A Timely Analysis of Legal Developments

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Colorado Court of Appeals holds that continued at-will employment, without more, is insufficient consideration in return for a promise not to compete.

Continued At-Will Employment Does Not Constitute Consideration for Noncompete Agreements in Colorado

By Darren E. Nadel and Katherine Dix

After years of uncertainty as to whether continued at-will employment constitutes consideration to support a noncompete agreement, the Colorado Court of Appeals squarely addressed the issue in *Lucht's Concrete Pumping, Inc. v. Horner* (No. 08CA0936, June 11, 2009). The appellate court clarified that continued at-will employment, without more, is insufficient consideration in return for a promise not to compete. The *Lucht's Concrete Pumping* panel further held that the duty of loyalty owed by an employee to his employer is only a fiduciary one when the employee is deemed an agent of the employer.

Colorado Noncompete Law – A Refresher

In Colorado, a presumption exists against the enforceability of restrictive covenants due to the "strong policy against covenants not to compete."[1] Restrictive covenants are only enforceable if: (1) the basis of the restrictive covenant fits within four statutorily defined exceptions to the prohibition on covenants not to compete;[2] (2) the restrictive covenant is reasonable as to duration and geographic scope; and (3) the covenant, as with all contracts, is supported by adequate consideration.

Prior to *Lucht's Concrete Pumping*, Colorado courts had not directly addressed whether continued at-will employment constitutes consideration to sustain a noncompete agreement. However, Colorado law has long recognized that new employment provides adequate consideration for a restrictive covenant.[3]

Factual And Procedural Background of *Lucht's Concrete Pumping*

In 2001, plaintiff Lucht's Concrete Pumping, Inc. (LCP) hired defendant Tracy Horner as its mountain division manager. LCP understood that the "key to the success or failure of its mountain division depended upon Horner and the relationships he would establish" because no other LCP employee possessed meaningful customer relationships in the mountain region.

On April 15, 2003, LCP requested that Horner sign an "employee non-disclosure and confidentiality agreement." Horner agreed and did in fact sign the agreement. In the agreement, Horner agreed not to compete with LCP for a period of 12 months following his termination. In exchange for the agreement, Horner, an at-will employee, received continued employment from LCP.

Horner resigned his employment on March 12, 2004. Three days later, he began working for defendant Everist Materials, LLP (Everist). Everist then began directly competing against LCP. However, Everist's direct competition with LCP did not occur overnight. As early as February 2004, Horner began discussing the possibility of joining Everist as an employee and assisting Everist in competing against LCP.

LCP sued Horner for breach of contract, breach of duty of loyalty, breach of fiduciary duty, and misappropriation of trade values. LCP further sued Everist for aiding and abetting breach of duty of loyalty, aiding and abetting breach of fiduciary duty, intentional interference with contract, and misappropriation of trade values.

The trial court granted summary judgment in favor of Horner on LCP's breach of contract claim, finding that the noncompete agreement was unenforceable due to the lack of consideration. Following a bench trial, the trial court found in favor of Horner and Everist on the remaining claims.

New Consideration Required for Noncompete Agreements

On LCP's appeal, the Colorado Court of Appeals first held that continued at-will employment, without more, is insufficient consideration for a noncompete agreement: "when an employee continues his or her job without receiving additional pay or benefits when a noncompete agreement is signed, the agreement lacks consideration."

The appellate court reasoned that by providing continued, at-will employment, the employer has not provided the employee with any benefit; due to the nature of at-will employment, the employer could terminate the employee at any time and for any reason both before and after the employee executed the agreement. Conversely, the employee's promise to refrain from competition could last months or even years beyond the termination date.

The appellate court was quick to distinguish prior cases wherein continued employment could furnish the necessary consideration to make a policy or procedure binding on an employer. Those actions were brought by employees to enforce an employer's promise for benefits, or to follow certain policies or procedures.

In the *Lucht's Concrete Pumping* case, Horner was asked to and did execute a noncompete agreement purporting to limit his right to compete for twelve months. However, he was not given a pay increase, promotion, nor any new benefit in consideration for his new commitment to LCP. For these reasons the Court held that the noncompete agreement was unenforceable for lack of consideration.

No "Heightened" Duty of Loyalty in the Employment Law Context

The Colorado Court of Appeals next held that no "heightened" duty of loyalty exists in the employment context. Instead, only when an employee is deemed an agent of the employer is the resulting relationship a fiduciary one. Thus, "the duty of loyalty ... applies in situations where an employer establishes that an employee has sufficient authority to create a principal-agent relationship."

The court found that Horner owed LCP a duty of loyalty because he: (1) maintained extensive customer relationships; (2) was responsible for recruiting employees and for reporting on future work; (3) held limited pricing authority; (4) managed many aspects of certain customer accounts; (5) supervised the work of other employees; and (6) more importantly, had ongoing personal contacts with many important clients.

When an agency relationship is created, the employee owes a duty to his employer to act solely for the benefit of the employer in all matters connected with the employment relationship. This includes a duty not to compete with the employer concerning the subject

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matter of the employment relationship, solicit customers, or solicit coworkers. However, an employee is entitled to take limited steps to prepare for competition with his or her employer after the termination of employment. In determining whether an employee's actions constituted mere preparation or active competition, Colorado courts will evaluate the nature of the preparation. Notably, an employee does not have a duty to disclose his or her intent to resign nor his or her plan to compete.

In light of the fact that the trial court found no evidence that Horner solicited LCP's customers or employees, nor disclosed any trade secrets or proprietary information, the appellate court upheld the trial court's determination that Horner did not violate his duty of loyalty.

Recommendations

In light of the *Lucht's Concrete Pumping* case, employers should consider:

- Redrafting restrictive covenants to explicitly recite the consideration the employer is providing to employees (stating, of course, that the consideration is something other than continued employment);
- Asking applicants or employees to sign restrictive covenants as a condition of their hire, raise, promotion, or receipt of additional benefits;
- Providing consideration in return for the execution of a restrictive covenant, such as a bonus payment or the ability to enroll in a company-sponsored life insurance plan; and
- Obtaining counsel to review whether existing restrictive covenants are enforceable or if an employer should require employees to re-sign restrictive covenants currently in place in return for additional consideration.

Darren E. Nadel is a Shareholder and Katherine Dix is an Associate in Littler Mendelson's Denver office. If you would like further information, please contact your Littler attorney at 1.888.Littler, info@littler.com, Mr. Nadel at dnadel@littler.com, or Ms. Dix at kdix@littler.com.

[1] *Dresser Inds., Inc. v. Sandvick*, 732 F.3d 783, 7787 (10th Cir. 1984).

[2] The legislature carved out four bases to support a noncompete agreement, including when the agreement is: (a) part of a purchase and sale of a business or the assets of the business; (b) intended to protect trade secrets; (c) intended to provide for the recovery of the expense of educating and training an employee who has worked for less than two years; and (d) cover executive and management personnel, and officers and employees who constitute professional staff to executive and management personnel. C.R.S. § 8-2-113.

[3] *See Freudenthal v. Espey*, 45 Colo. 488, 500, 102 P. 280 (1909).

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