Georgia's New Restrictive Covenant Act: How It Will Impact You

By Jason D'Cruz and Brian Harris

2011 Georgia House Bill 30, designed to substantially reenact the substantive provisions of the new Georgia Restrictive Covenant Act (the "Act") originally passed in 2009, is now law, signed by Governor Nathan Deal on May 11, 2011, immediately taking effect and codified at O.C.G.A.§13-8-50 et. seq. The Act dramatically changes the enforceability of restrictive covenants in employment agreements and corporate contracts entered into on or after the act's May 11 effective date. Although the Act applies beyond the employment context, this article specifically addresses important considerations for companies with Georgia employees, explores certain key sections of the Act, and provides practical pointers for drafting and enforcing restrictive covenants in employment agreements.

Pre-Act Law Versus New Law

Significantly, the Act is not a replacement for pre-Act case law governing restrictive covenants in Georgia. The Act applies only to those agreements "entered into on and after" the new Act's effective date (May 11, 2011). Agreements entered into prior to May 11, 2011 would still be interpreted and enforced under pre-Act case law.

The Act differs from pre-Act case law in five key areas by: (1) expressly permitting restrictive covenants, including non-compete covenants; (2) relaxing certain standards set by pre-Act case law for drafting enforceable covenants; (3) granting Georgia courts the power to "blue pencil" (i.e. judicially modify) restrictive covenants; (4) defining common terms which expands the permissible scope of certain covenants; and (5) establishing presumptively reasonable time limits for restrictive covenants.

Employee Defined

Before rolling out new agreements for your entire workforce, note that the Act does not necessarily apply to all employees. In fact, the Act specifically limits its application to covenants executed by certain employees, including:

- Executives;
- Research and development personnel or others (including independent contractors) in possession of confidential information that is important to the business of the employer;
- Those in possession of selective or specialized skills, learning, or abilities or customer contacts, customer information, or confidential information who has obtained such skills, learning, abilities, contacts, or information by reason of having worked for the employer; or
- Franchisees, distributors, lessees, licensees, or parties to a partnership agreement, or sales agents, brokers, or representatives in connection with franchise, distributorship, lease, license, or partnership agreements.

The Act specifically excludes from the definition of "employee" any employee who lacks selective or specialized skills, learning, or abilities or customer contacts, customer information, or confidential information.

Noncompete Covenants

The Act expressly authorizes noncompete covenants in employment agreements if reasonable in terms of time, geographic area, and scope of activity. However, such covenants may only be enforced following termination of employment against employees who meet one or more of the following tests:

(a) customarily and regularly solicit customers or prospects;
(b) customarily and regularly engage in making sales;
(c) have a primary duty of managing the enterprise (or a department or subdivision), 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 recommendations as to the change of status of other employees); or
(d) perform the duties of a "key employee" or of a "professional."

A "key employee" is broadly defined as an employee who, by reason of the employer's investment of time, training, money, or other factors, has gained a high level of notoriety or reputation as the employer's representative, or has gained a "high level of influence or credibility" with customers, vendors, or other business relationships. The definition also includes employees "intimately involved in the planning for or direction of the business" and those with "selective or specialized skills, learning, or abilities or customer contacts or customer information" acquired as a result of working for the employer.

A "professional" is an employee whose primary duty involves performing work requiring advanced knowledge "customarily acquired by a prolonged course of specialized intellectual instruction" or requiring talent "in a recognized field of artistic or creative endeavor."

Nonsolicit Covenants

A. Relaxed Drafting Standards

The Act also eases many of the restrictions affecting enforceability under pre-Act case law. For example, while nonsolicitation of customers covenants must remain limited to prohibiting solicitation for the purpose of providing products or services competitive with the employer's business, "no express reference to geographic area or the types of products or services considered to be competitive shall be required in order for the restraint to be enforceable."

Under the Act, a general reference to prohibiting soliciting or attempting to solicit business from customers will be presumed to apply to (1) customers or prospective customers with whom the employee had "material contact" (a term much more broadly defined under the new Act; see below), and (2) products or services competitive with (meaning the same as or similar to) those provided by the employer. Note, however, that such a relaxed drafting standard could invite litigation regarding whether a particular product or service is, in fact, competitive.

B. Broadly Defined Terms: "Material Contact" Example

As noted above, a nonsolicitation covenant under the new Act presumptively applies to any customer or prospective customer with whom the employee had "material contact." Under pre-Act case law, "material contact" is interpreted to mean contact between the employee and customer for the purpose of establishing, maintaining, or furthering a business relationship.

The new Act, however, extends the meaning to customers or prospective customers (a) "about whom the employee obtained confidential information in the ordinary course of business as a result of such employee's association with the employer; or (b) "who receives products or services authorized by the employer, the sale or provision of which results or resulted in compensation, commissions, or earnings for the employee within two years prior to the date of the employee's termination." This definition dramatically increases the scope of protection and prohibits solicitation of customers or prospects with whom the employee may never have dealt.

Nondisclosure Covenants

The Act expressly permits nondisclosure covenants protecting confidential information (information that does not rise to the level of a trade secret) to remain in effect for so long as such information remains confidential. This represents a departure from pre-Act case law where the lack of a reasonable, definitive time limit was fatal to nondisclosure covenants. Both pre-Act law and the new Act permit protection against use and disclosure of trade secrets for so long as the information constitutes a trade secret as defined by Georgia law.

Blue Penciling

The Act grants Georgia courts the authority to judicially modify covenants in employment agreements that would otherwise be too broad to enforce. Without the authority to blue pencil in the employment context prior to the Act, Georgia courts often rendered an entire covenant unenforceable on the basis of a minor drafting flaw, and if one covenant were unenforceable, it could void otherwise enforceable covenants in the same agreement.

The Act, however, appears to limit the court's new authority by defining "modification" to mean "the limitation of a restrictive covenant to render it reasonable in light of the circumstances in which it was made. Such term shall include: (a) severing or removing that part of a restrictive covenant that would otherwise make the entire restrictive covenant unenforceable; and (b) enforcing the provisions of a restrictive covenant to the extent that the provisions are reasonable." The definition thus appears to exclude the ability to rewrite or add terms to a covenant.

Presumptively Reasonable (and Unreasonable) Time Limits

Pre-Act case law provides employers no uniform standard for determining the reasonable length of a posttermination restrictive covenant. Employers only know generally that the duration of such covenants must be limited. The new Act sets definitive, presumptively reasonable, time limits. For example, for enforcement of restrictive covenants against former employees, the Act allows up to two (2) years following termination of their employment. Any such covenant for more than two (2) years following termination is presumptively unreasonable.

Next Steps

Employers should prepare to implement new contracts with employees designed to comply with and extract maximum benefit from the Act. First employers should evaluate which of their employees are subject to broader restrictions under the new Act. New contracts should include covenants that (a) restrict a broader scope of activity, including a possible noncompete restriction for appropriate employees, (b) are susceptible to judicial modification, if necessary, (c) rely on updated definitions, and (d) remain applicable for the maximum reasonable time periods post-termination.

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