants and will strike any provisions not narrowly drafted to protect an employer’s legitimate interests, such as the protection of trade secrets, confidential, non-public information, and current customer relationships. Employers should consider including temporal and geographic restrictions in all restrictive covenants, including confidentiality agreements, to avoid the risk that they will be construed as overbroad non-competition agreements. This decision also confirms that various business tort remedies remain available to Arizona employers whose employees misuse confidential information. Arizona employers should consider reviewing their restrictive covenants to determine if they appropriately protect business interests or whether they should be modified to strengthen enforceability.

Jackson Lewis attorneys are available to answer questions on this and other workplace developments. Please contact Robert K. Jones, jonesr@jacksonlewis.com, Stephen B. Coleman, colemanB@jacksonlewis.com, in our Phoenix office, (602) 714-7044, or the Jackson Lewis attorney with whom you regularly work.

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practices

Non-Competes and Protection Against Unfair Competition

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