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The Limited Availability to Employers of Additional Claims for Relief in Noncompetition Disputes

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April 11, 2012

The North Carolina Business Court has recently issued an opinion suggesting that, in most cases, an employer's claim for breach of a former employee's noncompetition agreement will be the employer's only possible remedy. North Carolina employers need to be aware of this limitation and take proper steps to ensure that they are able to fully protect their rights.

Losing the Valuable Employee

Almost all employers must deal with the loss of valuable employees from time to time. Many employers wisely utilize noncompetition agreements to limit the ability of key employees to directly compete against the employer immediately upon leaving. If a former employee begins to directly compete with the former employer and thereby violates a valid noncompetition agreement, the former employer can bring a lawsuit against the former employee. This is a breach of contract claim, where the particular contract happens to be the noncompetition agreement.

When a former employer brings suit for violation of a noncompetition agreement, it typically makes other legal claims as well. The employer may assert certain general "business torts" (e.g., fraud, tortious interference with contract, and tortious interference with prospective economic advantage), as well as a claim for misappropriation of trade secrets. However, a recent ruling by the North Carolina Business Court suggests that North Carolina courts are viewing these additional remedies with great skepticism in the context of standard noncompetition disputes. In most cases, a lawsuit for breach of the noncompetition agreement will be an employer's only possible remedy. North Carolina employers need to be aware of this limitation and take proper steps to ensure that they are able to fully protect their rights.

What Are "Business Torts"

"Business torts" are common law causes of action created to protect individuals and businesses in economic interactions. In some cases, the North Carolina General Assembly has expanded or modified these protections. Business torts include the following:

- Fraud: A material misrepresentation intended to be acted upon which actually deceives and harms another party;
- Negligent misrepresentation: False or incorrect information prepared without reasonable care and that is then acted upon to the harm of the misled party;

- Tortious interference with contract: Intentionally inducing a party not to perform a valid contract the party has previously made;
- Tortious interference with prospective economic advantage: Intentionally inducing a party not to enter a contract the party otherwise would have entered into;
- Unfair and deceptive trade practices : A claim based on § 75-1.1 of the North Carolina General Statutes for wrongful conduct that affects commerce and harms another party;

On their face, these claims seem perfectly applicable to various situations that commonly occur when a former employee violates a noncompetition agreement by improperly competing against the employee's former employer. For instance, former employers often want to bring claims for tortious interference with prospective economic advantage if the former employee convinces a potential customer not to enter into a business contract with the employer and instead to enter into a similar business contract with the former employee.

However, the North Carolina Business Court recently indicated in Akzo Nobel Coatings, Inc. v. Rogers that these claims are typically unavailable in situations that simply involve violations of a noncompetition agreement. The Business Court held in Akzo that there must either be some additional duty that the former employee owed to the employer – in addition to that spelled out in the noncompetition agreement – or the employer must prove that the former employee engaged in other improper acts beyond those associated with breaching the noncompetition agreement by competing against the former employer.

In the majority of noncompetition disputes, however, such additional considerations will not exist. The Business Court reasoned that the former employer's real gripe is usually simply that the former employee is competing with it even though the employee entered a noncompetition agreement promising not to do so. The Business Court is wary of allowing employers to "piggyback" other claims on top of this underlying contractual violation.

What the Future Holds

Moving forward, business torts are not going to provide any additional relief in the context of typical noncompetition disputes. Also, courts are inherently skeptical of noncompetition agreements, given the restrictions such agreements impose on freedom of employment. Courts engage in searching analysis to find any supportable basis to reject such agreements as unreasonable based on their duration, territory, and scope. In light of the fact that business tort claims will often be dismissed, it is vitally important to employers that proper, unassailably reasonable noncompetition agreements are in place. If an employer has a valid and enforceable noncompetition agreement, it will be able to successfully assert its right to stop any violations of the agreement and/or collect appropriate damages from the former employee. If not, the former employer may find its business tort claims dismissed by the court, only to discover later that it is also unable to obtain full relief under its noncompetition agreement.

Trade Secret Misappropriation

Claims for trade secret misappropriation often arise in the context of noncompetition disputes when an employee has taken commercially-valuable information from the former employer and then uses it to compete against the former employer. The North Carolina Trade Secrets Protection Act defines a trade secret as information that "derives independent actual or potential commercial value from not being generally known or readily ascertainable" and "is the subject of [reasonable] efforts…to maintain its secrecy." If someone acquires, discloses, or uses a trade secret without the proper authority or consent, the owner of the trade secret can bring a lawsuit for misappropriation.

In the same Business Court decision discussed above (and in another case this past February), the Court dismissed a claim for trade secret misappropriation based on the failure of the former employer to identify the trade secrets with "sufficient particularity." The employer had accused the former employee of misappropriating "proprietary formulas, methodologies, customer and pricing data and other confidential information concerning…fiberglass door coating products." These cases continue a growing trend in which North Carolina courts dismiss trade secret claims based on a lack of "sufficient particularity."

These Business Court trade secret decisions provide important lessons for North Carolina employers. First, it is important to know exactly what information the employer considers a trade secret. Such identification will help the employer in placing the appropriate restrictions on the distribution of the information, including monitoring exactly which employees should have access to it. Second, North Carolina courts are becoming increasingly skeptical of general business information being declared a trade secret – including basic customer information and sales data. Not all information used by a business is a trade secret. Businesses can rely only on having valid legal claims for specific types of information that they identify and treat as trade secrets. Much like claims based on the general business torts discussed above, the success of claims for trade secret misappropriation is likely to be more limited moving forward.

Conclusion

Noncompetition disputes are a fairly common occurrence in today's fluid labor markets. Business torts provide valid claims in various situations, but North Carolina courts are now indicating that such claims will be ineffective in general noncompetition disputes. Generalized claims for trade secrets also will be less successful. Employers need to be aware that the law is treating these claims with increasing skepticism and that this trend reinforces the need to comply with what have always been good business practices:

1. Ensuring that any noncompetition agreements are properly drafted and valid under North Carolina law;
2. Identifying what specific information constitutes true trade secrets; and,
3. Taking reasonable steps to protect that information.

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