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## Illinois eAuthority

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### **Illinois Supreme Court Resolves Split in Appellate Courts and Rejects Use of Rigid Tests to Evaluate Restrictive Covenants**

On December 1, 2011, the Illinois Supreme Court issued a unanimous opinion in *Reliable Fire Equipment Company v. Arredondo*, No. 111871, 2011 WL 6000743 (Dec. 1, 2011) holding that courts cannot use rigid, structured tests to determine whether restrictive covenants are enforceable. Specifically, the Illinois Supreme Court held that while courts must continue to evaluate whether an employer has a legitimate business interest that justifies the use of a restrictive covenant, courts should not use isolated, inflexible factors in making this assessment.

#### **Split in the Appellate Courts**

This decision resolves a split among the Illinois appellate courts first created by the Fourth District Appellate Court's 2009 decision in *Sunbelt Rentals, Inc. v. Ehlers*, 394 Ill. App. 3d 421 (4th Dist. 2009). In *Sunbelt*, the Fourth District held that "a court, when presented with the issue of whether a restrictive covenant should be enforced, should evaluate its reasonableness based only on its time and territory restrictions," and should not look to whether the employer has a legitimate business interest.

In *Reliable Fire Equipment Co. v. Arredondo*, 405 Ill. App. 3d 708, 723 (2d Dist. 2010), the Second District Appellate Court rejected the Fourth District's decision in *Sunbelt*, and held that Illinois Supreme Court precedent establishes that courts should determine whether an employer has a legitimate business interest, as part of a three-prong test to determine whether a restrictive covenant is reasonable.

The Illinois Supreme Court concurred, holding that it "emphatically disagreed" with the Fourth District's holding in *Sunbelt*, and reasserted that the legitimate business interest of an employer is a component courts should consider as part of the three-prong reasonableness test for restrictive covenants. The court then turned to the issue of the proper application of the legitimate business interest test.

## Factual Background

In 1997, Reliable Fire Equipment Company required all of its employees to sign non-competition covenants. Reliable sells, installs and services portable fire extinguishers and a variety of fire suppression and fire alarm systems. Arnold Arredondo and Rene Garcia signed the non-competition covenants with Reliable in which they promised, among other things, not to compete with Reliable during their employment and for one year following their termination from employment in Illinois, Indiana, or Wisconsin. In 2004, Arredondo and Garcia signed an operating agreement for a newly-formed corporation named High Rise Security Systems, which intended to supply engineered fire alarm and related auxiliary systems through the Chicago metropolitan area. Soon after, Reliable terminated Garcia on suspicion of competition and Arredondo resigned.

Reliable filed a multiple count complaint against Garcia, Arredondo, and High Rise Security Systems, alleging that they had violated the restrictive covenants in their employment agreements by providing services to Reliable customers and soliciting referrals from Reliable's referral sources. In response, Garcia, Arredondo, and High Rise Security filed a counterclaim seeking, among other things, a declaration that the restrictive covenants were unenforceable. The circuit court ruled that the restrictive covenants were unenforceable on the basis that Reliable did not satisfy its threshold obligation to establish it had a legitimate business interest in enforcing the agreement. The Second District Appellate Court affirmed on the same basis.

## Legal Analysis

The Illinois Supreme Court began its analysis by articulating the elements for determining whether a non-competition restrictive covenant is reasonable and, therefore, enforceable in the state of Illinois. The court held that an enforceable covenant must: (1) be no greater than is required for the protection of a legitimate business interest of the employer-promissee; (2) not impose an undue hardship on the employee-promisor; and (3) not be injurious to the public. The court then turned its focus to the issue of whether Reliable had a legitimate business interest that justified its non-competition restrictive covenant.

The Supreme Court held that the circuit court and appellate court erred in deciding the case solely under the "rigid and preclusive" legitimate business interest test established by the Illinois Appellate Court in *Nationwide Advertising Service, Inc. v. Kolar*, 14 Ill. App.3d 522, 673 (1st Dist. 1973). According to that test, a restrictive covenant would be enforced if the employer established at least one of the two legitimate business interests for enforcing the agreement, including that: (1) the employee acquired confidential information through his or her employment and subsequently attempted to use it for his or her own benefit or (2) by the nature of the business, the customer relationship is near permanent and but for his or her association with the plaintiff, the defendant would never have had contact with the clients in question.

Declaring that the *Kolar* test was "no longer valid," the Supreme Court held that "whether a legitimate business interest exists is based on the totality of the facts and circumstances of the individual case." The court went on to explain that "factors to be considered in this analysis include, but are not limited to, the near-permanence of customer relationships, the employee's acquisition of confidential information through his employment, and time and place restrictions." While cautioning that none of these factors should carry any more weight than any other, the Supreme Court held that courts should contemplate these factors and others alongside the unique facts and circumstances of each case.

## Practical Impact

[Carol Poplawski](#), a shareholder in Ogletree Deakins' Chicago office and member of the firm's Unfair Competition and Trade Secrets Practice Group, explained that this case reinforces the importance

of a company taking an individual approach to restrictive covenants. A one-size-fits-all restriction may not provide the greatest protection for a company seeking to impose reasonable post-employment restrictions since the facts and circumstances among job duties, markets, and industries vary greatly.

[Tobias Schlueter](#), a shareholder in Ogletree Deakins' Chicago office and on the Steering Committee of the firm's Unfair Competition and Trade Secrets Practice Group, explained that by eliminating protection of confidential information and near-permanent customers as the sole criteria for establishing a legitimate business interest and instead looking at the totality of circumstances, this decision creates a more favorable environment for employers to demonstrate that they have enforceable restrictive covenants.

### **Additional Information**

Should you have any questions about this decision or its impact on your workplace, contact the Ogletree Deakins attorney with whom you normally work or the Client Services Department at 866-287-2576 or via email at [clientservices@ogletreedeakins.com](mailto:clientservices@ogletreedeakins.com).