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ILLINOIS ENACTS SWEEPING REFORMS TO NON-COMPETE AND NON-SOLICIT AGREEMENTS—WHAT ALL EMPLOYERS NEED TO KNOW

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The Illinois General Assembly has enacted sweeping changes to the Illinois Freedom to Work Act, 820 ILCS § 90, *et seq.* (the "Act"), which will limit the use of covenants not to compete ("non-competes") and covenants not to solicit ("non-solicits") in employment agreements to employees earning more than certain compensation thresholds established by the amendments to the Act. The amendments to the Act also impose certain additional procedural requirements on employers utilizing non-competes and non-solicits. Senate Bill 672 ("SB 672") passed unanimously in the Illinois House and Senate, and Governor J.B. Pritzker is expected to sign the bill.

Here's what employers need to know.

DO THE CHANGES IN SB 672 IMPACT EXISTING EMPLOYMENT AGREEMENTS CONTAINING RESTRICTIVE COVENANTS?

No. SB 672 applies to non-competes and non-solicits entered into **after** January 1, 2022. Employers should review any form and/or template agreements to ensure compliance going forward, but need not make changes to agreements entered into **before** January 1, 2022, in order to comply with the Act. That said, if employers are considering revising their restrictive covenant forms, they should begin that process now, especially if they intend to ask existing employees to sign new forms prior to January 1, 2022.

WHAT KINDS OF POST-EMPLOYMENT RESTRICTIVE COVENANTS DOES SB 672 IMPACT?

SB 672 applies to "covenants not to compete" and "covenants not to solicit."

- **Covenant Not to Compete**: An agreement between an employer and an employee that restricts the employee from performing: (i) any work for another employer for a specified period of time; (ii) any work in a specified geographical area; or (iii) work for another employer that is similar to the employee's work for the employer.

- **Covenant Not to Solicit**: An agreement between an employer and an employee that restricts the employee from: (i) soliciting for employment the employer's employees (sometimes referred to as an "anti-poaching" provision); or (ii) soliciting, for the purpose of selling products or services of any kind to, or from interfering with the employer's relationships with, the employer's clients, prospective clients, vendors, prospective vendors, suppliers, prospective suppliers, or other business relationships.

SB 672 does **not** apply to other post-employment restrictive covenants:

- **Confidentiality & Trade Secret Protections**: Confidentiality agreements, covenants or agreements prohibiting the use or disclosure of trade secrets or inventions, and assignment of invention agreements or covenants, which are common in employment agreements.
- **Sale or Purchase of a Business**: Restrictive covenants entered into by a person purchasing or selling the goodwill of a business or otherwise acquiring or disposing of an ownership interest in a business.
- Employers should limit their application of this exclusion to the **owners** of a business, and should not treat all employment agreements executed as a result of a business sale/purchase as exempt from SB 672's other requirements.
- For example, if a purchaser wants to retain certain high-level employees from the purchased business, any employment agreements executed by those **employees** (i.e., non-owners) would be governed by SB 672.
- **"Garden Leave**:" Agreements between an employer and an employee requiring advance notice of termination of employment if, during the notice period, the employee remains employed and receives compensation.
- **No Rehire**: Agreements by which the employee agrees not to reapply for employment with the same employer after termination of the employee, which are sometimes included in separation agreements.

DOES SB 672 PROHIBIT NON-COMPETE AND NON-SOLICIT RESTRICTIVE COVENANTS?

For most employees, no. SB 672 **prohibits** covenants not to compete for: (i) state employees covered by a collective bargaining agreement; and (ii) employees in the construction industry, except construction employees who primarily perform management, engineering, architectural, design, or sales functions for the employer, or who are shareholders, partners, or owners in any capacity of the construction employer.

For all other employees, non-competes and non-solicits may be imposed if the employee in question meets certain earnings thresholds.

- **Non-Compete**: An employer may not enter into a covenant not to compete with an employee unless that employee's "actual or expected" annualized rate of earnings exceeds $75,000 per year, starting in calendar year 2022. The minimum earnings threshold increases every five years thereafter:
  - $80,000 per year beginning on January 1, 2027;
  - $85,000 per year beginning on January 1, 2032; and
  - $90,000 per year beginning on January 1, 2037.

- **Non-Solicit**: An employer may not enter into a covenant not to solicit with an employee unless that employee's "actual or expected" annualized rate of earnings exceeds $45,000 per year, starting in calendar year 2022. The minimum earnings threshold increases every five years thereafter:
  - $47,500 per year beginning on January 1, 2027;
  - $50,000 per year beginning on January 1, 2032; and
  - $52,500 per year beginning on January 1, 2037.

DO "EARNINGS" JUST MEAN AN EMPLOYEE'S SALARY, OR DOES IT INCLUDE OTHER COMPENSATION?

Earnings are defined **broadly** to include more than just an employee's base salary. Earned bonuses, commissions, or any other form of taxable compensation reflected on an IRS Form W-2 can be included in the calculation of an employee's "earnings." Additionally, elective deferrals not reflected on a W-2, including, but not limited to, employee contributions to a 401(k) plan, a 403(b) plan, a flexible spending account, a health savings account, and/or commuter benefit-related deductions, can be included as "earnings."

DOES AN EMPLOYER HAVE TO PROVIDE A "SIGNING BONUS" OR ANY OTHER PAYMENT TO AN EMPLOYEE FOR SIGNING AN AGREEMENT WITH RESTRICTIVE COVENANTS?

Not necessarily, but doing so will increase the likelihood of a court finding that a restrictive covenant is supported by "adequate consideration."

Under existing Illinois legal authority, a post-employment restrictive covenant must be supported by adequate consideration to be enforceable. The Illinois Appellate Court has ruled that at-will employment of less than two years is insufficient consideration to support a non-compete or non-solicit, absent some additional consideration (e.g., a signing bonus).[1] The ruling created some confusion, with some federal courts refusing to apply this "bright line" 2-year rule.[2]

SB 672 essentially codifies the above-referenced Illinois Appellate Court decision, defining "adequate consideration" to support a non-compete and/or non-solicit as: (i) at least two (2) years of at-will employment after the employee signs the agreement with non-compete and/or non-solicit restrictive covenants; or (ii) a period of employment "plus additional professional or financial benefits;" or (iii) "merely professional or financial benefits adequate by themselves." SB 672 does not expand on what constitutes a "professional or financial benefit," but it could include a cash bonus, a raise in salary, training, a promotion, or other employee benefits and/or payments. To ensure a restrictive covenant is supported by adequate consideration, regardless of the length of employment, employers may want to take the simplest approach and provide a cash "signing bonus" to any employee who signs an agreement with a non-compete/non-solicit.

IF AN EMPLOYEE MEETS THE SALARY THRESHOLD, AND THE EMPLOYER PROVIDES ADEQUATE CONSIDERATION, CAN AN EMPLOYER IMPOSE ANY NON-COMPETE AND/OR NON-SOLICIT PROVISIONS IT WANTS?

No. Under existing legal authority in Illinois, an employer may only impose post-employment restrictive covenants that are no greater than necessary to protect an employer's legitimate business interests. SB 672 clarifies some ambiguities under Illinois common law, and codifies the factors that courts should consider when determining whether non-compete and/or non-solicit restrictions are reasonably necessary to protect legitimate business interests. Those factors include:

- the employee's exposure to the employer's customer relationships or other employees;
- the near-permanence of customer relationships;
- the employee's acquisition, use, or knowledge of confidential information through the employee's employment;
- the time restrictions (i.e., the longer an employee is subject to the restrictions, the more likely a reviewing court will find them unreasonable);
- the geographic restrictions (i.e., if an employee's sales territory is Illinois, and a customer non-solicit applies to any customer of the employer anywhere in the world, regardless of whether the employee worked for or knew about that customer, a court may find that unreasonable); and

- the scope of the activity restrictions.

SB 672 also makes clear that determining whether a particular restrictive covenant is reasonable "must be determined on its own particular facts"—there is no "one size fits all" approach. Therefore, employers should continue to limit the restrictions in their non-compete and non-solicit covenants to those required to protect their legitimate business interests.

DOES AN EMPLOYER HAVE TO FOLLOW ANY PARTICULAR PROCEDURAL STEPS WHEN REQUIRING AN EMPLOYEE TO SIGN AN AGREEMENT CONTAINING A NON-COMPETE AND/OR NON-SOLICIT?

Yes. A non-compete or a non-solicit is unenforceable **unless**: (i) the employer advises the employee in writing to consult with an attorney prior to signing the agreement containing the non-compete/non-solicit; and (ii) the employer provides the employee with a copy of the agreement containing the non-compete/non-solicit at least 14 calendar days before the commencement of employment or the employer provides the employee with at least 14 calendar days to review the agreement containing the non-compete/non-solicit. Notably, SB 672 permits an employee to voluntarily elect to sign the agreement before the expiration of the 14-day period.

DOES SB 672 IMPOSE ANY PENALTIES ON AN EMPLOYER WHO ENTERS INTO, OR SEEKS TO ENFORCE, A VOID AND/OR UNLAWFUL NON-COMPETE AND/OR NON-SOLICIT RESTRICTIVE COVENANT?

Yes. First, in any civil action (including but not limited to a complaint or counter-claim) or arbitration filed by an employer to enforce a restrictive covenant, a prevailing employee is entitled to recover his or her costs and reasonable attorney's fees associated with defending against the action. Additionally, SB 672 gives the Illinois Attorney General's Office broad discretion to investigate any employer it believes has engaged in a "pattern or practice" of violating SB 672. The Attorney General may impose civil penalties up to $5,000 per violation, and $10,000 for any repeated violation within 5 years.

ADDITIONAL KEY PROVISIONS

- **Reformation Permitted**: Under existing legal authority, courts in Illinois may, but are not required to, reform a restrictive covenant—that is, revise it—if the court finds it too broad as written. SB 672 permits judicial modification of overly broad restrictions under certain circumstances, and codifies the factors a court may consider when determining whether a particular restrictive covenant should be revised: the fairness of the restraints as originally written, whether the original restriction reflects a good-faith effort to protect a legitimate business interest of the employer, the extent of a reformation or revision necessary to render the restrictive covenant reasonable/enforceable, and whether the parties included a clause

authorizing such modifications in their agreement. Employers should make sure that all employment agreements containing non-competes/non-solicits contain a provision expressly granting the court (or arbitrator) the right to judicially modify overly broad restrictions.

- **COVID-19 Related Terminations and Furloughs**: While the COVID-19 pandemic is hopefully abating in Illinois and across the country, SB 672 provides that non-competes/non-solicits are void and unenforceable against any employee terminated, laid off, and/or furloughed due to business circumstances or government orders related to COVID-19, or "under circumstances that are similar to the COVID-19 pandemic," which SB 672 does not define. Non-competes/non-solicits may only be enforced against a COVID-19 terminated/laid off employee if that employee is paid compensation equivalent to the employee's base salary from the time of termination through the end of the period of enforcement, minus compensation earned through subsequent employment during the period of enforcement.

Given these sweeping changes to the restrictive covenant legal landscape in Illinois, employers should consult legal counsel to evaluate their current forms and practices well in advance of the anticipated January 1, 2022 effective date of SB 672. BCLP regularly advises employers regarding best practices for restrictive covenant agreements in Illinois and throughout the United States, and we encourage you to reach out to one of our members to discuss how we can assist in achieving your business objectives.

>[1] Fifield v. Premier Dealer Servs., Inc., 993 N.E.2d 938 (1st Dist. 2013).

See Stericycle, Inc. v. Simota, 2017 WL 4742197, at *5 (N.D. Ill. Oct. 20, 2017) (refusing to apply *Fifield* and holding that 13 months of continued at-will employment constituted adequate consideration to enforce restrictive covenants); *see Avison Young-Chicago, LLC v. Puritz*, 2017 WL 5896887, at *6 (N.D. Ill. Nov. 29, 2017) (holding that 17 months of continued at-will employment constituted adequate consideration and reasoning that if called to rule on *Fifield*, the Illinois Supreme Court would adopt a flexible, fact-specific approach and reject "*Fifield*'s rigid, two-year rule").

RELATED PRACTICE AREAS

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