Non-compete Laws: North Carolina

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A Q&A guide to non-compete agreements between employers and employees for private employers in North Carolina. This Q&A addresses enforcement and drafting considerations for restrictive covenants such as post-employment covenants not to compete and non-solicitation of customers and employees. Federal, local or municipal law may impose additional or different requirements. Answers to questions can be compared across a number of jurisdictions (see *Non-compete Laws: State Q&A Tool (http://us.practicallaw.com/1-505-9589)*).

OVERVIEW OF STATE NON-COMPETE LAW

1. If non-competes in your jurisdiction are governed by statute(s) or regulation(s), identify the state statute(s) or regulation(s) governing:

- Non-competes in employment generally.
- Non-competes in employment in specific industries or professions.

GENERAL STATUTE AND REGULATION

Chapter 75 of the North Carolina General Statutes generally prohibits contracts that restrain trade or commerce and imposes statutory requirements for permissible restraints.

INDUSTRY- OR PROFESSION-SPECIFIC STATUTE OR REGULATION

Attorneys: N.C.R. of Prof'l Conduct 5.6

Rule 5.6 of the North Carolina Rules of Professional Conduct governs non-competes in the legal industry.

Locksmiths: 21 N.C. Admin. Code 29.0502(e)(5)

Title 21, Section 29.0502(e)(5) of the North Carolina Administrative Code governs non-solicitation and non-compete agreements for locksmiths.

2. For each statute or regulation identified in *Question 1*, identify the essential elements for non-compete enforcement and any absolute barriers to enforcement identified in the statute or regulation.

GENERAL STATUTE AND REGULATION

Contracts that restrain trade or commerce are generally illegal (*N.C. Gen. Stat. Ann. § 75-1*).

Agreements limiting a person's right to do business in North Carolina must be both:

- In writing.
- Signed by the party agreeing not to do business.

(*N.C. Gen. Stat. Ann. § 75-4.*)

INDUSTRY- OR PROFESSION-SPECIFIC STATUTE OR REGULATION

Attorneys: N.C.R. Prof'l Conduct 5.6

A lawyer cannot offer or make:

- A partnership, shareholders, operating, employment or other similar type of agreement that restricts the right of a lawyer to practice after termination of the relationship, except an agreement concerning benefits upon retirement.
- An agreement restricting a lawyer's right to practice as part of a settlement between private parties.

(*N.C.R. Prof'l Conduct 5.6.*)

Locksmiths: 21 N.C. Admin. Code 29.0502(e)(5)

Locksmiths cannot directly solicit customers in violation of a non-compete agreement (*21 N.C. Admin. Code 29.0502(e)(5)*).

ENFORCEMENT CONSIDERATIONS

3. If courts in your jurisdiction disfavor or generally decline to enforce non-competes, please identify and briefly describe the key cases creating relevant precedent in your jurisdiction.

Non-competes are disfavored in North Carolina (*Med. Staffing Network v. Ridgeway, 670 S.E.2d 321, 327 (N.C. Ct. App. 2009)*).

However, courts enforce non-competes that are:

- In writing.
- Part of an employment contract.
- Based on valuable consideration (see *Question 8*).
- Reasonable about time and territory (see *Questions 9 and 10*).
- Designed to protect a legitimate business interest.

(*Copypro, Inc. v. Musgrove, 754 S.E.2d 188, 191-92 (N.C. Ct. App. 2014)*.)

North Carolina courts refuse to enforce non-competes that are against the state's public policy (*United Labs., Inc. v. Kuykendall, 370 S.E.2d 375, 380 (N.C. 1988)*).

LEGITIMATE BUSINESS INTEREST

Employers have a legitimate business interest in protecting their unique assets, including:

- Customer contacts.
- Confidential information.

However, employers cannot protect their interests in a way that causes unreasonable hardship for employees. (*Copypro, 754 S.E.2d at 192*.)

Non-competes should be narrowly tailored to protect employers' legitimate business interests. Non-competes that prohibit employees from working in a capacity that is unrelated to the employees' former job are overly broad and unenforceable. (*Copypro, 754 S.E.2d at 192; Horner Int'l Co. v. McKoy, 754 S.E.2d 852, 857 (N.C. Ct. App. 2014); VisionAIR, Inc. v. James, 606 S.E.2d 359, 362 (N.C. Ct. App. 2004)*.)

Customer-based restrictions cannot extend beyond the customers with which the former employee had business contact (*Farr Assocs. v. Baskin, 530 S.E.2d 878, 882-83 (N.C. Ct. App. 2000)*).

North Carolina courts might not enforce non-competes that prohibit direct or indirect competition because they restrict too many activities (*VisionAIR, 606 S.E.2d at 362-63*).

4. Which party bears the burden of proof in enforcement of non-competes in your jurisdiction?

The party seeking to enforce a non-compete has the burden of proving that the agreement is reasonable (*Outdoor Lighting Perspectives Franchising, Inc. v. Harders, 747 S.E.2d 256, 264 (N.C. Ct. App. 2013)*).

5. Are non-competes enforceable in your jurisdiction if the employer, rather than the employee, terminates the employment relationship?

Courts are likely to enforce reasonable non-competes when the employer terminates the employment relationship. For example, in *Masterclean of N.C., Inc. v. Guy*, an employer filed a motion for a preliminary injunction against a discharged employee to enforce a non-compete agreement. The court denied the motion, but only because the scope of the agreement was not reasonable. (*345 S.E.2d 692, 696 (N.C. Ct. App. 1986)*).

If, however, the termination of employment is a material breach of contract, then an employee's performance under the non-compete may be excused (*Millis Constr. Co. v. Fairfield Sapphire Valley, 358 S.E.2d 566, 569-70 (N.C. Ct. App. 1987)*).

BLUE PENCILING NON-COMPETES

6. Do courts in your jurisdiction interpreting non-competes have the authority to modify (or "blue pencil") the terms of the restrictions and enforce them as modified?

North Carolina courts may modify or blue pencil an unreasonable non-compete restriction by deleting severable parts of the agreement to make the restriction reasonable. However, courts cannot otherwise revise or rewrite non-competes, and non-compete restrictions that are too broad are not rewritten or enforced. (*Whittaker Gen. Med. Corp. v. Daniel, 379 S.E.2d 824, 828 (N.C. 1989); Hartman v. W.H. Odell & Assocs., 450 S.E.2d 912, 920 (N.C. Ct. App. 1994)*.)

CHOICE OF LAW PROVISIONS

7. Will choice of law provisions contained in non-competes be honored by courts interpreting non-competes in your jurisdiction?

Choice of law provisions in non-competes generally are enforced (*Bueltel v. Lumber Mut. Ins. Co., 518 S.E.2d 205, 209 (N.C. Ct. App. 1999)*). However, North Carolina courts do not enforce a choice of law provision if:

- The law is contrary to North Carolina's public policy.
- North Carolina has a greater interest in the determination of the particular issue.
- North Carolina's law would apply in the absence of an effective choice of law provision.

(*Szymczyk v. Signs Now Corp., 606 S.E.2d 728, 732 (N.C. Ct. App. 2005)*.)

For more on choice of law provisions, see *Practice Note, Choice of Law and Choice of Forum: Key Issues (http://us.practicallaw.com/7-509-6876)*.

REASONABLENESS OF RESTRICTIONS

8. What constitutes sufficient consideration in your jurisdiction to support a non-compete agreement?

Under North Carolina law, sufficient consideration for a non-compete includes:

- The promise of new employment (*Farr Assocs., 530 S.E.2d at 881*).
- A change in the terms and conditions of employment, including:
  - a raise in pay;
  - a new job assignment;
  - a promotion; or
  - a bonus.

  (*Whittaker, 379 S.E.2d at 827; Hejl v. Hood, Hargett & Assocs., 674 S.E.2d 425, 428-29 (N.C. Ct. App. 2009)*.)

While continued at-will employment alone is insufficient consideration, an offer of continued employment for a specified duration may be sufficient consideration (*Cox v. Dine-A-Mate, Inc., 501 S.E.2d 353, 356 (N.C. Ct. App. 1998)*; *Amdar, Inc. v. Satterwhite, 246 S.E.2d 165, 167 (N.C. Ct. App. 1978)*).

9. What constitutes a reasonable duration of a non-compete restriction in your jurisdiction?

North Carolina courts consider time and territory together when determining whether a non-compete is reasonable, so that a longer restricted duration is acceptable when the geographic scope of the restriction is small and vice versa (*Kinesis Advertising, Inc. v. Hill, 652 S.E.2d 284, 294 (N.C. Ct. App. 2007)*).

Courts have considered six-month to three-year restrictions reasonable, depending on the geographic restrictions. Restrictions of five years or more are presumed to be unreasonable (*Farr Assocs., 530 S.E.2d at 881*). For example, in:

- *Market America, Inc. v. Christman-Orth*, the court held that a potentially nationwide restriction was acceptable where it only lasted for six months (*520 S.E.2d 570, 577-78 (N.C. Ct. App. 1999)*).
- *Precision Walls, Inc. v. Servie*, the court held that a one-year restriction was reasonable where it prohibited a former employee from working in a specific industry in two states (*568 S.E.2d 267, 272-73 (N.C. Ct. App. 2002)*).
- *Forrest Paschal Machinery Co. v. Milholen*, the court held that a two-year, 350-mile restriction was reasonable (*220 S.E.2d 190, 196-97 (N.C. Ct. App. 1975)*).
- *Hartman v. W.H. Odell & Associates*, the court held that a five-year restriction from the date of termination could be supported only by extreme conditions and a ten-year restriction was patently unreasonable (*450 S.E.2d 912, 917-18 (N.C. Ct. App. 1994)*).

Depending on the circumstances, non-competes that accompany the sale of a business may be enforced for longer periods of time (*Jewel Box Stores Corp. v. Morrow, 158 S.E.2d 840, 843-44 (N.C. 1968)*).

10. What constitutes a reasonable geographic non-compete restricion in your jurisdiction?

North Carolina courts consider time and territory together, so that a longer restricted duration is acceptable when the geographic scope of the restriction is small and vice versa (*Kinesis, 652 S.E.2d at 294*). North Carolina courts consider several factors to determine whether a geographic restriction is reasonable, including:

- The area or scope of the restriction.
- The area assigned to the employee.
- The area where the employee actually worked.
- The area where the employer operated.
- The nature of the employer's business.
- The nature of the employee's job and her knowledge of the employer's business operation.

(*Kinesis, 652 S.E.2d at 294*.)

To demonstrate the reasonableness of the geographic restriction in a non-compete designed to protect customer relationships, an employer must show:

- Where its customers are located.
- The extent of its business in those locations.
- Why the restriction's geographic scope was necessary to protect those customer relationships.

(*Kinesis, 652 S.E.2d at 294*; *Hartman, 450 S.E.2d at 917*.)

11. Does your jurisdiction regard as reasonable non-competes that do not include geographic restrictions, but instead include other types of restrictions (such as customer lists)?

Customer non-solicitation restrictions are enforceable in North Carolina (*Whittaker, 379 S.E.2d at 826*). Non-solicitation restrictions are analyzed the same way as non-competes (*Triangle Leasing v. McMahon, 393 S.E.2d 854, 857 (N.C. 1990)*).

Customer-based non-solicitation restrictions cannot extend beyond the customers with which the former employee had a business contact (*Farr Assocs., 530 S.E.2d at 882; Hejl, 674 S.E.2d at 430*).

12. Does your jurisdiction regard as reasonable geographic restrictions (or substitutions for geographica restrictions) that are not fixed, but instead are contingent on other factors?

North Carolina courts have allowed restrictions that are contingent on factors such as where the employee worked or where the business is located. For example, in:

- *Lloyd v. Southern Elevator Co.*, the court enforced a non-compete restricting a former employee from competing in any:
  - county in which he had worked during the two years before termination; and
  - location within 100 miles of the boundaries of those counties.

(*No. COA06-994, 2007 WL 1892500 (N.C. Ct. App. July 3, 2007)*.)

- *Lockhart v. Home-Grown Industries of Georgia, Inc.*, the court enforced a two-year non-compete prohibiting individual franchisees of a restaurant chain from operating either:
  - up to five miles from the chain's restaurants; or
  - within a specified distance of other franchisees.

(*No. 3:07-CV-297, 2007 WL 2688551 (W.D.N.C. Sept. 10, 2007)*.)

13. If there is any other important legal precedent in the area of non-compete enforcement in your jurisdiction not otherwise addressed in this survey, please identify and briefly describe the relevant cases.

INDEPENDENT CONTRACTORS

Independent contractors, like employees, may be bound by reasonable non-compete restrictions (*Market Am., Inc., 520 S.E.2d at 578*).

FORFEITURE AND PAYMENT PROVISIONS

Agreements for employees to forfeit benefits if they compete with their employers are not analyzed as non-competes because they are

not restraints of trade (*Newman v. Raleigh Internal Med. Assocs., 362 S.E.2d 623, 626 (N.C. Ct. App. 1987)*).

Additionally, agreements for employees to make a payment if they compete with their employers are not analyzed as non-competes because they are not restraints of trade. However, the payment provision must be an enforceable liquidated damages provision and not a penalty. (*Eastern Carolina Internal Med., P.A. v. Faidas, 564 S.E.2d 53, 55-57 (N.C. Ct. App. 2002)*.)

AFFILIATES

A non-compete prohibiting employment with a former employer's affiliates may be unenforceable as overly broad because affiliates may be in different industries and the prohibition would serve no legitimate business purpose (*Med. Staffing Network, 670 S.E.2d at 327-28*).

ASSIGNMENT

Non-competes generally may be assigned (*Kennedy v. Kennedy, 584 S.E.2d 328, 332 (N.C. Ct. App. 2003)*; *Keith v. Day, 343 S.E.2d 562, 568 (N.C. Ct. App. 1986)*).

However, an assignment that substantially changes the nature and extent of performance may make a contract unenforceable (*Kraft Foodservice, Inc. v. Hardee, 457 S.E.2d 596, 598-99 (N.C. 1995)*; *Webber v. McCoy Lumber Co., 303 S.E.2d 408, 410 (N.C. Ct. App. 1983)*; *Westpoint Stevens, Inc. v. Panda-Rosemary Corp., No. 99-CVS-9818, 1999 WL 33545512, at *9-10 (N.C. Super. Dec. 16, 1999)*).

SALE OF ASSETS

When assets are sold, the new owner has the right to enforce employment agreements, including non-competes. However, if the new owner does not negotiate new agreements, the restrictive period begins to run at the time of the asset sale (*Covenant Equip. Corp. v. Forklift Pro, Inc., No. 07CVS21932, 2008 WL 1945973, at *9 (N.C. Super. May 1, 2008)*).

STOCK SALE

A non-compete is enforceable by an entity acquiring the agreement through a stock purchase (*Phillips Elecs. N. Am. Corp. v. Hope, 631 F. Supp. 2d 705, 713-14 (M.D.N.C. 2009)*; *Covenant Equipment Corp., 2008 WL 1945973, at *9 n.11*).

REMEDIES

14. What remedies are available to employers enforcing non-competes?

Employers enforcing non-competes are entitled to:

- Injunctive relief (*A.E.P. Indus. v. McClure, 302 S.E.2d 754, 759-60 (N.C. 1983)*).
- Damages, including lost profits (*S. Bldg. Maint., Inc. v. Osborne, 489 S.E.2d 892, 895 (N.C. Ct. App. 1997)*).
- Liquidated damages, if the contract includes an enforceable liquidated damages provision (*Iredell Digestive Disease Clinic, P.A. v. Petrozza, 373 S.E.2d 449, 450-53 (N.C. Ct. App. 1988)*, aff'd, *377 S.E.2d 750 (N.C. 1989)*).

15. What must an employer show when seeking a preliminary injunction for purposes of enforcing a non-compete?

To obtain a preliminary injunction, an employer must show that the employer is likely to:

- Succeed on the merits of the case.
- Suffer irreparable loss unless the injunction is issued.

(*A.E.P. Indus., 302 S.E.2d at 759-60*.)

OTHER ISSUES

16. Apart from non-competes, what other agreements are used in your jurisdiction to protect confidential or trade secret information?

Other types of agreements used in North Carolina to protect confidential or trade secret information include:

- Non-solicitation.
- Confidentiality.
- Invention assignment.

17. Is the doctrine of inevitable disclosure recognized in your jurisdicion?

North Carolina courts have not adopted the doctrine of inevitable disclosure (*Analog Devices, Inc. v. Michalski, 579 S.E.2d 449, 454-55 (N.C. Ct. App. 2003)*; *Allegis Grp., Inc. v. Zachary Piper LLC, No. 12 CVS 2984, 2013 WL 709581, at *11 (N.C. Super. Feb. 25, 2013)*).

In 1996, a federal court predicted that North Carolina courts would enjoin threatened misappropriation of trade secrets based on the inevitable disclosure doctrine if both:

- The injunction was limited to preventing the disclosure of clearly identified trade secrets of significant value.
- The likelihood of disclosure could be shown by the degree of similarity between the employee's current and former positions, as well as the value of the information.

(*Merck & Co. v. Lyon, 941 F. Supp. 1443, 1460 (M.D.N.C. 1996)*.)

The court further predicted that North Carolina courts would not enjoin competitive employment based on the inevitable disclosure doctrine absent a showing of bad faith or underhanded dealing and that the competitor lacked comparable levels of knowledge and achievement (*Merck, 941 F. Supp. at 1460 n.5 and n.6*).