SHOULD YOU ASK EMPLOYEES TO SIGN A NONCOMPETE AGREEMENT?

Proprietary knowledge is critical to business success, and companies go to great lengths to protect intellectual property and trade secrets. For instance, many companies require employees to sign noncompete agreements upon their hiring to protect intellectual property from exiting the firm if the employee decides to leave.

Noncompete agreements are contracts between employees and companies that can be effective in dissuading employees from changing jobs and going to work for a competitor. They don’t prevent such job changes, but instill penalties or threaten legal action if the employee moves to a competitor within a certain time period.¹

Often a noncompete agreement is considered a required term of employment with a company. If an employee violates a noncompete agreement, he or she may be liable for legal action by the company according to relevant state laws.

Noncompete agreements can protect a company’s short-term interests in a wide range of areas:
- Intellectual property and trade secrets
- Production processes and formulations
- Innovative technologies
- Confidential financial and marketing information
- Customer lists and vendor relationships
- Goodwill with customers
- Knowledge of business practices
- Specialized training or techniques

Over the past 25 years, U.S. businesses have increased their use of noncompete agreements. This has been attributed to the rising value of trade secrets, increasing technological innovation, threats from foreign governments and competitors, and a highly mobile workforce. Analysts estimate that about 20% of U.S. workers are currently bound by a noncompete agreement, and nearly twice that number will be at some point in their careers.²

PROS AND CONS OF NONCOMPETE AGREEMENTS
Some of the advantages and disadvantages of noncompete agreements include:³

Pros
- **Security and integrity** — Protection of intellectual property signals to investors and the market that a company maintains high standards for preserving its intellectual property and competitive advantages.
- **Employee retention** — Competitors may be less likely to try to recruit employees if they know a company requires a noncompete agreement.
- **Customer retention** — Higher employee retention often translates to greater continuity in customer service and relationships.
- **Protection against unfair competition** — Noncompete agreements discourage ex-employees from capitalizing on a company’s trade secrets and proprietary processes and products.
- **Payback clause protection** — Some noncompete agreements require employees to pay back part of their training costs if they leave within a certain timeframe after receiving paid, specialized training.
Some companies are choosing to forgo noncompete agreements in favor of non-disclosure agreements as a condition of employment.

Cons

- **Recruitment challenges** — Many job candidates view noncompete agreements as a barrier that could limit their mobility and future opportunities. Millennial workers, who change jobs more frequently than older generations, may be turned off by the restrictions of noncompete agreements.

- **A potential advantage for competitors** — If competitors don’t require noncompete agreements, their companies may be viewed as more attractive to candidates who want greater freedom and flexibility.

- **Negative perception** — Job-hunting employees are likely to seek new employment with a similar company in the same or related field. Because noncompete agreements restrict future employment opportunities, they are often viewed as punitive.

- **Varied enforcement** — Every state has its own laws regarding noncompete agreements and enforcement varies widely. Courts are often unwilling to enforce noncompete agreements as they limit a person’s ability to earn a living.

Non-disclosure agreements offer an alternative

Some companies are choosing to forgo noncompete agreements in favor of non-disclosure agreements as a condition of employment. A non-disclosure agreement is a legal contract that creates a confidential relationship between a company that holds confidential information and an employee to whom this confidential information will be disclosed. The agreements specify what information is considered private and classified.

Non-disclosure agreements are legally enforceable and the type of information and knowledge that can be covered under a non-disclosure agreement is virtually limitless. They provide the company with a higher level of security for proprietary information, processes and products without being as restrictive. Companies should consult with their legal counsel and human resources executives to determine the best route to follow.

To discuss these topics in more detail, please contact your PNC Relationship Manager.