

2016

Exploring the Validity of Covenants-Not-to-Compete in Nebraska

Rachel Leigh

University of Nebraska at Kearney

Follow this and additional works at: <https://openspaces.unk.edu/undergraduate-research-journal>



Part of the [Business Commons](#), and the [Law Commons](#)

Recommended Citation

Leigh, Rachel (2016) "Exploring the Validity of Covenants-Not-to-Compete in Nebraska," *Undergraduate Research Journal*: Vol. 20 , Article 4.

Available at: <https://openspaces.unk.edu/undergraduate-research-journal/vol20/iss1/4>

This Article is brought to you for free and open access by the Office of Undergraduate Research & Creative Activity at OpenSPACES@UNK: Scholarship, Preservation, and Creative Endeavors. It has been accepted for inclusion in Undergraduate Research Journal by an authorized editor of OpenSPACES@UNK: Scholarship, Preservation, and Creative Endeavors. For more information, please contact weissell@unk.edu.

Exploring the Validity of Covenants-Not-to-Compete in Nebraska

Rachel Leigh

INTRODUCTION

Covenants-not-to-compete have been an issue between employers and employees for centuries. Within the last century, it has been common for these disputes to end up in the courtroom; Nebraska is no exception. The following paper will analyze what the Nebraska Supreme Court expects from a covenant-not-to-compete in order for it to be enforceable. The three components that the courts need present in a covenant will be explained and linked with past Nebraska cases. These cases paint a clear picture for employers on what must be included in a covenant-not-to-compete for it to be upheld in court.

DEFINING COVENANTS-NOT-TO-COMPETE

Covenants-not-to-compete are also frequently referred to as noncompete agreements. These agreements are “generally part of a contract of employment or a contract to sell a business, in which the covenantor agrees for a specific period of time and within a particular area to refrain from competition with the covenantee” (Pivateau, 2008). The covenantor would be considered the employee while the covenantee the employer. This contract would usually be signed by both parties and is not intended to punish the employees upon their termination. The agreements are used to “protect the employer from unfair competition” and are primarily in place to “protect an employer’s customer base, trade secrets, and other information necessary for its success” (Pivateau, 2008).

Many people believe that covenants-not-to-compete encourage employers to invest more into their employees’ skill development. If a manager is looking to hire a new worker for a specialized job, they want to be sure that this new employee will not take the skills learned while working for this job and go work for a competitor. The noncompete agreement allows for the employer to have some faith that they will be able to protect their customer base and, to a certain extent, some of the specialized skills from being used for the benefit of a competitor (Pivateau, 2008). However, in order for this covenant-not-to-compete to be upheld in the courtroom, the agreement must be deemed reasonable.

ANALYSIS OF THE COMPONENTS OF VALID COVENANTS-NOT-TO-COMPETE

Reasonable. Whether or not a noncompete agreement is reasonable depends greatly upon the court under which it is brought. The Nebraska Supreme Court will consider an agreement reasonable if it “is ‘not injurious to the public,’ is ‘not greater than is reasonably necessary to protect the employer in some legitimate interest,’ and is ‘not unduly harsh and oppressive on the employee’” (Riekens, 1999). These three stipulations will be explained in greater detail in the following sections.

NOT INJURIOUS TO THE PUBLIC

When a court is deciding if the covenant-not-to-compete is injurious to the public, they are looking to determine if upholding the agreement is in the best interest of the public. If a covenant-not-to-compete would prevent a doctor from opening a practice in an area where there are no doctors for thirty-plus miles, then the court would probably rule that the noncompete agreement is invalid. However, very rarely will the decision to uphold the agreement come down to whether or not it is injurious to the public.

NOT GREATER THAN IS NECESSARY TO PROTECT EMPLOYER'S INTEREST

The following items cannot restrict the employee any more than is necessary to protect the employer's interests. If the Nebraska courts find any of these pieces to be overly constrictive to the employee, then they will not uphold the covenant-not-to-compete.

Geographical Area

In many cases, employers feel the need to put restrictions on the area in which a previous employee can work after their termination. There have been instances where an employee will leave a company and want to start a competing business or begin working for a competitor in the area. It is not uncommon for noncompete agreements to have a set radius for a certain amount of time in which the past employee cannot work in competition with the previous employer. The following case between National Farmers Union Service Co. and Bruce Edwards is a good example of how the Nebraska Court system will usually rule on similar cases.

Bruce Edwards entered into an agreement with National Farmers Union Service to sell insurance for them. He signed a covenant-not-to-compete that stated that he would not engage in selling insurance within 25 miles of St. Paul, Nebraska, for up to a year (*National Farmers Union Service v. Edwards*). Two years later, Edwards left the company and began selling insurance in Grand Island in competition with National Farmers Union Service. They brought suit against him for breaching the covenant-not-to-compete.

The court found the agreement to be unreasonable regardless of the fact that Grand Island, Nebraska, was less than 25 miles away from St. Paul. Due to Grand Island's large population, the court felt that the contract was unreasonable and overly broad (*National Farmers Union Service v. Edwards*). It is crucial to a Nebraska case that the noncompete agreements be extremely conservative in the stipulations that it places on employees.

Time

Time references the amount of time after the employee's termination that they are unable to be in competition with the company that they were previously working for. It is very common for the Nebraska courts to deem the noncompete agreement invalid in the areas of geographical area and length of time that it is enforceable. They will usually say that broad limitations put upon the employee are unreasonable. This next case of *Vlaslin v. Johnson and Company* is another example of this.

Neal Vlaslin was hired by Len Johnson and Company, Inc., an insurance company. Upon hiring, he was required to sign a covenant-not-to-compete. This agreement stated that upon his termination, he could not "enter into the insurance business within a 50-mile radius of the City of

Ogallala for a period of 3 years” (*Vlasin v. Johnson*). While working for Johnson and Company, Vlasin oversaw all of their accounts. After two years of working for them, he quit without notice. He then approached the court to keep Johnson from enforcing the noncompete agreement. The court deemed “the covenant was too broad and is unreasonable and unenforceable” (*Vlasin v. Johnson*). This allowed Vlasin to work in direct competition with Johnson and Company with no restrictions on time or geographical area.

Solicitation of Former Clients

In many scenarios, employers ask newly hired workers to sign a covenant-not-to-compete if they will be working with customers’ confidential information. This is to ensure that if the employee is terminated, the company has some protection if the previous employee starts contacting the customers directly asking them to partner with their new business. The court case of *Cole v. Byerly* proves a good example for this.

Kenneth Byerly worked for Dana Cole and Company, a public accounting firm. Upon assuming managerial duties, Byerly was asked to sign a noncompete agreement that stated he would not, upon termination, work with or for any business doing public accounting or any similar work for a period of two years within a 75 mile radius of Atkinson, Nebraska (*Cole v. Byerly*). Six years after beginning his work as an assistant manager, Byerly decided to quit due to not being made a partner in the time that he worked for Cole and Company.

Upon leaving the company, Byerly proceeded to open up his own accounting business in O’Neill, Nebraska, about 20 miles away. Cole and Company brought suit against Byerly, saying that he had breached his contract. They were also able to prove that in the past, when a manager quit and started their own business, they lost 40% of their client base to the new competitor (*Cole v. Byerly*). Cole and Company produced evidence that 75-80% of Byerly’s customer base were within the 75 mile radius. The Nebraska Supreme Court found these facts to be enough evidence to prove that the businesses had too much overlap and Byerly’s business “imposed a burden” upon Cole and Company in restoring their clientele (*Cole v. Byerly*). Therefore, the court upheld the covenant-not-to-compete that was signed by Byerly upon assuming his managerial duties.

An instance where the courts did not enforce a covenant-not-to-compete was in the case between Terry Whitten and Terry Malcolm. Dentist Terry Whitten owned Midlands Dental Center and employed Terry Malcolm, a recent college graduate (*Whitten v. Malcolm*). Upon hiring Malcolm, Whitten requested that he sign a noncompete agreement that stated that he could not practice dentistry within a 25-mile radius of Falls City, Nebraska, and Sabetha, Kansas, for one year following his termination (*Whitten v. Malcolm*).

Two years after signing this agreement, Malcolm began practicing dentistry with another doctor in Falls City. Whitten filed a suit against Malcolm for breaching their contract. The court ruled that because there were two separate cities listed in the noncompete agreement, the covenant was unreasonable in that “Whitten did not treat every individual in the area” and, therefore, unenforceable (*Whitten v. Malcolm*). The agreement should have restricted Malcolm from working with Whitten’s clients instead of preventing him from working in a set area, which was too broad for the court to enforce.

The courts in Nebraska are more likely to enforce a noncompete agreement when it is reasonable and in place to protect the company interests. The Nebraska Supreme Court has held that, “such a covenant may be valid only if they were non-solicitation agreements” or “if it restricts the former employee from working for or soliciting the former employer’s clients or accounts with whom the former employee actually did business and has personal contact” (Riekes, 2001).

A business that wants to take a previous employee to court for breaching a noncompete agreement should have precise information on the employee’s duties in relation to the customer information. They should also be able to prove that they have lost customers due to the past employee’s work as a competitor. An employer will have an easier time convincing a Nebraska court that the covenant-not-to-competete needs to be enforced to protect their own interests in the area of solicitation of former clients than either geographical area or time.

NOT OPPRESSIVE TO THE EMPLOYEE

The final stipulation in determining a covenant-not-to-competete reasonable or not is whether or not it is oppressive to the employee. “A restrictive covenant must not be unduly burdensome on the employee by making it difficult or impossible for him to work in any appropriate new job” (Ingram, 2002). While there are no cases in Nebraska where the courts have used this argument to find a noncompete agreement unenforceable, there have been other states that have. One case in which the court has deemed the covenant-not-to-competete reasonable and enforceable is in Illinois: *Millard Maintenance Service Co. v. Bernero*.

George Bernero had previously worked for Millard Maintenance Service Co., a janitorial contractor in Chicago, Illinois. He was a senior account executive and had signed multiple noncompete agreements (*Millard Maintenance Service Co. v. Bernero*). Upon quitting his job at Millard Maintenance Service Co., Bernero began work for a competitor, Executive Building Maintenance. Millard brought suit against Bernero, trying to enforce the noncompete agreements that he had signed. These agreements stated that Bernero could not work in competition with Millard for two years after his termination in three counties in which Millard did their primary business (*Millard Maintenance Service Co. v. Bernero*). The courts found the agreement to be enforceable due to the reasonableness of the limitations put on Bernero. They were “found to impose no unreasonable burden on the employee” (Ingram, 2002).

It is more common, however, to have a case where the courts find the noncompete agreement to be too oppressive towards the employee. Such is the case between Schlumberger Well Service and Blaker. Schlumberger Well Service fired Jerry Blaker, a division manager, after 15 years with the company (*Schlumberger Well Service v. Blaker*). Blaker had been in charge of selling Schlumberger’s wireline logging of oil and gas wells, which could be done anywhere oil was found. Upon being hired, Blaker had signed an agreement that stated that if he was terminated, he would be unable to compete with Schlumberger anywhere inside North America due to their services being so specialized (*Schlumberger Well Service v. Blaker*). “The court found that enforcing this restriction would ‘be potentially devastating to both Blaker and his family’” (Ingram, 2002).

While neither of the cases occurred in the state of Nebraska, they give good examples of how courts rule when it comes to noncompete agreements putting restrictions on past employee's ability to find work. Nebraska courts will usually rule that a covenant-not-to-compete is unreasonable if it puts unnecessary restrictions upon someone in the areas of geographical area and time.

Blue Pencil Doctrine.

In addition to ruling a noncompete agreement unreasonable and unenforceable, Nebraska courts will not allow any modifications or "blue penciling" to the agreement after it has been written. "The 'blue-pencil test' is a 'judicial standard for deciding whether to invalidate the whole contract or only the offending words'" (Pivateau, 2008). Some states are willing to "throw out" or modify the unreasonable part of the contract; while other states, such as Nebraska, will deem the entire contract as unenforceable. This is often referred to as the "no modification" approach or the "all-or-nothing rule" (Pivateau, 2008).

CONCLUSION

When looking to have an employee sign a covenant-not-to-compete, employers need to be sure that their agreement is, above all, reasonable. It must not be injurious to the public, not greater than is necessary to protect their own interests in the areas of geographical area, time, or solicitation of former clients, and not in any way oppressive to the employee. In the state of Nebraska, it is advised that a lawyer be contacted to write the agreement or look it over to ensure that all parts of the covenant are reasonable. Even if deemed reasonable by the lawyer, there is still a chance that it would not be enforced by Nebraska courts. If any part of the contract is found to be unreasonable by the courts, the entire agreement will be unenforceable due to the Blue Pencil Doctrine.

The area that would be the most persuasive for the employer to use in an attempt to persuade the courts to enforce their noncompete agreement would be in the solicitation of former clients. The employer would need to provide sound proof that their covenant-not-to-compete was protecting them from an employee taking their clients from them. They would also need to prove that the employee did indeed contact the clients and persuade them to begin doing business with them.

WORKS CONSULTED

- "Antitrust Significance of Covenants Not to Compete." *Michigan Law Review* 64.3 (1966): 503. Fenwick & West LLP. Web. 3 Dec. 2015.
- Cole v. Byerly*. Supreme Court of Nebraska. 211 Neb. 903; 320 N.W.2d 916; 1982 Neb. LEXIS 1145. LexisNexis Academic. Web. Date Accessed: 2015/12/04.
- Dow v. Gotch*. Supreme Court of Nebraska. 113 Neb. 60; 201 N.W. 655; 1924 Neb. LEXIS 279. LexisNexis Academic. Web. Date Accessed: 13 Nov. 2015.
- Ingram, John Dwight. Covenants Not to Compete. 36 Akron L. Rev. 49. (2002): 12820 words. LexisNexis Academic. Web. Date Accessed: 2015/11/25.
- Mertz v. Pharmacists Mutual Insurance Co.* Supreme Court of Nebraska. 261 Neb. 704; 625 N.W.2d 197; 2001 Neb. LEXIS 80; 143 Lab. Cas. (CCH) P59,285. LexisNexis Academic. Web. Date Accessed: 2015/12/04.
- Millard Maintenance Service Co. v. Bernero*. Appellate Court of Illinois. 207 Ill. App. 3d 736; 566 N.E.2d 379; 1990 Ill. App. LEXIS 1897; 152 Ill. Dec. 692. LexisNexis Academic. Web. Date Accessed: 2015/12/06.
- National Farmers Union Service v. Edwards*. 220 Neb. 231. Supreme Court of Nebraska. 14 June 1985. Justia Law. N.p., 2015. Web. 05 Dec. 2015.
<<http://law.justia.com/cases/nebraska/supreme-court/1985/278-4.html>>.
- Polly v. Hilderman & Company*. Supreme Court of Nebraska. 225 Neb. 662; 407 N.W.2d 751; 1987 Neb. LEXIS 935; 28 Wage & Hour Cas. (BNA) 405. LexisNexis Academic. Web. Date Accessed: 2015/12/04.
- Pivateau, Griffin Toronjo. Putting the Blue Pencil Down: An Argument for Specificity on Noncompete Agreements. 86 Neb. L. Rev. 672. (2008): 17989 words. LexisNexis Academic. Web. Date Accessed: 2015/11/25.
- Riekens, Steven J. Dead or Alive? Territorial Restrictions in Covenants-Not-to-Compete in Nebraska. 33 Creighton L. Rev. 175. (December, 1999): 12410 words. LexisNexis Academic. Web. Date Accessed: 2015/11/25.
- Riekens, Steven J. Territorial Restrictions in Covenants-Not-to-Compete in Nebraska, Part II. 35 Creighton L. Rev. 23. (December, 2001): 3182 words. LexisNexis Academic. Web. Date Accessed: 2015/11/25.
- Schlumberger Well Service v. Blaker*. United States Court of Appeals for the Seventh Circuit. 859 F.2d 512; 1988 U.S. App. LEXIS 14341. LexisNexis Academic. Web. Date Accessed: 2015/12/06.
- Swift, Kenneth. Void Agreements, Knocked-Out Terms, and Blue Pencils; Judicial and Legislative Handling of Unreasonable Terms in Noncompete Agreements. 24 Hofstra Lab. & Emp. L.J. 223. (Winter, 2007): 14019 words. LexisNexis Academic. Web. Date Accessed: 2015/12/04.
- Vlasin v. Johnson*. Supreme Court of Nebraska. 235 Neb. 450; 455 N.W.2d 772; 1990 Neb. LEXIS 178; 5 I.E.R. Cas. (BNA) 784. LexisNexis Academic. Web. Date Accessed: 2015/12/03.

Whitten v. Malcolm. Supreme Court of Nebraska. 249 Neb. 48; 541 N.W.2d 45; 1995 Neb. LEXIS 249; 11 I.E.R. Cas. (BNA) 470; 1996-1 Trade Cas. (CCH) P71,321. LexisNexis Academic. Web. Date Accessed: 2015/12/09.