Key Considerations for Buyers

A review of this decision and other cases leads to a conclusion that had the non-competition covenant in the purchase documentation been drafted differently, the buyer may have achieved its aims by keeping the employee from competing during the one year after his employment ended. For example, the Fillpoint decision distinguished an earlier decision in Alliant Ins. Servs. v. Gaddy which upheld identical covenants in a purchase agreement and an employment agreement which applied for the later of five years following the purchase or two years after termination of the employee’s employment with the new company.

When drafting non-compete agreements, buyers and their counsel should consider the following:

- **Integrate, Integrate, Integrate.** It is critically important that the various transactional documents appropriately reference each other, particularly if non-compete covenants are contained in documents outside of the Purchase Agreement. The covenants in different deal documents should also be consistent with each other. One of the factors which may have influenced the decision in Fillpoint was the fact that Maas had already satisfied his non-compete in his purchase agreement. Accordingly, the buyer had to justify separate and different non-compete provisions in the employment agreement. Had the provisions been consistent with each other, it would not have faced this battle.

- Make Your Case for Enforcement in the Deal Documents. The non-compete provisions should be drafted with an eye towards subsequent legal challenge and should make the case themselves as to their absolute necessity to protect the acquired business’s goodwill. This can be done through a number of means including, recitals confirming that the purpose of the non-compete is to protect the goodwill and the reasonableness of the provisions in doing so, closing conditions and other provisions which make clear the buyer would not have closed on the purchase without these essential protections, and allocating part of the deal consideration to goodwill.

- Don’t be Greedy. Buyers should not overreach by barring sellers from activities beyond the scope of the statutory exception. The courts will take umbrage at covenants which not only bar solicitation of the customers and employees of the acquired business but which cast a broader net to all of the buyer’s employees and customers. Practitioners sometimes take a reflexive comfort that courts will look favorably upon non-compete agreements with overbroad or omit restrictions and make them enforceable by providing reasonable limitations. However, California courts will not go so far as striking a new bargain for the purposes of saving an already-adequate covenant. As stated by the Court in Strategic, “had the parties intended to reach such a limited – and enforceable – covenants, they could have negotiated for them. We will not do so for the parties now.”

Conclusion

The law governing non-competes in California mergers and acquisitions serves as another example that careful thought and analysis is requisite to accomplish the parties’ objectives and to implement their bargained agreements. Parties who proceed without understanding what courts will permit and who overreach do so at their peril.

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