

Federal Appeals Court Upholds Broad Non-competition Covenant Signed in Sale of a Business in Georgia

By Todd Van Dyke

September 20, 2010

While Georgia's appellate courts generally disapprove of restrictive covenant agreements, the Eleventh Circuit Court of Appeals has reminded potential business buyers that Georgia courts will enforce broad restrictive covenant agreements when they are entered into ancillary to the sale of a business. *Mohr et al. v. BNY Mellon*, No. 10-11890 (11th Cir. 2010).

When purchasing a business, the buyer often requires the prior owners to sign restrictive covenant agreements as part of the sale. Those agreements can prohibit the prior owners from competing or soliciting customers and employees after their employment ends. The purpose of such agreements is to protect the good will and assets of the business that is purchased. The buyer would be deprived of the benefit of the purchase if the prior owners leave, compete, and entice customers or employees to join them at their new enterprise.

Current Law

Georgia appellate courts have long held that restrictive covenant agreements entered into in the context of the sale of a business may be drafted broadly. Such covenants are reviewed under the "much lesser scrutiny afforded sale of business contracts." *Habif, Arogeti & Wynne, P.C. v. Baggett*, 498 S.E.2d 346, 353 (Ga. Ct. App. 1998). The Georgia Court of Appeals has reaffirmed this point. *Am. Control Sys., Inc. v. Boyce*, 694 S.E.2d 141, 145 and n.17 (Ga. Ct. App. 2010) (finding reasonable a covenant not to "directly, or indirectly . . . be connected with or concerned in any business enterprise or employment which shall be in competition with the business of" the purchaser).

Non-competition Covenant Upheld

In the purchase agreement and in their employment agreements, two former employees agreed not to compete against the buyer, BNY Mellon. The purchase agreement provided that the employees would not compete against the corporation "in any capacity" within 50 miles of any city listed on an attached schedule for 12 months after termination or resignation. The schedule listed 27 cities in Georgia and South Carolina and 16 cities in 12 other states. In the event the corporation ended its business activities in a particular city, the covenant stated that the city would be eliminated from the schedule. The employment agreements cross-referenced the non-competition covenant in the purchase agreement.

Two days after their resignation, the former employees filed a complaint requesting a declaratory judgment that the restrictive covenants were "invalid and unenforceable . . . under Georgia law" and an injunction to prevent the corporation from enforcing the covenants.

The former employees argued the non-competition covenant was overly broad and unenforceable because it prohibited them from working for a competitor in any capacity. They argued the territorial limitation in the covenant was too vague to be enforceable and they did not have contacts in all of the cities listed on the schedule. The District Court agreed with the former employees and held the covenant was unenforceable. The appeals court reversed. The Court held the covenant was the product of an arms' length negotiation between the corporation and the former employees and, therefore, the covenant was entitled to substantial protection and latitude. The Court held the former employees specifically negotiated the terms of the covenant and agreed in the purchase agreement that it was reasonable under the circumstances.

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The Court noted the former employees agreed in the purchase agreement that the geographic territory was reasonable and an integral and essential part of the sale of the business. The Court held that Georgia law does not require exact precision in the statement of the geographic territory, and the territory (in the context of the sale of a business) is determined by the territory served by the employer, not the employee. Lastly, in the event the corporation no longer does business in any of the cities listed on the schedule, the Court held the District Court need only blue pencil, or strike, those cities from the schedule.

For these reasons, the Eleventh Circuit returned the case to the District Court with instructions to enter a preliminary injunction against the former employees that enforces the non-competition covenant.

New Legislation

Mohr shows just how difficult it can be to enforce restrictive covenants in Georgia. The procedural history of the case shows the District Court twice held the non-competition covenant unenforceable, and the Eleventh Circuit twice reversed — showing that reasonable minds can differ under Georgia's current rules.

Employers may soon get some relief from those rules. The Georgia Legislature has enacted new [law](#) (OCGA § 13-8-56) with principles for determining the reasonableness of restrictive covenants. *See* Ga. L. 2009, p. 231. Thus, the legislature recognizes that restrictive covenants in employment contracts serve to protect legitimate business interests.

The statute, however, will become effective only if an amendment to the Georgia Constitution passes voter approval in the November 2010 general election. *See* Ga. L. 2009, p. 231, § 4.

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