Do Non-Compete Clauses Unfairly Handcuff Employees?

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Employers today increasingly require their employees to sign a contract promising not to compete for a period of time after they leave a firm. Employers justify these “non-compete” agreements as necessary to protect trade secrets. The protection of valuable trade secrets is a legitimate concern for many businesses, and because employees are the most likely cause of trade secret leakage for companies, employers justify these non-compete clauses as a vital contractual way to prevent the misappropriation of trade secrets in the first place.

But non-compete agreements can seriously hamstring employees, especially those who specialize in a narrow field and can find it hard to get any job that is not in some way competitive with the former employer. As a result, the majority of states that allow non-compete agreements require that they are reasonable in duration (one to two years is typically the maximum), geography (the restraint shouldn’t apply outside the area where the employer engaged in business), and the nature of the work deemed “competitive.”

In contrast, the few states like California that prohibit these agreements provide only very narrow exceptions, such as when someone is selling a business and therefore getting paid for its “goodwill.”

Besides the effect on individual employees, many believe there are also social costs with non-competes. For example, most employees do not challenge them, so they either stay in a job they do not like, or they leave and try to apply their skills in a completely different area. Some economists see non-competes as a very inefficient way to distribute human capital. They argue that the great success of Silicon Valley compared to the Boston technology corridor (the two started out in the 1980s with equivalent high-tech industries) is evidence of the social value of prohibiting non-competes. The assumed “leakage” of information resulting from Silicon Valley’s highly-mobile labor force actually cross-pollinates new innovation and new startups.

The use of non-competes by employers, however, continues to grow — and in some cases have been required not just of key executives or scientists but also of low-level employees who arguably have no real exposure to confidential information. The most notorious of these cases have involved summer camp counselors and restaurant waiters having to sign non-competes. These non-competes seem designed not for the legitimate protection of trade secrets but simply to make it harder for competitors to hire workers.

In response to such inappropriate uses of non-competes, the White House issued a report in May of 2016 that called upon states to reconsider their laws in light of the legitimate needs of business as well as the potential for abuse. Given the importance of protecting both trade secrets and employee rights, the debate is sure to continue over the proper use of non-compete contracts.