

Blue Pencil Doctrine and the Enforceability of Noncompete and Nonsolicitation Agreements

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In *LTD v. Herman*, 2019 COA 113 (No. 18CA0950), the court addressed an issue of first impression in Colorado – when, if ever, is a court required to blue pencil¹ a noncompete or nonsolicitation agreement to comply with Colorado law.

Factual Background

Herman worked as a legal recruiter for 23 LTD, d/b/a Bradsby Group (Bradsby). When she was hired, Herman signed an employment agreement with noncompete and nonsolicitation provisions. Bradsby terminated Herman’s employment after several years, and shortly thereafter Herman founded a company that focused on law firm succession planning. She also performed legal recruiting services similar to her former role at Bradsby.

Following the start of her new business, Herman reached out to a lawyer that she initially contacted as a potential candidate while at Bradsby to see if anyone in the lawyer’s network would be interested in an open position she was working on. The lawyer then inquired whether a different position, which Herman had tried to fill while at Bradsby, was still open. Herman inquired with the law firm, which was a Bradsby client, and the law firm ultimately hired the lawyer and paid Herman (through her business) \$12,000 for her role in the hiring. When Bradsby learned about Herman’s role in this placement, Bradsby sued her for breach of the noncompete and nonsolicitation provisions, arguing that enforcement of those provisions was necessary to protect its trade secrets.

Overview of Colorado Noncompete Law

In general, agreements not to compete, with some narrow exceptions, are contrary to the public policy of Colorado. The public policy underlying the unenforceability of noncompetition provisions is a prohibition on the restraint of trade or the right to make a living. Further, courts have held that a nonsolicitation agreement is a form of noncompete agreement.

There are exceptions to the general rule. One exception is C.R.S. § 8-2-113(2)(b), which provides that the prohibition against covenants not to compete that restrict the right of any person to receive compensation for performance of skilled or unskilled labor for any employer, shall not apply to: “[a]ny contract for the protection of trade secrets.” However, Colorado courts have held that an enforceable noncompete provision under a statutory exception still requires that such limitation is reasonable and narrowly drafted.

The Contract Provisions

¹ The court in this case noted that while some courts use the term “blue penciling” to refer only to the removal of words from a noncompete or nonsolicitation provision without modifying or adding any other terms, here the court joins other courts and uses the term to refer to any modification of a noncompete or nonsolicitation provision by a court.

In *LTD*, the noncompete provision states, in relevant part:

“Upon termination of his/her employment with Bradsby, Account Executive . . . shall not . . . within the Restricted Area for a period of twelve (12) months from the date of termination of employment become an owner, partner, investor, or shareholder in any entity that competes with Bradsby without prior written consent of Bradsby”

The agreement defines the “Restricted Area” as any place “within 30 miles of Bradsby’s principal place of business,” which is located in downtown Denver.

The nonsolicitation provision states, in pertinent part:

“Upon termination of his/her employment with Bradsby, Account Executive . . . shall not within the Restricted Area, for a period of twelve (12) months from the date of termination of employment, contact or solicit the business of any person, entity, applicant, client, employer or prospective employer who Bradsby has contacted or solicited during the twelve (12) months prior to the Account Executive’s termination”

The agreement also included a severability clause, which states (emphasis added):

“In the event that any portion of this Agreement shall be held unenforceable, it is agreed that the same shall not affect any other portions of this Agreement, and the remaining covenants and restrictions or portions thereof shall remain in full force and effect; *further, if the invalidity or unenforceability is due to the unreasonableness of the time or geographical area covered by a covenant and restriction, the covenants and restrictions shall nevertheless be effective for the period of time and for such area as may be determined to be reasonable by a court of competent jurisdiction.*”

Procedural History

At the district court level, a jury determined that Herman had not breached the noncompete provision, presumably based on evidence presented at trial that Herman’s company was not primarily a recruiting company and that any recruiting work was undertaken outside the Restricted Area. But the jury returned a verdict in favor of Bradsby on the nonsolicitation claim and awarded nominal damages of one dollar. The district court set aside that verdict and entered judgment in favor of Herman holding that the nonsolicitation provision violates Colorado law and the court declined to narrow (i.e. “blue pencil”) the provision to render it enforceable.

On appeal, Bradsby argued that the district court erred in declining to blue pencil the nonsolicitation provision because the severability section of the agreement obligated the court to do so or alternatively, if the agreement did not actually require the court to blue pencil the agreement, the court abused its discretion in declining to do so.

Analysis and Holding

The court rejected the proposition that contracting parties, by inclusion of language in a contract, may compel a court to blue pencil an agreement that violates Colorado public policy. The court held that

while a trial court has broad discretion to blue pencil an offensive restrictive covenant, parties to an agreement cannot contractually obligate a court to blue pencil noncompete or nonsolicitation provisions to render unenforceable terms enforceable.

The court also rejected Bradsby's argument that even if the court was not compelled to blue pencil the agreement, it abused its broad discretion in declining to do so because its decision was not manifestly arbitrary, unfair, or unreasonable, or contrary to law. The court held that it is the obligation of a party who has, and wishes to protect, trade secrets to craft contractual provisions that do so without violating Colorado public policies. Thus, the district court did not err in declining to blue pencil this agreement.

The court went on to note that, even if private parties could require a court to correct their contracts, the contract in this case does not do so. Specifically, the pertinent portion of the severability clause provides (emphasis added):

“[I]f the invalidity or unenforceability is *due to the unreasonableness of the time or geographical area covered by a covenant and restriction*, the covenants and restrictions shall nevertheless be effective for the period of time and for such area as may be determined to be reasonable by a court of competent jurisdiction.”

As noted by the district court, any conceivable mandatory duty (which this court rejected) to blue pencil the contract is limited to correcting overbreadth in the agreement's geographic and temporal restrictions. Those restrictions are not at issue. The fact that the severability provision specifically authorizes a court to modify the geographic and temporal restrictions suggests, if anything, that only those two restrictions were intended to be subject to modification by a court.

Takeaway

In the author's opinion, there are two drafting lessons to be learned from this case:

First, enforceable noncompete and nonsolicitation provisions must be narrowly drafted to be reasonable in all respects, not just in duration and geographic scope. It would be a risky policy to draft an overly broad noncompete or nonsolicitation provision in reliance on a court to blue pencil the agreement as a backstop. If tested, a court may decline to exercise its broad discretion to blue pencil the agreement.

Second, consider whether your severability clause is broad enough. While it may not have changed the outcome of this case, the court noted that Bradsby's argument would have been stronger if the severability clause provided for “blue penciling” of more than just the geographic and temporal restrictions, which were not at issue in this case.