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Business Success

For You
Thursday April 23, 2009

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When "Noncompetes" Come Back To Haunt You

Cliff Ennico

"Several years ago, I ran a small retail business in my hometown. I sold out to a competitor, who made me sign a noncompete agreement saying that I wouldn't run or own a similar business anywhere in my home state for a period of 10 years. I didn't think that would be a problem, as I had landed a job with a big corporation and never thought I would go back into that business. Well, the corporate job didn't pan out, and an old college friend of mine said he would provide me with financing if I opened up another retail store like the one I had. The problem is that stupid noncompete I signed. Several people have told me not to worry because noncompetes like this are rarely enforced, especially since it's been over six years since I signed the noncompete. But I'm afraid of getting sued, and the noncompete has four years yet to go. Do I have any recourse here?"

When selling a business, the buyer always asks the seller to sign a noncompete agreement to ensure that the seller doesn't move across the street, open up a new store, and steal all the business from the store he or she just sold. The buyer's lawyer who drafts the agreement always tries to make these as broad as possible, and the seller's lawyer always tries to keep the noncompete as narrow as possible so the seller can still make a living if he's forced by circumstances (as this reader is) to go back into the business.

A lot of people think noncompetes aren't enforceable and sign them without thinking. That's a very bad idea, because in almost all states noncompete agreements are indeed enforceable if they are "reasonable in scope and time." In plain English, that means:

- the noncompete cannot last forever, or for an unreasonably long period of time; and
- the noncompete must prohibit competition only within a radius that is reasonable for the type of business.

For example, a noncompete that forbids the owner of a doughnut shop from opening another shop anywhere in the state is almost certain to be stricken down as "unreasonable," since studies show the average person will not travel more than one or two miles out of their way to buy a doughnut and coffee for breakfast. On the other hand, a noncompete agreement forbidding the seller of a software publishing business from creating or selling similar software products anywhere in the United States for several years might well be enforced as "reasonable," since most software products are sold over the Web and so are not limited to a local marketplace.

In short, whether or not a noncompete will be enforced will depend on the type of business, the actual language used in the noncompete, and the laws of your state.

But even if a noncompete is technically unenforceable, it can still muck up your life.

The sad and dirty truth is that most people who want you to sign a noncompete agreement don't have any intention of winning their day in court. All they want to do is get into court. Once they're there, they will ask the court for an "injunction" -- a restraining order forbidding you from competing until the lawsuit is resolved. If the court issues an injunction, you're toast. Even though you have an excellent chance of winning the lawsuit, getting that judgment will take years of your life and cost you thousands and thousands of dollars in legal fees. By the time you get your judgment, it won't be

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worth anything.

When faced with a noncompete agreement from your past, talk to a local attorney, and scrutinize the exact language of the noncompete very carefully. In this case, one possible loophole is the fact that it prohibits the reader from "running or owning" a competing business. It doesn't say anything about "being employed by," "managing" or "working for" a competing business elsewhere in the state.

So -- if your local attorney agrees that's how the agreement should be interpreted -- you could set up the business with your old college friend as the sole owner. You would then be employed by him for the four years remaining on your noncompete, earning a fixed salary as well as a percentage of the business profits each year as a performance incentive. At the end of the four years, you would have the option of buying an ownership interest in the business from your friend for a specified price.

I would also suggest opening the business as far away from your buyer as possible, and avoid soliciting business from your old customers. That way, even if he finds out you're back in business, the fact that you're not actually hurting him may lead him to ignore the noncompete, or offer you the chance of "buying out" the noncompete for a reasonable price.

Cliff Ennico (cennico@legalcareer.com) is a syndicated columnist, author and former host of the PBS television series "Money Hunt." This column is no substitute for legal, tax or financial advice, which can be furnished only by a qualified professional licensed in your state. To find out more about Cliff Ennico and other Creators Syndicate writers and cartoonists, visit our Web page at www.creators.com.

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Chris Lytle's Sales Tip -- Selling Better While Having Fun

Chris Lytle's Sales Tip: "When I'm selling at my best, I'm more playful," said a seminar participant recently. "Work is more fun than fun," suggests Noel Coward. Selling at your best is fun. You smile more. You are more at ease with your customers and they react accordingly. Customers sit through plenty of boring meetings. What can you do to add a measure of "playfulness" to your next customer encounter?

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Quote of the Day

Bobby Unser, race car driver

"Success is where preparation and opportunity meet."

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