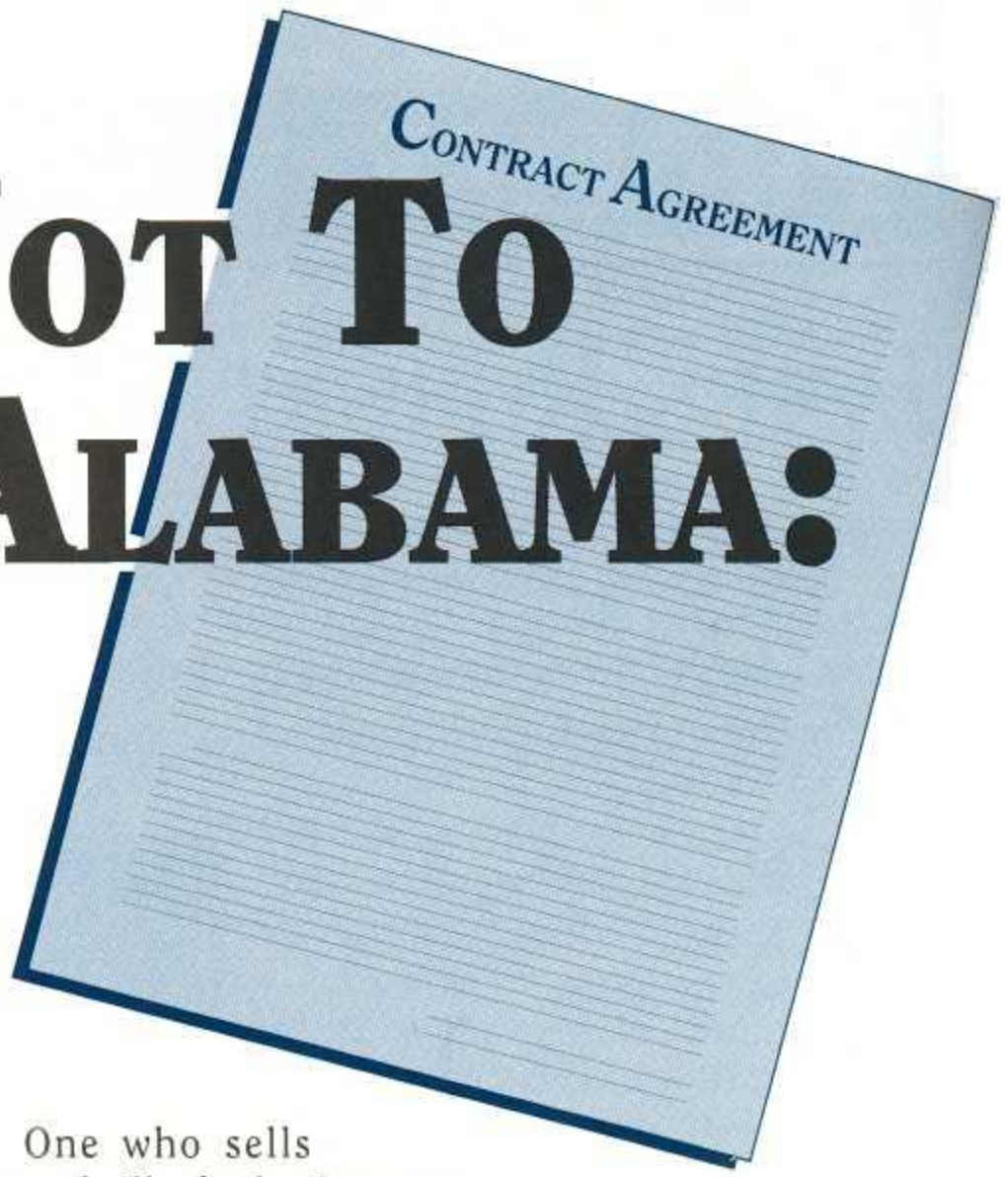
COVENANTS NOT TO COMPETE IN ALABAMA: REVISITED[1]



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This article discusses situations in which one person covenants or contracts with another not to compete. The enforceability of such agreements is restricted by statute in Alabama and many other states.[2] Even when the covenant is of a type expressly allowed by the Alabama statute,[3] it still is subject to a judicially adopted test of reasonableness.

This article presents examples of different situations in which such agreements have been used and subsequently considered by the courts. However, the reader should remember that there is no paucity of authority in this area. In just the last ten years, the Alabama Supreme Court has decided over 35 of these cases. As one court noted regarding the law on this subject:

> This is not one of those questions on which the legal researcher cannot find enough to quench his thirst. To the contrary there is so much authority it drowns him. It is a sea — vast and vacillating, overlapping and bewildering. One can fish out of it any kind of strained support for anything, if he lives so long. This deep and unsettled sea pertaining to an employee's covenant not to compete with his employer after termination of employment is really Seven Seas . . ..[4]

At least one judge faced with the duty of deciding a case involving a covenant not to compete declined to embark upon this "Seven Seas" of authority:

> Because of a demanding caseload, family responsibilities and a desire to consider other matters in life, this court has been dissuaded from reading all of the available authorities.[5]

The Alabama statute applicable to covenants not to compete provides:

> (a) Every contract by which anyone is restrained from exercising a lawful profession, trade or business of any kind otherwise than is provided by this section is to that extent void.
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> (b) One who sells the goodwill of a business may agree with the buyer and one who is employed as an agent, servant or employee may agree with his employer to refrain from carrying on or engaging in a similar business and from soliciting old customers of such employer within a specified county, city or part thereof so long as the buyer, or any person deriving title to the goodwill from him, or employer carries on a like business therein.
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> (c) Upon or in anticipation of a dissolution of the partnership, partners may agree that none of them will carry on a similar business within the same county, city or town, or within a specified part thereof, where the partnership business has been transacted.[6]

The statute begins in subsection (a) by declaring void *all* contracts by which anyone is restrained from exercising a lawful profession, trade or business. In analyzing a situation involving a covenant not to compete governed by Alabama law, one generally should begin with the proposition that all such covenants are void, *except* as subsections (b) or (c) exempt the covenant from the blanket prohibition of subsection (a). One also should consider whether the covenant can be characterized as a lawful partial restraint or forfeiture provision not governed by the Alabama statute.

Of course, actions on contracts containing covenants not to compete, in addition to satisfying the Alabama statute, are subject to the same defenses as any other contract action. For example, a party seeking to enforce a contract containing a covenant not to compete must have been qualified to do business in Alabama at the time the covenant was executed.[7] Likewise, to be enforceable the covenant must be mutually binding and provide consideration to both parties. In *Hill v. Rice,*[8] the employee dance instructor agreed not to compete after termination of his employment, but the employer in the contract did not agree to provide the employee with any minimum hours or compensation. The Alabama Supreme Court held

that the contract lacked mutuality at its inception and remanded the case to the circuit court for a determination as to whether reasonable employment in fact had been provided to the employee before termination of the relationship.

However, merely because a covenant is made at some point after employment commences does not necessarily render it invalid for lack of consideration. In *Daughtry v. Capital Gas Co.*,[9] a gas company sued its former branch manager-routeman to enforce a covenant signed after employment had commenced. The employment continued for eight months after execution of the covenant, at which time the employee left voluntarily. The court held that the "continued employment" of the employee constituted sufficient consideration.[10]

While this article focuses primarily on the validity of covenants not to compete, practitioners should be aware that litigation in this area often includes other claims arising out of the employment relationship and its termination. For example, in *James S. Kemper & Co. Southeast, Inc. v. Cox & Associates, Inc.*,[11] the former employer sued its former employee and his new employer, asking for injunctive relief to enforce the covenant, damages against the former employee for breach of contract, and damages against the new employer for knowing and intentional interference with the covenant. The Supreme Court of Alabama ruled that (1) the covenant was enforceable by injunction, (2) the former employee was liable for damages for breach of contract, and (3) the new employer was liable for damages for intentional and knowing interference with the contractual relationship between the plaintiff former employer and its former employee.

For purposes of discussion, the covenants *not* disallowed by the Alabama statute may be divided into three categories: (1) employee-employer, (2) sale of the goodwill of a business or partnership dissolution, and (3) partial restraints and forfeiture provisions.

EMPLOYER-EMPLOYEE COVENANTS

Frequently, as a condition of employment or otherwise, employees will agree not to compete with their employers after termination of their employment. Alabama courts view such restraints with disfavor "because they tend not only to deprive the public of efficient service, but tend to impoverish the individual."[12] As the Alabama Supreme Court declared in *Calhoun v. Brendle, Inc.*,[13] "One does not have an unfettered right to be free of competition in this country, and contracts which seek to restrain one in the exercise of his right to practice a lawful trade or profession are disfavored."

Consistent with the court's general attitude toward post-employment restraints, the employment exception to the general prohibition of all contracts in restraint of trade is narrowly construed. For example, Alabama courts will not enforce a contract provision restricting the practice of a profession. This refusal to enforce such contracts is based on the court's interpretation of subsection (a) to the Alabama statute which provides:

> Every contract by which anyone is restrained from exercising a lawful profession . . . otherwise than is provided by this section is to that extent void.

Neither subsection (b) nor subsection (c) of the statute exempt contracts restricting the practice of a "profession." Applying this interpretation, the Alabama Supreme Court consistently has refused to enforce post-employment restrictions signed by professionals.

In defining what is a "profession" and who are "professionals," the Supreme Court of Alabama has referred to the late Dean Roscoe Pound's definition found in the *Lawyer from Antiquity to Modern Times:*

> The term refers to a group of men pursuing a learned art as a common calling in the spirit of a public service — no less a public service because it may incidentally be a means of livelihood. Pursuit of the learned art is the purpose. Gaining a livelihood is incidental, whereas, in a business or trade it is the entire purpose.[14]

The callings the court has defined as "professions" include physicians,[15] veterinarians,[16] and certified public accountants,[17] as well as public accountants.[18] However, in *Dobbins v. Getz Exterminators of Alabama, Inc.*, the court, noting that "there are multitudes of businesses but few professions," rejected the argument that pest control technicians were professionals by virtue of a statute referring to them as "persons engaged in professional services."

The court also has construed the wording of the Alabama statute, which allows restrictive covenants only as to "an agent, servant or employee," to preclude the enforceability of covenants entered into by independent contractors and sales agents.[20] In *Premier Industrial Corp. v. Marlow,*[21] the court refused to enforce covenants between a corporation and its "independent sales agents." In determining whether the independent sales agents were independent contractors (covenant not enforceable) as opposed to employees (covenant enforceable), the court applied the following test:

> For one to be an employee, the other party must retain the right to direct the manner in which the business shall be done, as well as the result to be accomplished, or in other words, not only what shall be done, but how it shall be done.[22]

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Another way by which the court has narrowly construed the exceptions to the Alabama statute is to preclude enforcement of covenants by anyone other than the parties to them. For example, in *Wyatt Safety Supply Co. v. Industrial Safety Products, Inc.,*[23] the court, reversing a trial judge's decision granting injunctive relief, refused to permit a successor to the employer to enforce noncompetition agreements between the employees and the predecessor employer. In this case, the plaintiff, Industrial Safety Products, had obtained covenants from a number of its employees. Subsequent to obtaining these covenants, Industrial Safety Products engaged in a number of corporate reorganizations whereby it merged with another company and temporarily changed its name. It subsequently emerged from these reorganizations as Industrial Safety Products. Because the court considered the reorganized Industrial Safety Products a separate entity from the Industrial Safety Products that originally obtained the covenants, it refused to enforce the covenants.[24]

Despite the disfavor with which the court says it views post-employment agreements, covenants have been enforced in numerous cases. The Alabama Supreme Court and Court of Civil Appeals have enforced covenants not to compete made by top level banking executives,[25] insurance executives and agents,[26] television broadcasters,[27] radio announcers,[28] newspaper publishers,[29] advertising managers,[30] gas company[31] and dry cleaning routemen,[32] pest control managers and technicians,[33] travel agents,[34] and even coffee salesmen.[35]

In determining whether to enforce a contractual provision in restraint of employment, the Alabama Supreme Court asks whether:

1. the employer has a protectable interest;
2. the restriction is reasonably related to that interest;
3. the restriction is reasonable in time and place; and
4. the restriction imposes no undue hardship on the employee.[36]

If these questions can be answered in the affirmative, then the agreement typically will be enforced.

A. The employer must have protectable interest

The Alabama Supreme Court first held that an employer must have a "protectable interest" before its covenants will be enforced in the 1982 decision of *DeVoe v. Cheatham.*[37] In *DeVoe,* the employer hired an inexperienced employee and trained the employee to install vinyl tops on automobiles. The employee later was discharged and the employer sought to enforce a restrictive covenant prohibiting the employee from working for a competitor for five years within a 50-mile radius of Decatur. The court held that the restriction was not enforceable, because the employer had no protectable interest. The court went on to explain that in order for a protectable interest to exist, "the employer must possess 'a substantial right in its business sufficiently unique to warrant the type of protection contemplated by [a] noncompetition agreement."[38] The court stated:

> If an employee is in a position to gain confidential information, access to secret lists, or to develop a close relationship with clients, the employer may have a protectable interest in preventing that employee from competing. But in the present case, DeVoe learned no more than the normal skills of the vinyl top installation trade, and he did not engage in soliciting customers. There is no evidence that he either developed any special relationship with the customers or had access to any confidential information or trade secrets. A simple labor skill, without more, is simply not enough to give an employer a substantial protectable right unique in his business. To hold otherwise would place an undue burden on the ordinary laborer and prevent him or her from supporting his or her family.[39]

Soon after its decision in *DeVoe*, the court was called upon again to discuss its protectable interest requirement. In *James S. Kemper,*[40] a lumber industry casualty insurer sued its former salesman seeking to enjoin him from competing statewide for a two-year period. The evidence showed the employee had been trained and even carried at a loss for several years so that he could build up a client base, and had "full supervision" over his employer's business in Alabama from 1963 to 1981. Based on these facts, the Alabama Supreme Court enforced the covenant, stating that the employee "clearly had access to valuable trade information and customer relationships in the course of his employment," and that "such information and the clientele acquaintance involved clearly constitute[d] a protectable interest."[41]

Since *DeVoe* and *James S. Kemper*, the protectable interest requirement has been the focus of much litigation. In a variety of contexts, the court has refused to enforce post-employment covenants where the employment relationship was of short duration or where the court felt the employee was more akin to the simple laborer in *DeVoe,* than to the insurance salesman in *James S. Kemper*. For example, in its 1986 *Calhoun v. Brendle, Inc.* decision,[42] the court reversed a trial judge's order enjoining an employee whose job was to check and refill fire extinguishers. The employer argued it had a protectable interest in both its customer relationships and its customer list. Disagreeing with the employer, the court held that just because an employee may have talked with customers and customers knew his face did not support the trial court's finding of a "close relationship" between the employee and the employer's customers. As for the customer list, the court held that in order to be protectable a customer list "must be treated in a confidential manner by the employer."[43] Because the names of all the customers were kept on a magnetic board visible to all employees, the court ruled the customer list was not entitled to protection.[44]

The court also has found no protectable interest and refused to enforce a covenant signed by an insurance agent employed for only one year who denied taking customer information with him when he left,[45] copier technicians who the court said at best possessed simple labor skills,[46] and a television station advertising salesman employed for only two months.[47]

One should not interpret these decisions as an indication of the court's unwillingness to enforce covenants not to compete made by employees. Where a covenant is signed by an employee who had substantial customer contact during his employment, or had access to confidential information possessed by his employer, the covenant will be enforced. For example, in January of this year, in *Clark v. Liberty Nat'l Life Insurance*

Co.,[48] the Alabama Supreme Court affirmed a judgment declaring valid a noncompetition agreement signed by one of Liberty National's insurance agents and awarding damages against the employee for breach of the covenant. The employee had worked for Liberty National as an agent from 1981 until he resigned on March 4, 1988. Noting that the employee was Liberty National's "sole contact" with its policyholders, and recognizing that these relationships were a "valuable asset," the court held that Liberty National "clearly" had a protectable interest in these customer relationships.

A few months prior to its *Clark* decision, the court held that employers also have a protectable interest warranting enforcement of noncompetition provisions where they impart to their employees confidential information. In *Central Bancshares of the South, Inc. v. Puckett*,[49] the Alabama Supreme Court reversed a lower court's decision refusing to enforce statewide a covenant between Central Bank and two of its former top executives. The trial court had enjoined the employees only from soliciting Central Bank's existing customers and employees, but not from competing in the banking business. In reversing, the court stated:

> While we agree with the trial judge that Central Bank has a protectable interest in its customer relations and relations with its employees, we do not agree that that protectable interest is limited to its customers and employees. As the trial judge indicated, Central Bank has a prominent position in the banking industry in the state of Alabama. Moreover, Brannon and Puckett, as key employees of Central Bank, had peculiar access to all of the techniques and strategies of the bank responsible for that position. If an employee is in a position to gain confidential information, access to secret lists, or to develop a close relationship with clients, the employer may have a protectable interest.[50]

In addition to customer relationships and access to confidential information, a protectable interest also can arise from an employer's investment in its employees. In *Nationwide Mutual Insurance Co. v. Cornutt*,[51] the Eleventh Circuit Court of Appeals, reversing a summary judgment granted to an employee, conducted a thorough analysis of the Alabama decisions discussing the protectable interest requirement. After noting that a protectable interest may arise where the employee is in a position to gain confidential information, access to secret lists, or develop a close relationship with clients, the Court recognized that a protectable interest "can also arise from the employer's investment in its employee, in terms of time, resources and responsibility."[52] In reversing, the Eleventh Circuit stated that the trial court's ruling could well leave the employer's protectable "investment interest . . . unvindicated."[53]

B. Restriction must be reasonably related to employer's protectable interest

Even where an employer establishes the existence of a protectable interest, either in its customers or confidential information, the court will only prohibit competition that threatens that protectable interest. This point recently was illustrated in the *Central Bancshares* decision where the court stated:

> We find that the restriction regarding competition in the banking business is reasonably related to Central Bank's protectable interest, because the restriction is designed to protect Central Bank only in the area in which it has a legitimate interest: the banking industry. The agreement specifically prohibits Brannon and Puckett from competing in the banking business; it does not preclude Brannon and Puckett from pursuing work outside of banking.[54]

If Central Bank had attempted to prevent these employees from working in another line of business, the restriction would not have been enforceable, because it would not have been reasonably related to Central Bank's protectable interest.[55]

C. Restriction must be reasonable in time and place

The Alabama statute provides that an "employee may agree with his employer to refrain from carrying on or engaging in a similar business and from soliciting old customers of such employer within a specified county, city or part thereof so long as the . . . employer carries on a like business therein." The Alabama Supreme Court describes this statutory language as requiring that any restriction be "reasonable in time and place." While the singular word "county" is used in the statute, a restriction may cover a much wider area if reasonable.[56]

Where a restriction is overly broad or otherwise unreasonable, Alabama courts have the equitable power to strike any unreasonable portion and enforce the remainder.[57] In *Mason Corp. v. Kennedy*,[58] the Alabama Supreme Court conferred upon trial courts the power to rewrite or "blue pencil" contracts in this manner. The court stated:

> We hold that a court of equity has the power to enforce a contract against competition although the territory or period stipulated may be unreasonable, by granting an injunction restraining the [employee] from competing for a reasonable time and within a reasonable area.[59]

What constitutes a reasonable geographic area depends upon the proof of what protection the business needs. As the Eleventh Circuit recently advised in *Cornutt*,[60] "To secure enforcement of a non-compete clause within a particular territory, the employer must demonstrate that it continues to engage, in that locale, in the activity that it seeks to enjoin."[61] Applying this logic, the Alabama Supreme Court endorsed a trial judge's order limiting to one county the territorial restriction to be enforced by injunction where 90 percent of the employer's customers were located in that county.[62] In two other cases, the court held employers entitled to statewide injunctions where it was shown that the employers conducted statewide business and the employees had statewide responsibility.[63] As the court noted in applying a covenant to the geographic area covering the entire United States east of the Rocky Mountains, a covenant not to compete may properly include part of Alabama, all of Alabama, or "more territory than the state of Alabama," depending on the circumstances.[64]

While few Alabama cases expressly discuss what period of

time is reasonable for a valid employment restriction, it is clear that durations of two years and less will pass judicial scrutiny.[65] On more than one occasion the court has stated, "[T]here can be no doubt that a two-year period for the restriction is reasonable." One should be cautious, however, in attempting to enforce an employment covenant for a duration of longer than two years. In *Mason Corp. v. Kennedy*,[67] the court refused to enforce a five-year covenant against a former employee, where the employee already had refrained from competing for two years and four months immediately following his termination.

D. Restriction must not impose an undue hardship on employee

Typically, when the court refuses to enforce a covenant on the basis that the employer lacks a protectable interest, it also will find as additional support for its decision that the covenant would place an undue burden or hardship on the employee.[68] For example, in *Chavers v. Copy Products Co.*,[69] the court, after finding the employer lacked a protectable interest, added:

> [T]he restriction in question places an "undue hardship" on Chavers. Though he is a highly skilled working man, he is nevertheless still only a working man, and it is undisputed that the only trade he knows and by which he can support himself and his family is copier maintenance and repair.[70]

Similarly, in *Sheffield v. Stoudenmire*,[71] the court stated, "This restriction imposes an undue hardship on Stoudenmire, who is fifty years old, married, and possesses significant financial obligations."[72]

However, where the covenant does not appear to be the product of any unequal bargaining power or overreaching on the part of the employer, the court may use the fact that the employee received considerable consideration as additional support for its decision to enforce a covenant. For example, in *Central Bank of the South v. Beasley*,[73] the court recognized that consideration can be an important factor in the undue burden analysis. The court stated:

> Considering all the circumstances, we cannot hold that Beasley will suffer undue hardship if the covenant is enforced according to its terms. As a former director and officer of First National, he bargained for and received over a quarter of a million dollars for his stock. He is free to accept employment in a bank outside of Baldwin County, or he can accept a non-banking position within Baldwin County. On March 16, 1985, he will be totally free of the noncompetition covenant. We do not see how any lesser burden could be placed on Beasley without completely derogating both the covenant's purpose and its consideration.[74]

While the *Central Bank* case addressed a situation involving the sale of goodwill, not an agreement between an employee and employer, the court recently quoted the above passage as support for its decision to enforce covenants made by employees who received approximately $1.8 million and $800,000 for their agreements not to compete.[75]

SALE OF GOODWILL OF BUSINESS OR PARTNERSHIP DISSOLUTION

Subsection (b) of the Alabama statute permits the seller of the goodwill of a business to agree with the buyer to refrain from carrying on or engaging in a similar business. Subsection (c) of the Alabama statute provides that partners upon or in anticipation of a dissolution of a partnership may agree that none of them will carry on a similar business where the partnership business has been transacted. Alabama courts considering covenants not to compete executed in such situations have not been nearly so restrictive in construing the agreements as they have been in construing covenants executed by employees. Although never articulated by an Alabama court, this probably is due to the fact that covenants executed in connection with the sale of goodwill are negotiated between sophisticated individuals capable of arms-length bargaining who usually receive greater consideration for their covenants than do employees.

In order for a covenant not to compete to be valid when executed in connection with the sale of a business, it is not necessary that the contract of sale specifically state that the transaction includes the sale of goodwill. It is sufficient if the contract indicates that the buyer is taking over a going concern.[76] However, the contract of sale must contain a provision prohibiting competition, because a covenant not to compete never will be implied when a business is being sold.[77]

Just as contracts restricting the practice of a profession are void in the employment context, so too are such contracts when executed by a professional in connection with the sale of a business or the dissolution of a partnership. For example, in *Friddle v. Raymond*,[78] the Alabama Supreme Court affirmed a trial judge's refusal to enforce a covenant not to compete contained in an agreement memorializing the dissolution of a partnership between two veterinarians. The Court held, "Because veterinarians are professionals, they are not excluded from the general rule prohibiting covenants not to compete."[79]

Similarly, in *Thompson v. Wiik, Reimer & Sweet*,[80] an accountant sold her accounting business and agreed not to compete for a period of time, during which she was to receive a share of the profits from the purchaser. The contract specifically provided that the payments were not for goodwill. The purchasers failed to make the payments and the seller sought damages. The Court held void the covenant not to compete and the provision for payments for such covenant, citing its previous decisions holding contracts restricting the practice of a profession void. In subsequent decisions, the court has distinguished its decision in *Thompson* and required purchasers to continue to make payments to sellers even though the sellers' covenants not to compete were found void.[81] The court justified its ruling in these subsequent decisions on the basis that there was sufficient consideration, other than the covenant, provided by the seller to support the purchase price.[82]

In *First Alabama Bancshares, Inc. v. McGahey*[83] and *Central Bank of the South v. Beasley*,[84] the court made clear that the purchase of stock can equate to the sale of goodwill.[85] In both these decisions, the court considered transactions in which local banks were merged into larger bank holding com-

panies. In each case, the major stockholders of the local bank sold their stock to a larger bank holding company and in the process agreed not to compete with the holding company, but then violated their covenants. The Alabama Supreme Court rejected the stockholders' contention that the sale of their stock was not a transfer of goodwill, holding that stockholders of corporations are the equitable owners of the assets of the corporation and can themselves transfer these assets, including goodwill.

In two instances, the court refused to enjoin wives of sellers of businesses from competing with the businesses their husbands sold. In *Russell v. Mullis*,[86] an action was brought against a wife to enjoin her from operating a convenience store in competition with two convenience stores her husband previously sold to the plaintiff. Noting that the wife "was not a party to either contract," and the evidence showed that the convenience store was "owned and operated solely" by the wife, the court denied the plaintiff's request for injunctive relief against the wife. The court did recognize that had the facts shown that the husband assisted his wife in operating the store or the wife assisted the husband in violating the covenant, the wife properly could be enjoined.[87]

The outcome was the same in *Livingston v. Dobbs*,[88] where the court refused to enjoin a wife from competing with the purchaser of her husband's barbecue business, even though she had signed a noncompetition clause. The court reasoned that even though the wife had agreed not to compete, the agreement she signed was unenforceable because it did not meet one of the exceptions found in subsections (b) or (c) of the Alabama statute. The wife was not an employee of the purchaser nor did she own any of the business her husband sold.

The court made clear in *Files v. Schaible*[89] that it will not tolerate circumvention of valid covenants not to compete through the use of front people. Files sold to Schaible the Ellis Red Barn Restaurant in Demopolis, Alabama. In doing so, Files agreed not to compete for five years within five miles of the Ellis Red Barn Restaurant. Shortly after the sale, a restaurant called Ellis V began operating across the street from the Ellis Red Barn Restaurant. Schaible brought suit. While the evidence at trial showed that the lease purchase agreement for operation of the Ellis V was signed by a former Red Barn waitress and that others were involved in financing and running the operation, the court had no difficulty in affirming a jury verdict in the amount of $50,000 against Files where there was testimony that Files told a number of people that he had managed to find a way to get around the noncompetition agreement.[90]

Like post-employment restraints, the court will enjoin competition only for a reasonable time and within a reasonable geographic location. Simply because the restriction may be ambiguous, vague or overly broad does not render the entire covenant invalid. Rather, "[T]he court may strike the unreasonable restriction from the agreement or the court can enforce the contract within its reasonable limits."[91]

Agreements not to compete with sold businesses have been enforced in areas as expansive as the entire United States and Canada for a period of five years[92] to areas as small as Baldwin County for two years.[93] Again, like post-employment restraints, the guiding light has been what protection is necessary under the particular facts of the case. Put more simply, "Where did the sold business operate prior to the sale?"[94]

PARTIAL RESTRAINTS AND FORFEITURE PROVISIONS

In various contexts, the court has construed contractual provisions as only partial restraints on trade not governed by the Alabama statute. While many of these decisions seem to conflict with and even contradict other decisions of the court, they can be quite useful in enforcing an otherwise invalid restraint.

In three decisions, the Alabama Supreme Court has held that agreements by employees not to solicit customers are only partial restraints of trade not subject to the Alabama statute.[95] For example, in *Hoppe v. Preferred Risk Mut. Ins. Co.*, the court stated, "A prohibition against soliciting [customers] is the not the same as a prohibition against engaging in a lawful profession, trade or business."[96] The court reasoned that where an employee is not prohibited from ***competing***, but merely from soliciting customers, the agreement only partially restrains trade and is not even governed by the Alabama statute.[97]

In glaring contrast to these decisions, the Court held void and unenforceable in *Cherry, Bekaert & Holland v. Brown*[98] a provision requiring an accountant withdrawing from a partnership to pay a set fee to the partnership for any partnership clients he represented during the first three years after withdrawal. Even though the fee may have been so steep as to prevent the withdrawing partner from doing any work for the accounting firm's clients for the three year period, the provision still had only the effect of preventing solicitation with the partnership's clients. It was not a prohibition on engaging in a lawful profession. Under the rationale employed by the court in *Hoppe*, it would seem that the provision would have been viewed as a partial restraint not subject to the Alabama statute. Nonetheless, the court not only applied the Alabama statute to void the agreement, but charged the accounting firm with attempting to "subvert and circumvent the laws and policies of Alabama regarding covenants not to compete."[99]

There are many types of other provisions or agreements that the court has viewed and labeled partial restraints. For example, in *Tomlinson v. Humana, Inc.*,[100] the court endorsed the use of an exclusive service contract between a physician and a hospital. By the terms of the contract, the physician was required to supply all primary pathology services needed at three Humana hospitals. The agreement was challenged by

another pathologist. The Court, characterizing the agreement as "only a partial restraint," held the agreement enforceable, because it allowed the plaintiff pathologist to work at other hospitals and did not affect the public interest.

The Court reached the same conclusion in *Gafnea v. Pasquale Food Co.*,[101] where the restriction was located in a franchise agreement and prevented the franchisee only from operating another pizza parlor within five miles for a period of 18 months. If the court had not construed these provisions as partial restraints, they would have failed the Alabama statute, because they were not between employers and employees, nor did they involve the sale of a business or the dissolution of a partnership.

Perhaps the best statement of the law regarding partial restraints was set forth by the court in *Alabama-Tennessee Natural Gas Co. v. Huntsville*,[102] where the court upheld a contract giving the City of Huntsville the exclusive right to sell gas in Madison County. In enforcing the agreement as only a partial restraint of trade, the court stated:

> It is true that contracts in general restraint of trade violate the policy of the law and are therefore void, but as observed in *Terre Haute Brewing Co. v. McGeever*, "Every contract, however, which at all restrains or restricts trade, is not void; it must injuriously affect the public weal; that it may affect a few or several individuals engaged in a like business does not render it void. Every contract of purchase and sale to some extent injures other parties; that is, it necessarily prevents others from making the sale or sales consummated by such contract."
>
> Contracts in partial restraint of trade are always upheld, when properly restricted as to territory, time and persons, where they are supported by sufficient consideration.[103]

Applying this rationale in other cases, the court has approved of a landlord's agreement with a tenant not to lease space in a shopping center to any of the tenant's competitors,[104] and an agreement in which a retailer agreed to buy all the beer he needed from another party.[105]

Another form of restraint often employed by businesses to partially restrain or discourage competition is a forfeiture provision. The Alabama Supreme Court has recognized that provisions whereby an employee agrees to forfeit certain benefits can be valid and enforceable under Alabama law.[106] According to the court, these provisions do not implicate the Alabama statute.

In *Courington v. Birmingham Trust National Bank*,[107] an employee entered into an agreement with a bank that provided that the employee would forfeit all of the bank's contributions to his account in a profit sharing plan in the event he took employment with a competing bank. When the employee resigned and took employment with a competitor, the bank refused to pay him its contributions to his account. The employee sued to recover the bank's matching contribution. After reviewing decisions from throughout the United States, and noting that "forfeiture-by-competition clauses appear to be widely used in the business community" and "with few exceptions upheld," the court found the employee forfeited his benefits by taking employment with one of the bank's competitors.[108]

In *Southern Farm Bureau Life Ins. Co. v. Mitchell*,[109] the Alabama Court of Civil Appeals approved the use of a forfeiture provision similar to the one in *Courington*. In *Mitchell*, an insurance agent's employment contract provided that he would not be entitled to renewal commissions after termination of his employment if he began representing any other insurance company in the state of Alabama. After the agent was terminated, and began serving as an agent for other insurers, Southern Farm Bureau ceased sending him renewal commissions. The agent sued. The court held that the contract involved a valid forfeiture provision rather than an invalid damage clause and did not fall within the terms of the Alabama statute.

One type of partial restraint the Alabama Supreme Court will not enforce is the "no switch" agreement. A "no switch" agreement is an arrangement between competitors where each agrees not to hire the other's employees. In both *Defco, Inc. v. Decatur Cylinder, Inc.*,[110] and *Dyson Conveyor Maintenance, Inc. v. Young & Vann Supply Co.*,[111] the court refused to enforce these agreements. In both cases, the employers argued that the provisions were only partial restraints, because they did not foreclose the employees from gainful employment elsewhere. The Alabama Supreme Court disagreed, reasoning that in neither case had the employees themselves agreed with their employer not to be employed by the competitor. Because the agreements did not meet any of the exceptions found in the Alabama statute, they were struck down.

REMEDIES FOR VIOLATION

The normal remedy for one seeking to enforce a covenant not to compete is an injunction prohibiting the covenantor from violating the agreement.[112] In addition to obtaining an injunction prohibiting competition, a party may be entitled to damages for breach of the covenant.[113] Finally, a new employer may be enjoined from employing the party agreeing not to compete, or may be assessed damages for interfering with the covenant.[115]

LAW TO BE APPLIED

Quite often, contracts containing covenants not to compete, like other contracts, provide that the contract shall be governed by the law of another state. The court recently was confronted with such a situation in *Cherry, Bekaert & Holland v. Brown*,[116] where an accountant signed a partnership agreement providing that North Carolina law would govern. Under North Carolina law, the contract was enforceable; under Alabama law, it was not. The Alabama Supreme Court, declaring that the covenant at issue "clearly flies directly in the face of the public policy of Alabama," refused to enforce the contractual choice of law provision and applied Alabama law to void the agreement.[117]

CONCLUSION

As may be evident from this article, it is often difficult to predict where a trial or appellate court may draw the fine line between reasonable protection of an employer's or purchaser's business and an unreasonable restraint on trade. As the court cautioned in *Robinson v. Computer Servicenters, Inc.*,[118]

"[E]ach particular contract must be tested by determining on the facts *of the particular case* whether the restriction upon one party is greater than is reasonably necessary for the protection of the other party." While this article is in no way exhaustive, it is hoped that it provides some guidance in the drafting of restraints on competition and some assistance to counsel who may be drawn in after litigation commences. ■

Endnotes

1. The predecessor to this article appeared in the November 1983 edition of *The Alabama Lawyer*. While this article generally employs the same format as its predecessor, it emphasizes the cases decided and doctrines developed since 1983. However, unlike the previous article, this article does not address any antitrust implications on this subject matter.
2. *See generally* a. Valiulis, *Covenants Not To Compete: Forms, Tactics, and the Law* (1985 & Supp. 1992).
3. *Ala. Code* § 8-1-1 (1975).
4. *Hill v. Rice*, 259 Ala. 587, 591, 67 So. 2d 789, 793 (1953) (quoting *Arthur Murray Dance Studios of Cleveland v. Witter*, 105 N.E.2d 685, 687 (Ohio C.P. 1952)).
5. Unpublished memorandum opinion entered in *Consultants & Designers, Inc. v. Butler Service Group, Inc.*, No. CV 80-PT-0754-S (N.D. Ala. Nov. 3, 1981).
6. *Ala. Code* § 8-1-1 (1975).
7. *See Advance Indus. Sec., Inc. v. William J. Burns Int'l Detective Agency*, 377 F.2d 236 (5th Cir. 1967); *C & C Products, Inc. v. Premier Indus. Corp.*, 290 Ala. 179, 275 So. 2d 124 (1972).
8. 259 Ala. 587, 67 So. 2d 789 (1953).
9. 285 Ala. 89, 229 So. 2d 480 (1969).
10. 285 Ala. at 91, 229 So. 2d at 483; *see also Clark v. Liberty Nat'l Life Ins. Co.*, ___ So. 2d ___, 1992 WL 207 (Ala. Jan. 3, 1992) (holding that consideration for covenant signed on April 1, 1985 was employment until March 4, 1988); *but see Robinson v. Computer Servicenters, Inc.*, 346 So. 2d 940 (Ala. 1977) (enforcement of covenant denied where employer intended to terminate employee at the time covenant was signed); *Mason Corp. v. Kennedy*, 286 Ala. 639, 244 So. 2d 585 (1971) (refusing to enforce covenant for full five-year duration where it was "uncertain" what consideration was "moving to employee").
11. 434 So. 2d 1380 (Ala. 1983).
12. *Sheffield v. Stoudenmire*, 553 So. 2d 125, 126 (Ala. 1989) (quoting *Robinson*, 346 so. 2d at 943).
13. 502 So. 2d 689, 693 (Ala. 1986).
14. *Friddle v. Raymond*, 575 So. 2d 1038, 1040 (Ala. 1991) (quoting *Odess v. Taylor*, 282 Ala. 389, 396, 211 So. 2d 805, 812 (1980)).
15. *Salisbury v. Semple*, 565 So. 2d 234 (Ala. 1990); *Odess v. Taylor*, 282 Ala. 389, 211 So. 2d 805 (1968).
16. *Friddle*, 575 So. 2d at 1040.
17. *Cherry, Bekaert & Holland v. Brown*, 582 So. 2d 502 (Ala. 1991); *Mann v. Cherry, Bekaert & Holland*, 414 So. 2d 921 (Ala. 1982); *Thompson v. Wiik, Reimer & Sweet*, 391 So. 2d 1016 (Ala. 1980).
18. *Burkett v. Adams*, 361 So. 2d 1 (Ala. 1978).
19. 382 So. 2d 1135 (Ala. Civ. App., 1980)
20. *Premier Indus. Corp. v. Marlow*, 292 Ala. 407, 295 So. 2d 396, *cert. denied*, 419 U.S. 1033 (1974); *C& C Products, Inc. v. Fidelity & Deposit Co.*, 512 F.2d 1375 (5th Cir. 1975); *Blalock v. Perfect Subscription Co.*, 458 F. Supp. 123 (S.D. Ala. 1978), *aff'd*, 599 F.2d 743 (5th Cir. 1979).
21. *Premier Indus.*, 292 Ala. 407, 295 So. 2d 396.
22. *Premier Indus.*, 292 Ala. at 411-412, 295 So. 2d at 299 (quoting *Odess v. Taylor*, 282 Ala. 389, 396, 211 So. 2d 805, 811 (1968)).
23. 566 So. 2d 728 (Ala. 1990).
24. *See also Russell v. Birmingham Oxygen Serv., Inc.*, 408 So. 2d 90 (Ala. 1981) (holding wholly-owned subsidiary could not enforce covenants between its employees and its parent corporation); Unpublished memorandum opinion entered in *Metromedia, Inc. v. Jennings*, no. CV 83-H-5866-NE (M.D. Ala. 1984) (holding corporation which purchased all of the assets of another corporation could not enforce the covenants the purchased corporation had with its employees).
25. *Central Bancshares of the South, Inc. v. Puckett*, 584 So. 2d 829 (Ala. 1991).
26. *Clark v. Liberty Nat'l Life Ins. Co.*, ____So. 2d _____, 1992 WL 207 (Ala. Jan. 3, 1992); *James S. Kemper & Co. Southeast, Inc. v. Cox & Assocs., Inc.*, 434 So. 2d 1380 (Ala. 1983).
27. *Booth v. WPMI Television Co.*, 533 So. 2d 209 (Ala. 1988).
28. *Cullman Broadcasting Co. v. Bosley*, 373 So. 2d 830 (Ala. 1979().
29. *Tyler v. Eufaula Tribune Publishing Co.*, 500 So. 2d 1005 (Ala. 1986).
30. *Parker v. Ebsco Indus.*, 282 Ala. 98, 209 So. 2d 383 (1968).
31. *Daughtry v. Capital Gas Co.*, 285 Ala. 89, 229 So. 2d 480 (1969).
32. *Shelton v. Shelton*, 238 Ala. 489, 192 So. 55 (1939).
33. *Rush v. Newsom Exterminators*, 261 Ala. 610, 75 So. 2d. 112 (1954); *Slay v. Hess*, 252 Ala. 455, 41 So. 2d 582 (1949); *Dobbins v. Getz Exterminators of Alabama, Inc.*, 382 So. 2d 1135 (Ala. Civ. App. 1980).
34. *Daniel v. Trade Winds Travel, Inc.*, 532 So. 2d 653 (Ala. Civ. App. 1988).
35. *Dixon v. Royal Cup, Inc.*, 386 So. 2d 481 (Ala. Civ. App. 1980).
36. *Central Bancshares of South, Inc. v. Puckett*, 5834 So. 2d 829 (Ala. 1991) (quoting *James S. Kemper & Co. Southeast, Inc. v. Cox & Assocs., Inc.*, 434 So. 2d 1380, 1384 (Ala. 1983)).
37. 413 So. 2d 1141 (Ala. 1982).
38. *Id.* at 1142 (quoting *Cullman Broadcasting Co. v. Bosley*, 373 So. 2d 830, 836 (Ala. 1979)).
39. 413 So. 2d at 1143.
40. 434 So. 2d 1300 (Ala. 1983).
41. *Id.* at 1384.
42. 502 So. 2d 689 (Ala. 1986).
43. *Id.* at 692.
44. *Id.*; *see also Orkin Exterminating Co. v. Etheridge*, 582 So. 2d 1102, 1104 (Ala. 1991) (finding employer lacked protectable interest in customer list "available to anyone who walked into [employer's] office").
45. *Sheffield v. Stoudenmire*, 553 So. 2d 125 (Ala. 1989).
46. *Chavers v. Copy Products Co.*, 519 So. 2d 942 (Ala. 1988); *Greenlee v. Tuscaloosa Office Prods. & Supply Co., Inc.*, 474 So. 2d 669 (Ala. 1985).
47. *Birmingham Television Corp. v. DeRamus*, 502 So. 2d 761 (Ala. Civ. App. 1986).
48. ___ So. 2d ___, 1992 WL 207 (Ala. Jan. 3, 1992).
49. 584 So. 2d 829 (Ala. 1991).
50. *Id.* at 831 (quotation marks and citation omitted).
51. 907 F.2d 1085 (11th Cir. 1990).
52. *Id.* at 1087-1088.
53. *Id.* at 1088.
54. *Central Bancshares*, 584 So. 2d at 831.
55. *See also Cullman Broadcasting Co. v. Bosley*, 373 So. 2d 830, 835 (Ala. 1979).
56. *McNeel Marble Co. v. Robinette*, 259 Ala. 66, 69, 65 So. 2d 221, 223 (1953).
57. *Cullman Broadcasting*, 373 So. 2d at 835; *Mason Corp. v. Kennedy*, 286 Ala. 639, 645, 244 So. 2d 585, 590 (1971).
58. 286 Ala. 639, 244 So. 2d 585.
59. 286 Ala. at 645, 244 So. 2d at 590.
60. 907 F.2d 1085 (11th Cir. 1990)
61. *Id.* at 1088; *see also James S. Kemper & Co. Southeast Inc. v. Cox & Assocs. Inc.*, 434 So. 2d 1380, 1385 (Ala. 1983) (noting that "the area in which the [insurance] agent was active for the insurance company" is the appropriate territory to enjoin competition).
62. *Daughtry v. Capital Gas Co.*, 285 Ala. 89, 93, 229 So. 2d 480, 484 (1969).
63. *Central Bancshares*, 584 So. 2d at 832; *James S. Kemper*, 434 So. 2d at 1385.
64. *Parker v. Ebsco Indus.*, 282 Ala. 98, 104, 209 So. 2d 383, 386 (1968).
65. *Clark v. Liberty Nat'l Life Ins. Co.*, ___ So. 2d ____, 1992 WL 207 (Ala. Jan. 3, 1992); *Central Bancshares*, 584 So. 2d at 831; *James S. Kemper*, 434 So. 2d at 1384.
66. *Clark*, 1992 WL 207 (quoting *James S. Kemper*, 434 So. 2d at 1385).
67. 286 Ala. 639, 244 So. 2d 585 (1971).
68. *See Sheffield v. Stoudenmire*, 553 So. 2d 125, 126-27 (Ala. 1989); *Chavers v. Copy Products Co.*, 519 So. 2d 942, 945 (Ala. 1988); *Calhoun v. Brendle, Inc.*, 502 So. 2d 689, 694 (Ala. 1986).
69. 519 So. 2d 942 (Ala. 1988).
70. *Id.* at 945.
71. *Sheffield*, 553 So. 2d 125.
72. *Id.* at 126-127.
73. 439 So. 2d 70 (Ala. 1983).
74. *Id.* at 74.
75. *See Central Bancshares of the South, Inc. v. Puckett*, 584 So. 2d 829, 832 (Ala. 1991).
76. *Russell v. Mullis*, 479 So. 2d 727, 729 (Ala. 1985); *Files v. Schaible*, 445 So. 2d 257, 260 (Ala. 1984); *Maddox v. Fuller*, 233 Ala. 662, 173 So. 12 (1937).
77. *Joseph v. Hopkins*, 276 Ala. 18, 23-24, 158 So. 2d 660, 665 (1963) (citing *Collas v. Brown*, 211 Ala. 443, 100 So. 769 (1924)).
78. 575 So. 2d 1038 (Ala. 1991).
79. *Id.* at 1040.
80. 391 So. 2d 1016 (Ala. 1980).
81. *Salisbury v. Semple*, 565 So. 2d 234, 236 (Ala. 1990); *Mann v. Cherry, Bekaert & Holland*, 414 So. 2d 921, 924 (Ala. 1982).
82. *Salisbury*, 565 So. 2d at 236 (purchaser required to continue payments where 70 percent of the purchase price was allocated to the covenant not to compete and 30 percent for goodwill); *Mann*, 414 So. 2d at 924 (contract not void even though covenant unenforceable where purchaser also obtained client list and goodwill).
83. 355 So. 2d 681 (Ala. 1977).
84. 439 So. 2d 70 (Ala. 1983).
85. *See also Kershaw V. Knox Kershaw, Inc.*, 523 So. 2d 351, 357 (Ala. 1988) (holding that a stock swap between two brothers constituted a sale of goodwill).
86. 479 So. 2d 727 (Ala. 1985).
87. *Id.* at 729 (citing *Daughtry v. Capital Gas Co.*, 285 Ala. 89, 229 So. 2d 480 (1969)).
88. 559 So. 2d 569 (Ala. 1990).

89. 445 So. 2d 257 (Ala. 1984).
90. *Id.* at 261.
91. *Kershaw v. Knox Kershaw, Inc.*, 523 So. 2d 351, 359 (Ala. 1988).
92. *Id.* at 359.
93. *Central Bank of the South v. Beasley*, 439 So. 2d 70, 73 (Ala. 1983).
94. *See Kershaw*, 523 So. 2d at 359 (holding covenant enforceable only to extent that it prohibited where business was conducted prior to the sale); *Central Bank*, 439 So. 2d at 73.
95. *Corson v. Universal Door Systems, Inc.*, ____ So. 2d ____, 1991 WL 172434 (Aug. 9, 1991); *Hoppe v. Preferred Risk Mut. Ins. Co.*, 470 So. 2d 1161 (Ala. 1985); *FAMEX, Inc. v. Century Ins. Servs., Inc.*, 425 So. 2d 1053 (Ala. 1982); *see also Hughes Assocs., Inc. v. Printed Circuit Corp.*, 631 F. Supp. 851 (N.D. Ala. 1986)
96. 470 So. 2d at 1163.
97. *Id.* at 1164.
98. 582 So. 2d 502 (Ala. 1991).
99. *Id.* at 506.
100. 495 So. 2d 630 (Ala. 1986).
101. 454 So. 2d 1366 (Ala. 1984).
102. 275 Ala. 184, 153 So. 2d 619 (1963).
103. *Alabama-Tennessee Natural Gas Co.*, 275 Ala. at 193, 153 So. 2d at 627 (quotation marks and many citations omitted) (quoted in *Hibbett Sporting Goods, Inc. v. Biernbaum*, 391 So. 2d 1027 (Ala. 1980)).
104. *Hibbett Sporting Goods*, 391 So. 2d 1027.
105. *Terre Haute Brewing Co. v. McGeever*, 198 Ala. 474, 73 so. 889 (1916).
106. *Courington v. Birmingham Trust Nat'l Bank*, 347 So. 2d 377 (Ala. 1977); *Southern Farm Bureau Life Ins. Co. v. Mitchell*, 435 So. 2d 745 (Ala. Civ. App. 1983).
107. 347 So. 2d 377.
108. Before employing a forfeiture provision such as the one used by the bank in *Courington*, one should review the Employee Retirement Income Security Act of 1974 which preempts state law regarding covered employee benefit plans and prohibits forfeiture of employee benefits except as permitted under the Act.
109. 435 So. 2d 745.
110. ___ So. 2d ____, 1992 WL 208 (Ala. Jan. 3, 1992).
111. 529 So. 2d 212 (Ala. 1988).
112. *See, e.g., Booth v. WPMI Television Co.*, 533 So. 2d 209 (Ala. 1988) (enjoining television advertising salesmen from working for another television station within a 60 mile radius for one year).
113. *Clark*, 1992 WL 207 (employer awarded $14,819.61 for employee's violation of covenant); *Files v. Schaible*, 445 So. 2d 257 (Ala. 1984) (restaurant purchaser awarded $50,000 where seller breached covenant by opening competing by opening competing business across the street).
114. *Daughtry v. Capital Gas Co.*, 285 Ala. 89, 229 So. 2d 480 (1970).
115. *James S. Kemper & Co. Southeast, Inc. v. Cox & Associates, Inc.*, 434 So. 2d 1380 (Ala. 1983).
116. 582 So. 2d 502 (Ala. 1991).
117. *See also Blalock v. Perfect Subscription Co.*, 458 F. Supp. 123 (S.D. Ala. 1978), *aff'd*, 599 F. 2d 743 (5th Cir. 1979).
118. 346 So. 2d 940, 943 (Ala. 1977) (emphasis in original) (citing *Hill v. Rice*, 259 Ala. 587, 67 So. 2d 789 (1953)).

CORPORATE COUNSEL SECTION

To better serve the needs of corporate attorneys in Alabama, the Alabama State Bar formed the Corporate Counsel Section Task Force. The task force was chartered to determine if there is sufficient interest among members of the bar to support a Corporate Counsel Section. Several of Alabama's in-house corporate attorneys expressed a desire to see a section address the particular needs of corporate counsel.

The proposed section would serve members of the state bar who regularly provide legal services to corporate clients, either as in-house corporate attorneys or as attorneys in private practice who regularly advise corporate clients. The initial, informal investigation has uncovered a surprising number of attorneys in the state whose practice fits one of these two criteria.

The benefits of participation in the section would be numerous. First, by networking with similarly-situated attorneys, members could exchange information about library holdings, sample policies and practices, methods for managing in-house law offices, in-house training and development, and other topics. Second, the section would seek to provide continuing legal education programs which focus on the needs of in-house counsel in Alabama. Third, a quarterly newsletter could address current issues of interest to in-house counsel. Other publications might include various checklists submitted by members of the section, and an Alabama Corporate Counsel's Desk Reference. Among other possible section activities is a computer bulletin board accessible by any members of the section having the appropriate computer technology.

Members could contribute to the section's accomplishments by participating in committee addressing areas such as:
- in-house attorney monitoring and development programs;
- the development and maintenance of in-house legal libraries;
- in-house practice and technology;
- policies, practices and procedures;
- ethics;
- law department management;
- section publications; and
- section programs.

The task force is now trying to identify all members of the state bar who would be interested in the creation of such a section. If you are interested, please complete and return the attached response card. This does not commit you to become a member of the section (if formed), nor does it commit you to perform any work toward creating the section. Rather, it simply helps the task force determine the level of interest in forming such a section. In addition to this message in *The Alabama Lawyer*, a direct mail campaign is being conducted to attorneys who may not be directly involved in state bar activities, but who may want to participate in a corporate counsel program.

Jud Hennington, Task Force Chairperson

I would be interested in joining the proposed **Corporate Counsel Section** of the Alabama State Bar.

_____

Name

_____

Firm

_____

Mailing address, City, State, ZIP)

Please return by June 1, 1992, to Keith B. Norman, Director of Programs, Alabama State Bar, P.O. Box 671, Montgomery, AL 36101.