Illinois Legislature Passes Comprehensive Non-Compete Legislation

Labor & Employment Law Update

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As reported in prior blogs, the Illinois legislature for several months has been considering amendments to the Illinois Freedom to Work Act that apply to non-compete and non-solicitation restrictions. Amundsen Davis attorneys worked closely with the Illinois Chamber of Commerce to protect the interests of employers as much as possible during the legislative process.

The legislature has now passed SB672. It is generally viewed as a compromise between employer and employee interest groups. It is not a ban on restrictive covenants, but it does impose important limits on them.

The legislature will send SB672 to Governor Pritzker for signature before the end of the month. The governor then will have up to 60 days from receipt to act. It is widely expected that the governor will sign the bill, probably sometime in August.

The amendments are effective for any contract entered into after January 1, 2022.

The legislation is comprehensive and detailed, and should be read in its entirety. However, important highlights of the new legislation include the following:

Income Thresholds for Non-Compete and Non-Solicitation Agreements

One of the most important changes is the establishment of income thresholds for non-compete and non-solicitation agreements.

For agreements entered into on or after January 1, 2022, an employee's actual or expected annualized earnings must exceed $75,000 per year in order for the employee to be subject to a non-compete clause. This threshold increases to $80,000 on January 1, 2027, $85,000 on January 1, 2032, and $90,000 on January 1, 2037. A non-compete agreement does not include a confidentiality agreement or a covenant prohibiting the use or disclosure of trade secrets or inventions, so those contracts can continue to be used regardless of the employee's income.

Additionally, for agreements entered into on or after January 1, 2022, an employee's actual or expected annualized earnings must exceed $45,000 per year in order for the employee to be subject to a non-solicitation clause. This threshold increases to $47,500 on January 1, 2027, $50,000 on January 1, 2032, and $52,500 on January 1, 2037. A non-solicitation agreement includes any agreement that bans solicitation of not only customers or prospective customers, but also employees, and vendors, among other categories.

"Earnings" for purposes of these thresholds includes earned salary, earned bonuses, earned commissions, or any other form of compensation reported on an employee's IRS Form W-2.

The legislation also prohibits employers from entering into a covenant not to compete or not to solicit with any employee who an employer terminates, furloughs, or lays off as the result of business circumstances or governmental orders related to COVID-19, or under circumstances that are similar to the COVID-19 pandemic, unless the employer pays the employee pursuant to a formula contained in the Act. It also prohibits covenants not to compete for individuals covered by a collective bargaining agreement under the Illinois Public Labor Relations Act, the Illinois Educational Labor Relations Act, or certain individuals employed in the construction industry. Construction employees who primarily perform management, engineering or architectural, design or sales functions for the employer; or are a shareholder, partner, or owner in any capacity for of the employer may be covered by a covenant to compete or a covenant not to solicit.

Pre-Signing Notice and Review Period

The legislation adds a new Section 20 which provides that non-compete and non-solicitation clauses are illegal and void unless (1) the employer advises the employee in writing to consult with an attorney before entering into the covenant; and (2) the employer provides the employee with a copy of the covenant at least 14 calendar days before the commencement of the employee's employment or the employer provides the employee with at least 14 calendar days to review the covenant.

Attorney's Fees for Employees Who Prevail in Litigation

Many restrictive covenants provide that the employer may recover its attorney's fees if it prevails in litigation to enforce a covenant. The new legislation levels the playing field by providing that, if an employee prevails on a claim to enforce a covenant not to compete or a covenant not to solicit, the employee shall recover his or her attorney's fees and costs.

Attorney General Enforcement

The amendments also provide for the Illinois Attorney General to investigate and prosecute abusive restrictive covenant practices. If the Attorney General has reasonable cause to believe that an employer is engaged in a pattern and practice prohibited by this Act, the Attorney General may initiate or intervene in a civil action in the name of The People of the State in any appropriate court to obtain appropriate relief. The Act grants the Attorney General broad investigative powers and provides for a wide range of remedies including civil penalties not to exceed $5,000 for each violation or $10,000 for each repeat violation within a 5 year period.

Adequate Consideration Defined

The definition of "adequate consideration," consistent with the *Fifield v. Premier Dealer Services* decision that was discussed in detail in a prior blog is that an "at will" employee must work for at least two years after entering into the restrictive covenant contract in order for it to be enforceable. Notably, the new statutory standard of "at least two years" actually is stricter than the standard that courts developed in the wake of *Fifield*. Courts applying *Fifield*, particularly in the federal system, used two years as a rule of thumb, but were willing to find adequate consideration based on lesser periods of post-contract employment (*e.g.*, 18 months) in certain cases, such as when the employee voluntarily resigned. The new legislation would appear to deny courts such flexibility.

The amendments also provide, alternatively, that the employer can provide "a period of employment plus additional professional or financial benefits, or merely professional or financial benefits adequate by themselves." After *Fifield*, many employers sought to avoid potential consideration problems by providing a monetary payment to the at-will employee as additional consideration for the agreement; otherwise they would run the risk that the restrictive covenant would be deemed unenforceable if the employee resigned or was terminated less than two years after signing the restrictive covenant agreement. Unfortunately, as with *Fifield* itself, this new provision provides no guidance as to what "professional or financial benefits" would be deemed sufficient as an alternative to two years or more of at will employment.

Definition of Employer's "Legitimate Interest" and Standard for Enforceability

SB672 adds new Sections 7 and 15 to the Act which essentially codify the approaches to determining the legitimate interest of the employer, and determining whether the restriction is enforceable to protect the interest, that were established in 2011 by the Illinois Supreme Court in *Reliable Fire Equipment Co. v. Arredondo* case also discussed in a previous blog. This approach provides that, while exposure to "near-permanent" client relationships and the possession of confidential information are legitimate interests, there is no limit as to what can be a protectable interest and the "totality of the facts and circumstances" must be considered by the court in every case. Once the interest is identified, the restrictions must be deemed reasonable according to various criteria, such as whether they are no more burdensome than necessary to protect the interest of the employer, and whether they are injurious to the public. No single factor is determinative and the same covenant could be enforceable in one case, yet not be enforceable in a different case. These provisions codify the approach that courts and practitioners have been following since *Reliable Fire*.

Reformation of Overbroad Restrictions

As with the definition of "adequate consideration," and the provisions regarding an employer's legitimate interests and how to determine whether a restriction is reasonably tailored to protect the interest, SB672 adds a new Section 35 that essentially codifies existing law regarding the reformation of overbroad covenants. It provides that, while "extensive judicial reformation" may be against the public policy of the State of Illinois, a court may exercise its discretion to modify an unreasonable or overbroad restriction rather than hold that it is wholly unenforceable. Factors to be considered "include 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."

As stated above, these amendments apply to any restrictive covenant contract entered into after January 1, 2022. Employers obviously need to make sure any contracts entered into after that date fully comply with the new law. In addition, employers who would like to get restrictive covenants in place before these rules go into effect would be well-advised to work with experienced employment counsel to accomplish that objective in compliance with existing law.