Covenants Not To Compete
(TROs and Preliminary Injunctions)

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Special Superior Court Judge
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A. Temporary Restraining Order.

Purpose: Preserve status quo so that court can rule on a preliminary injunction.

Notice to adverse party: A TRO may be granted without written or oral notice to the adverse party or to that party's attorney if:

1. It clearly appears from specific facts shown by **affidavit** or by **verified complaint** that immediate and irreparable injury, loss or damage will result to the applicant before the adverse party or that party's attorney can be heard in opposition, and

2. The applicant's attorney certifies to the court **in writing** the efforts, if any, that have been made to give the notice and the reasons supporting the claim that notice should not be required. Rule 65(b).

Content of TRO: Every temporary restraining order granted without notice shall:

RULE 65(b)

1. Have date and hour of issuance endorsed on order;

2. Be filed forthwith in the clerk's office and entered of record;

3. Define the injury and state why it is irreparable;

4. State why the order was granted without notice;

5. Shall expire not more than 10 days from entry.

RULE 65(d)

6. Set forth the reasons for its issuance;

7. Be specific in terms;

8. Describe in reasonable detail, and not by reference to the complaint or other document, the act or acts enjoined or restrained.

Duration:

1. No more than 10 days from entry.
2. May be extended for one additional 10 day period if applicant makes request for extension within original 10-day period and shows good cause for extension. Reasons for granting any extension must be entered of record. May also be extended with consent of enjoined party. Rule 65(b).

Security. No restraining order or preliminary injunction shall issue except upon the giving of security by the applicant, **in such sum as the judge deems proper**, for the payment of such costs and damages as may be incurred or suffered by any party who is found to have been wrongfully enjoined or restrained. Rule 65(c).

> The trial court has power not only to set the amount of security but to dispense with any security requirement whatsoever where the restraint will do the defendant no material damage, where there has been no proof of likelihood of harm and where the applicant for equitable relief has considerable assets and is able to respond in damages if defendant does suffer damages by reason of a wrongful injunction. *Keith v. Day,* 60 N.C. App. 559, 299 S.E.2d 296 (1983) (quoting *Federal Prescription Service, Inc. et al. v. American Pharmaceutical Assoc.,* 636 F. 2d 755, 759 (D.C. Cir. 1980)). However, "any order that precludes one from earning a livelihood and that has the potential to destroy that person's means of income production for years to come is too potent to issue without security." *Id.*

B. Preliminary Injunctions.

Purpose: Preserve the status quo until a trial on the merits. *See Lambe v. Smith,* 11 N.C. App. 580, *582, 181 S.E.2d 783,784 (1971).*

Burden of proof: At hearing on preliminary injunction, the party who obtained the TRO must go forward with request for preliminary injunction, or court must dissolve the TRO. Rule 65(b). *See Pruitt v. Williams,* 288 N.C. 368, 218 S.E.2d 348 (1975).

Notice to adverse party. No preliminary injunction shall be issued without notice to the adverse party. Rule 65(a). "Notice" is not defined. However, a preliminary injunction can only be issued after notice and a hearing, which affords the adverse party an opportunity to present evidence in his behalf. *Lambe v. Smith,* 11 N.C. App. 580, 181 S.E.2d 783 (1971). A preliminary injunction entered without notice affects a "substantial right" and is immediately appealable. *See Perry v. Baxley Development, Inc.* 188 N.C. App. 158, 655 S.E.2d 460 (2008).

Interaction with Rule 6(d). Rule 6(d) requires 5 days notice before hearing on a motion. Also requires that affidavits be served with the motion. Formal compliance with 6(d) may not be necessary if opposing party has adequate notice to allow preparation of a defense.

Grounds for granting motion for preliminary injunction.

1. A preliminary injunction is an extraordinary measure taken by a court to preserve the status quo of the parties during litigation. It will be issued only (1) If plaintiff is able to show the likelihood of success on the merits of his case and (2) if plaintiff is likely to sustain irreparable loss unless the injunction is issued, or if, in the opinion of the court, issuance is necessary for the protection of plaintiff's rights during the course of litigation. *See A.E.P. Indus., Inc. v. McClure,* 308 N.C. 393, 302 S.E.2d 754 (1983); *Waff Bros., Inc. v. Bank,* 289 N.C. 198, 221 S.E. 2d 273 *Triangle Leasing Company, Inc. v. McMahon,327 N.C. 224, 393 S.E.2d 854 (1990).*
2. To establish a likelihood of success on the merits, the employer must make a *prima facie* showing that the covenant is valid and enforceable against the employee. *NovaCare Orthotics & Prosthetics East, Inc. v. Speelman,* 137 N.C. App. 471, 528 S.E.2d 918 (2000).

C. Applying the requirements of Rule 65 to covenant not to compete cases.

Requirement that plaintiff show likelihood of success on the merits of the case.

1. **"**Where a preliminary injunction is sought to enforce a non-competition clause in an employment contract, the Supreme Court has held that the employment agreement itself must be valid and enforceable in order for the employer to be able to show the requisite likelihood of success on the merits". *Triangle Leasing Co. v. McMahon,* 327 N.C. 224, 227-28, 393 S.E.2d 854, 857 (1990) (citing *A.E.P. Industries,* 308 N.C. 393, 302 S.E.2d 754).

2. A covenant in an employment agreement providing that an employee will not compete with his former employer is "not viewed favorably in modern law". *Hartman v. W.H.Odell & Assocs.,* 117 N. C. App. 307, 311, 450 S.E.2d 912, 916 (1994).

3. A covenant not to compete is enforceable if it is: (1) in writing, (2) made part of a contract of employment; (3) based on valuable consideration; (4) reasonable both as to time and territory; and (5) not against public policy. *Triangle Leasing* Co., Inc. v. *McMahon,* 327 N.C. 224, 228, 393 S.E.2d 854, 857 (1990); *Moses H. Cone Mem'l Health Servs. Corp. v. Triplett,* 167 N.C. App. 267, 605 S.E.2d 492, 497 (2004).

    a. **Requirement that the covenant be in writing**. If covenant was a part of original, oral contract of employment, it was founded on valuable consideration even though covenant was not put into writing and signed until after defendant started work. *See Robins & Weill,Inc. v. Mason,* 70 N.C.App. 537, 320 S.E.2d 693 (1984). In addition to being in writing the covenant must be signed by the one who agrees not to compete. *See G.S.*75-4.

    b. **Requirement that agreement be part of contract of employment**. Some cases suggest that covenant must be entered into as part of "original contract of employment." *See New Hanover Rent-A-Car, Inc. v. Martinez,* 136 N.C. App. 642, 644, 525 S.E.2d 487 (2000). However, if covenant was part of original, oral contract of employment and was supported by consideration, it was enforceable even though not put into writing and signed until after defendant started work. *See Robins & Weill, Inc. v. Mason,* 70 N.C. App. 537, 320 S.E.2d 693 (1984).

    c. **Requirement that agreement be supported by consideration**. Where the covenant is entered into in connection with an employee's being hired for a job, it is generally held that mutual promises of employer and employee furnish valuable considerations each to the other for the contract. *Hejl v. Hood, Hargett & Assoc.,* 674 S.E.2d 425, 2009 N.C. App. Lexis 377, (2009) citing *Reynolds & Reynolds Co. v. Tart,* 955 F. Supp 547, 553 (W.D.N.C.)

(quoting *Greene Co. v. Kelley,* 261 N.C. 166, 168, 134 S.E.2d 166, 167 (1964). However, when the restrictive covenant is entered into after an already existing employment relationship, the covenant must be supported by "new consideration." *Greene Co.,* 261 N.C. at 168, 134 S.E.2d at 167.

Our courts have held the following benefits all meet the "new" or "separate" consideration required for a non-compete agreement entered into after a working relationship already exists:

- continued employment for a stipulated amount of time, *Amdar, Inc. v. Satterwhite,* 37 N.C. App. 410, 246 S.E.2d 165, *disc. Review denied,* 295 N.C. 645, 248 S.E.2d 249 (1978);

- a raise, bonus, or other change in compensation, *Clyde Rudd & Associates, Inc. v. Taylor,* 29 N.C. App. 679, 225 S.E.2d 602 (1976); a promotion, *Associates, Inc. v. Taylor,* 29 N.C. App. 679, 225 S.E.2d 602 (1876);

- additional training, *Safety Equipment Sales & Service, Inc. v. Williams,* 22 N.C. App. 410, 206 S.E.2d 745 (1974); uncertificated shares, *Kinesis Adver., Inc. v. Hill,* 187 N.C. App. 1, 652 S.E.2d 284 (2007);

- or some other increase in responsibility or number of hours worked, *Whittaker Gen. Med. Corp. v. Daniel,* 324 N.C. 523, 379 S.E.2d 824 (1989).

- "The slightest consideration is sufficient to support the most onerous obligation, the inadequacy… is for the parties to consider at the time of making the agreement, and not for the court when it is sought to be enforced. *Catawba Valley Machinery Co. v. Insurance Co.,* 13 N.C. App. 85, 90-91, 185 S.E.2d 308, 311-12 (1971) (quoting *Young v. Highway Commission,* 190 N.C. 52, 57, 128 S.E. 401, 403 (1925), *cert denied,* 280 N.C. 302, 186 S.E.2d 176 (1972).

d. **Requirement that covenant be reasonable as to time and territory**.

- **Time.** "A five-year time restriction is the outer boundary which our courts have considered reasonable, and even so, five-year restrictions are not favored." *Farr Assocs.,* 138 N.C. App. At 280, 530 S.E. 2d at 881. See *Welcome Wagon, Inc. v. Pender,* 255 N.C. 244, 120 S.E.2d 739 (1961). See also *Kennedy v. Kennedy,*160 N.C. App. 1, 584 S.E.2d 328 (2002) (enforcing covenant for a period of 3 years); *Precision Walls, Inc. v. Servie,* 152 N.C. App. 630, 568 S.E.2d 267 (2002) (enforcing 1 year covenant); *Triangle Leasing Co., v. McMahon,* 327 N.C. 224, 393 S.E.2d 854 (1990)(upholding 2 year restriction).

When a non-compete reaches back to include clients of the employer during some period in the past, that look-back period must be added to the restrictive period to determine the real scope of the time limitation. *Farr Assocs.* at 280, 530 S.E.2d at 881.

- **Territory. "**A restriction as to territory is reasonable only to the extent it protects the legitimate interests of the employer in maintaining [its] customers." *Manpower, Inc. v. Hedgecock,* 42 N.C. App. 515, 523, 257 S.E.2d 109, 115 (1979).

"To prove that a geographic restriction in a covenant not to compete is reasonable, an employer must first show where its customers are located and that the geographic scope of the covenant is necessary to maintain those customer relationships." *Hartman v. Odell and Assoc., Inc.,* 117 N.C. App. 307, 312, 450 S.E.2d 912, 917 (1994), *disc. review denied,* 339 N.C.612, 454 S.E. 2d 251 (1995).

"The territory embrace[d] [by the covenant] shall be no greater than is reasonably necessary to secure the protection of the business or good will of the employer." *A.E.P. Industries v. McClure,* 308 N.C. 393, 408, 302 S.E.2d 754, 763 (1983) (quoting *Asheville Associates v. Miller and Asheville Associates v. Berman,* 255 N.C. 400, 404, 121 S.E.2d 593, 595 (1961).

Factors to determine in deciding whether geographic scope of restriction is reasonable include (1) area or scope of restriction, (2) area assigned to employee, (3) area in which employee actually worked, (4) area in which employer operated, (5) nature of business involved, and (6) nature of employee's duty and his knowledge of business operation. *Farr Assocs.,* 138 N.C. App. 276, 530 S.E.2d 878 (2000). See also *Visionair, Inc. v. James,* 167 N.C. App. 504, 606 S.E.2d 359 (2004) (holding covenant providing that employee could not compete with employer within the Southeast was overbroad and unenforceable); *Masterclean of North Carolina, Inc. v. Guy,* 82 N.C. App. 45, 345 S.E.2d 692 (1986)(refusing to enforce covenant that prohibited former employee from competing anywhere in the United States); *Starkings Court Reporting Services, Inc. v. Collins,* 67 N.C. App. 540, 313 S.E.2d 614 (1984) (declining to enforce covenant prohibiting reporter from engaging in court reporting within 50 miles of county).

Restrictions barring an employee from working in an identical position for a direct competitor are valid and enforceable. *Precision Walls Inc., v. Servie,* 152 N.C. App. 630, 568 S.E.2d 267 (2002). However, restrictive covenants are unenforceable where they prohibit the employee from engaging in future work that is distinct from the duties actually performed

by the employee. *Henley Paper Co. v. McAllister,* 253 N.C.529, 117 S.E.2d 431 (1960).

The time and geographic limitations of a covenant not to compete must be considered in tandem, such that "[a] longer period of time is acceptable where the geographic restriction is relatively small, and vice versa." *Farr Associates Inc. v. Baskin,* 138 N.C. App. at 280, 530 S.E.2d at 881 (citing *Jewel Box Stores Corp. v. Morrow,* 272 N. C. 659, 158 S.E.2d 840 (1968)).

e. **Requirement that covenant not contravene public policy**. Distinction is between whether there will be an inconvenience to the public or whether there will be a substantial question of potential harm. For covenants not to compete concerning doctors see *Iredell Digestive Disease Clinic v. Petrozza,* 92 N.C. App. 21, 24, 373 S.E. 2d 449, 451 (1988), *affirmed,* 324 N.C. 327, 377 S.E. 2d 750 (1989), where the court stated "A covenant not to compete between physicians is not contrary to public policy if it is intended to protect a legitimate interest of the covenantee and is not so broad as to be oppressive to the covenantor or the public…If ordering the covenantor to honor his contractual obligation would create a substantial question of potential harm to the public health, then the public interests outweigh the contract interests of the covenantee, and the court will refuse to enforce the covenant…But if ordering the covenantor to honor his agreement will merely inconvenience the public without causing substantial harm, then the covenantee is entitled to have his contract enforced". See also *Kennedy v. Kennedy,* 160 N.C. App. 1, 584 S.E.2d 328 (2003).

In order to determine whether there is a substantial question of potential harm to the public health, the court will examine: (1) the shortage of specialists in the field in the restricted area; (2) whether the enforcement of the covenant creates a monopoly in that specialty area; and (3) the patients' interest in having a choice in the selection of a physician. *Statesville Medical Group v. Dickey,* 106 N.C. App. 669, 673, 418 S.E.2d 256, 259, *review denied,* 333 N. C. 257, 424 S.E.2d 922 (1992).

The "public policy" requirement has also been used interchangeably with whether the covenant protects a "legitimate business interest" of the employer. *Professional Liability Consultants, Inc. v. Todd,* 122 N.C. App. 212, 218, 468 S. E. 2d 578, 582 (1996); *Hartman v. Odell & Assocs., Inc.,* 117 N. C. App. 307, 311, 450 S. E. 2d 912, 916 (1994).

Plaintiff is likely to suffer irreparable loss unless the injunction is issued, or if, in the opinion of the court, issuance is necessary for the protection of plaintiff's rights during the course of litigation.

1. Our courts have held that intimate knowledge of the business operations or personal association with customers provides an opportunity to a former employee to injure the business of the covenantee. *See United Labraories, Inc. v. Kuykendall,* 322 N.C. 643, 370 S.E.2d 375 (1988).

2. In *A.E.P. Industries, v. McClure,* 308 N.C. 393, 302 S.E.2d 754 (1983) the North Carolina Supreme Court accepted plaintiff's argument that:

> "[in a] noncompetition agreement, breach is the controlling factor and injunctive relief follows almost as a matter of course; damage from the breach is presumed to be irreparable and the remedy at law is considered inadequate. It is not necessary to show actual damage by instances of successful competition, but it is sufficient if such competition, in violation of the covenant, may result in injury."
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> The court consequently held that "[w]here the primary ultimate remedy sought is an injunction; where the denial of a preliminary injunction would serve effectively to foreclose adequate relief to plaintiff; where no "legal" (as opposed to equitable) remedy will suffice; and where the decision to grant or deny a preliminary injunction in effect results in a determination on the merits, plaintiff has made a showing that the issuance of a preliminary injunction is necessary for the protection of its rights during the course of litigation". Id. at 410, 302 S.E.2d at 764.

D. Issuance of preliminary injunction.

1. Similar to the order granting the TRO, the order granting the preliminary injunction shall (1) set forth the reasons for its issuance; (2) shall be specific in terms; and (3) shall describe in reasonable detail, and not by reference to the complaint or other document, the act or acts enjoined or restrained. Rule 65(d).

2. Interaction with Rule 52(a)(2). Findings of fact and conclusions of law are necessary on the granting or denying of a preliminary injunction or any other provisional remedy **only** when required by statute expressly relating to such remedy or requested by a party. Rule 52(a) (2). Absence a request by a party that the court make findings of fact and conclusions of law, the court is required to state only the reasons for its issuance. See *Pruitt v. Williams,* 25 N.C. App. 376, 213 S.E.2d 369 (1975).

3. The injunction is binding only upon the parties to the action, their officers, agents, servants, employees and attorneys, and upon those persons in active concert or participation with them who receive actual notice in any manner of the order by personal service or otherwise. Rule 65(d).

4. Security. No restraining order or preliminary injunction shall issue except upn the giving of security by the applicant, **in such term as the judge deems proper**, for the payment of such costs and damages as may be incurred or suffered by any party who is found to have been wrongfully enjoined or restrained. Rule 65(c).

   The trial court has power not only to set the amount of security but to dispense with any security requirement whatsoever where the restraint will do the defendant no material damage, where there has been no proof of likelihood of harm and where the applicant for equitable relief has considerable assets and is able to respond in damages if defendant does suffer damages by reason of a wrongful injunction. *Keith v. Day,* 60 N.C. App. 559, 299 S.E.2d 296 (1983) (quoting *Federal Prescription Service, Inc. et al. v. American Pharmaceutical Assoc.,* 636 F. 2d 755, 759 (D.C. Cir. 1980)). However, “any order that precludes one from earning a livelihood and that has the potential to destroy that person’s means of income production for years to come is too potent to issue without security.” *Id.* For examples of cases in which a bond was set see *Barr-Mullin, Inc. v. Browning,* 108 N.C. App. 590, 424 S.E.2d 226 (1993)(trial court required $10,000 bond for injunction barring former employee and his new company from marketing software); *Curtis1000, Inc. v. Youngblade,* 878 F. Supp. 1224 (D. Iowa 1995)(bond of $200,000 for preliminary injunction enjoining salesperson from violating covenant not to compete); *Standard Register Co. v. Cleaver,* 30 F. Supp. 2d 1084 (D. Ind. 1998)(requiring $150,000 bond for preliminary injunction).

"Wrongfully enjoined or restrained" means:

- Final adjudication substantially favorable to the defendant on the merits of plaintiff's claim. *See Industrial Innovators, Inc. v. Myrick-White,* 99 N.C. App. 42, 392 S.E.2d 425 (1990); or

- Final adjudication that does not address the merits-e.g., on jurisdictional grounds-if the defendant also shows that he or she was entitled to engage in the enjoined activity, *see id;* or

- Voluntary dismissal (by stipulation of parties). *See id.*

5. No security required of State of N.C., or its counties or municipalities or officers or agencies acting in official capacity. Damages may be awarded against these parties. Rule 6(c).

6. Surety submits to court's jurisdiction of the court and irrevocably appoints clerk of court as agent for service of process. Rule 65(c).

7. Liability may be enforced upon motion (served on clerk) or by independent action. Rule 65(c).

8. Wrongfully enjoined or restrained party may seek damages against party that procured the injunction and the surety by motion. No need to show malice or lack of probable cause if proceeding by motion. No right to jury trial if matter heard upon motion.

E. Prohibitory and Mandatory Injunctions.

Injunctions may be classified as "prohibitory" and "mandatory". The former are preventive in character, and forbid the continuance of a wrongful act or the doing of some threatened or anticipated injury; the latter are affirmative in character, and require positive action involving a change of existing conditions—the doing or undoing of an act. *Roberts v.Madison County Realtors Association, Inc.,* 344 N.C. 394, 474 S.E.2d 783 (1996) citing 42 *Am. Jur. 2d Injunctions §9 (1969);* accord *Seaboard Air Line R.R. Co. v. Atlantic Coast Line R.R.,* 237 N.C. 88, 94, 74 S.E.2d 430, 434 (1953).

Mandatory injunctions are disfavored as an interlocutory remedy. "As a general rule, since the purpose of an interlocutory injunction is solely to retain the status quo [pending final resolution on the merits], only a prohibitory injunction is proper [as opposed to a mandatory injunction, which would alter the status quo]. *Roberts v. Madison* citing John F. Dobbyn, *Injunctions In a Nutshell* 163 (1974). However, in *Roberts* the court went on to say that "[H]owever, we note that under circumstances which indicate 'serious irreparable injury to the petitioner if the injunction is not granted,

no substantial injury to the respondent if the injunction is granted, and predictably good chances of success on the final decree by the petitioner, a mandatory interlocutory injunction could properly be issued.'" Citing *Dobbyn* at 167-68.

F. Rewriting unenforceable covenant not to compete.

When the language of a covenant not to compete is overly broad, North Carolina's "blue pencil" rule severely limits what the court may do to alter the covenant. A court at most may choose not to enforce a distinctly separable part of a covenant in order to render the provision reasonable. It may not otherwise revise or rewrite the covenant. *Hartman v. W.H. Odell and Associates, Inc.* 117 N.C. App. 307, 450 S.E.2d 912 (1994). If a non-compete covenant "is too broad to be a reasonable protection to the employer's business it will not be enforced. The courts will not rewrite a contract if it is too broad but will simply not enforce it." *Whittaker General Medical Corporation v. Daniel,* 324 N.C. 523, 528, 379 S.E.2d 824, 828 (1989).

G. Appeal of order granting/denying motion for preliminary injunction.

Appeal of a trial court's ruling on a motion for preliminary injunction is interlocutory. For appellate review to be appropriate, the trial court's ruling must have deprived the appellant of a substantial right that will be lost absent review before final disposition of the case. N.C.G.S. §1- 277, 7A-27. In cases involving an alleged breach of a non-competition agreement and an agreement prohibiting disclosure of confidential information, North Carolina appellate courts have routinely reviewed interlocutory court orders both granting and denying preliminary injunctions, holding that substantial rights have been affected. See, *QSP, Inc., v. Hair,* 152 N.C. App. 174, 566 S.E.2d 851 (2002). On appellate review of a preliminary injunction, the court is not bound by the trial court's findings of fact. Rather, the appellate court reviews the evidence *de novo* and makes its own findings of fact and conclusions of law. *Szymczyk v. Signs Now Corp.,* 168 N.C.App. 182, 606 S.E.2d 728 (2005). Nevertheless, a trial court's ruling on a motion for a preliminary injunction is presumed to be correct, and the party challenging the ruling bears the burden of showing it was erroneous. *Analog Devices, Inc. v. Michalski,* 157 N.C.App. 462, 579 S.E.2d 449 (2003).