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Major Changes in Colorado Non-Compete/Non-Solicitation Law Set To Become Effective on August 10, 2022

On August 10, 2022, major changes in Colorado law go into effect for restrictive employment covenants, i.e., covenants not to compete (non-competition covenants) and covenants not to solicit customers of an employee's former employer (non-solicitation covenants). For many years, Colorado has limited non-competition covenants by statute, Colorado Revised Statutes §8-2-113, which prohibits non-competition covenants with specified exceptions, including when they are part of a contract for sale of a business. The most frequent and heavily litigated exception in the old law permitted an employer to require non-competition covenants for executive and management personnel, and for officers and employees who constitute professional staff to such personnel. Courts and parties frequently wrestled with the question whether an employee had been an "executive" or "management" personnel of the former employer.

Highly Compensated Employee Exception

The amendments apply to non-competition and non-solicitation covenants entered into after August 10. The amendments state that covenants not to compete are void, with specified exceptions. The exception for executive and management personnel is eliminated. Instead, the new law permits an exception for "highly compensated employees" (HCE) of the former employer seeking to enforce a non-competition covenant (i.e., employees making more than $101,250 per year) both at the time the covenant was entered into and at the time it is enforced. The Colorado Department of Labor and Employment will annually adjust the HCE salary threshold. In addition to meeting the HCE threshold, the former employer must prove that the covenant is for the protection of trade secrets and is no broader than necessary to protect trade

secrets.

Non-solicitation covenants seeking to limit a former employee from contacting customers will only be enforceable against employees earning at least 60 percent (presently $60,750) of the HCE threshold, at the time the covenant was entered into and at the time it is enforced. In addition, the former employer must show that the non-solicitation covenant is no broader than necessary to protect the employer's legitimate interest in protecting trade secrets.

Thus, in addition to meeting the salary requirements, both non-competition and non-solicitation covenants must be specifically tailored for the purpose of protecting trade secrets. Absent such a showing, a covenant that simply prohibits employees from working for a competitor is no longer valid. However, the amended statute retains the exception permitting restrictive covenants related to the sale of a business. It retains but modifies provisions to recover training costs that are not for regular on-the-job training, and for requiring repayment of scholarships in apprenticeship programs. The amendments do not change the existing law prohibiting restrictions on the right of physicians to practice medicine when moving to a new medical practice, but permitting compensation for damages related to such competition.

Notice Requirements

Even in the limited instances when restrictive covenants are permitted, the employer must provide written notice of a non-competition covenant. For an applicant or prospective worker, the employer must provide such notice of a non-competition covenant before the worker accepts the employer's offer of employment. For a current worker, the employer must provide such notice at least 14 days before the earlier of the effective date of the covenant, or the effective date of any additional compensation or change in terms of employment that provides consideration for the covenant. The employer must provide such notice clearly and conspicuously in a separate document, which must direct the employee's attention to the specific section of the document containing the non-competition covenant, and must be signed by the employee to be effective.

Penalties

The amendments provide that an employer shall not enter into, present to an employee or prospective employee as a term or employment, or attempt to enforce a non-competition covenant that is void under the statute. In addition to actual damages, the amendments provide for a penalty of $5,000 per employee or prospective employee harmed by violation of the statute. The Colorado Attorney General or the affected employee can bring an action for injunctive relief and to recover penalties. A court may reduce or waive the penalty if an employer shows that the act or omission giving rise to the legal action was in good faith and that the employer had reasonable grounds to believe its act or omission was not a violation of the statute. In a private legal action, the employee may recover attorney fees in addition to actual damages and costs.

Moreover, criminal liability is possible. If a person uses "force, threats, or other means of intimidation to prevent [an employee] from engaging in any lawful occupation at any place the [employee] sees fit," the person commits a class 2 misdemeanor, which could lead to up to 120 days in prison and/or a $750 fine. The scope and application of criminal liability remain to be seen, but clearly it is an additional deterrent to recklessly imposing restrictive covenants in violation of the statute.

Colorado Venue and Law Required

The amendments limit venue clauses that attempt to require a Colorado employee to adjudicate a non-competition covenant outside of Colorado. In addition, they provide that regardless of a contrary choice-of-law provision, Colorado law governs such covenants for a worker who, at the time of termination of employment, primarily resided and worked in Colorado.

Recommendations

Before presenting or requiring non-competition or customer non-solicitation covenants after August 10, clients should review such covenants carefully to ensure that they comply with the amended statute. Companies should avoid routinely imposing restrictive covenants upon whole classes of employees, and instead should apply covenants selectively only to employees who meet the HCE salary thresholds. Also, restrictive covenants must be tailored specifically to protecting trade secrets. In addition, companies should prepare systematically to meet the notice requirements.

Key Takeaways

- On August 10, a statutory amendment goes into effect that substantially limits the enforceability of non-competition and non-solicitation covenants under Colorado law.
- Employers that attempt to enforce invalid non-compete and/or non-solicitation covenants may be subject to civil penalties and even criminal liability.
- Employers should audit their practices regarding the use of non-compete and non-solicitation provisions and make sure they are acting in compliance with the new Colorado law.

This article was drafted by Michael Belo, an attorney in Spencer Fane's Denver office. For more information, please visit www.spencerfane.com.