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New Law Expands Prohibitions on Restrictive Covenant Agreements With Illinois Employees

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Illinois Governor J.B. Pritzker signed new legislation on August 13 amending the Illinois Freedom to Work Act (the Act). The amended Act codifies certain existing common law principles and imposes new requirements that will greatly impact the enforceability of noncompetition and nonsolicitation agreements entered into with employees after January 1, 2022. Illinois employers should review and update any form restrictive covenant agreements to ensure compliance.

The Act contains separate definitions for "covenants not to compete" and "covenants not to solicit." A "covenant not to compete" includes not only an agreement restricting an employee from working for another employer for a specific period of time, in a specific geographic area, or in a similar role, but also includes an agreement that "imposes adverse financial consequences on the former employee if the employee engages in competitive activities" after the termination of employment. The definition specifically excludes nonsolicitation agreements, confidentiality agreements, agreements prohibiting the use or disclosure of trade secrets, invention assignment agreements, agreements related to the purchase or sale of the goodwill of a business, "garden leave" agreements, and covenants not to reapply for employment.

The Act defines a "covenant not to solicit" to include agreements that restrict an employee from (1) soliciting for employment the employer's employees; or (2) soliciting, for the purpose of selling products or services of any kind to, or from interfering with the employer's relationship with, the employer's clients, vendors, suppliers, or other business relationships.

The Act greatly expands prohibitions on both noncompetition and nonsolicitation agreements with certain Illinois workers. Most significantly, the Act prohibits noncompetition agreements with any employee earning $75,000 or less annually ("earnings" includes salary, earned bonuses, earned commissions, and any other form of taxable compensation reflected—or expected to be reflected—as wages tips or other compensation on an employee's W-2, plus any elective deferrals such as employee contributions to a 401(k) plan, a 403(b) plan, a flexible, spending account, or a health savings account, or commuter benefit-related deductions), and bars nonsolicitation agreements with employees earning $45,000 or less (amounts that will increase as specified in the Act beginning January 1, 2027).

Additionally, the law bans noncompetition agreements with employees covered by a collective bargaining agreement under the Illinois Public Labor Relations Act or the Illinois Education Labor Relations Act, and individuals employed in construction (subject to certain exceptions described in the Act). The Act further prohibits employers from entering into noncompetition or nonsolicitation agreements with any employee who is furloughed or whose employment is terminated due to circumstances related to the COVID-19 pandemic (or similar circumstances), unless enforcement of the agreement includes compensation equivalent to the employee's base salary at the time of termination, minus compensation earned through subsequent employment during the period of enforcement.

The Act also imposes significant new notice requirements that will impact the enforceability of restrictive covenant agreements. For any noncompetition or nonsolicitation agreement to be enforceable (regardless of the employee's earnings), employers are required to provide employees with a copy of the covenant at least 14 calendar days before the commencement of the employee's employment or to provide the employee

with at least 14 days to review the agreement before signing (though an employee may voluntarily elect to sign before the expiration of the 14-day period), and must also advise employees in writing to consult with an attorney before signing. Any agreement that does not meet these notice requirements is deemed "illegal and void."

In addition to creating new salary thresholds and notice requirements, the Act also codifies several Illinois common law doctrines regarding the enforceability of noncompetition and nonsolicitation agreements. Specifically, the law now makes clear that restrictive covenant agreements will be enforced only if (1) the employee receives adequate consideration; (2) the agreement is ancillary to a valid employment relationship; (3) the agreement is no greater than is required for the protection of a legitimate business interest of the employer; (4) the agreement does not impose undue hardship on the employee; and (5) the agreement is not injurious to the public.

The Act defines "adequate consideration" as either (1) two years of continued employment after signing the agreement; or (2) other adequate consideration, "which consideration can consist of a period of employment plus additional professional or financial benefits or merely professional or financial benefits adequate by themselves." The Act does not define "professional or financial benefits," but could conceivably be argued to include a benefit such as a bona fide promotion or additional (non-illusory) compensation. The law also clarifies that courts must consider the "totality of the facts and circumstances of the individual case" in determining whether an agreement protects the legitimate business interests of the employer. Such factors include, but are not limited to, an employee's access to confidential information or exposure to customers and the "near permanence" of the customer relationships at issue. Courts may also consider the length of the restriction, the geographic scope of the restriction, and the scope of the restricted activities.

Significantly, the Act also codifies various "blue penciling" and severability principles under Illinois law, clarifying that courts have the discretion to "reform or sever" provisions from restrictive covenants, rather than holding the covenant unenforceable. The Act notes that courts may consider a number of factors in exercising this discretion, including "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 such reformation, and whether the parties included a clause authorizing such modifications in their agreement."

The new law is also likely to have an impact on litigation involving post-employment restrictive covenants. If an employer seeks to enforce a noncompetition or nonsolicitation agreement against an employee and the employee prevails in court or an arbitration, the Act permits the employee to recover reasonable attorney fees, costs, and "appropriate relief" arising from the litigation. The Act also gives the Illinois Attorney General the right to initiate or intervene in a civil action when "the Attorney General has reasonable cause to believe that any person or entity is engaged in a pattern and practice prohibited by this Act." The Act takes effect on January 1, 2022 and does not apply to any agreements entered with employees prior to that date. However, before the end of the year, employers should review of any form agreements containing restrictive covenants to ensure compliance with the new law.■

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