Colorado's Non-Compete Statute Q&A

What Employers Need to Know

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This article helps employers understand how changes to Colorado's non-compete statute affect existing and future restrictive covenant provisions.

The Colorado legislature's significant changes to the state's noncompetition and restrictive covenants statute became effective on August 10, 2022. The Restrictive Employments Agreement Act (Act)[1] is a major overhaul of CRS § 8-2-113, which enshrines Colorado's restrictive covenants restrictions. Previously, the statute only expressly addressed non-competes. Now, the statute addresses restrictive covenants more broadly, including not only non-compete clauses but also provisions addressing the non-solicitation of business and customers, confidentiality provisions, and reimbursement for training and education costs. A previous *Colorado Lawyer* article summarized the new provisions and addressed related considerations for both workers and employers.[2] This article answers common questions about employer compliance and liability under the new provisions.

What Are the Main Changes?

Among other changes, the Act inserted notice requirements to the statute and compensation thresholds that must be satisfied for certain restrictive covenants to lawfully encumber a worker. An employer's failure to comply with the notice provisions may result in not only a void restrictive covenant agreement but also potential enforcement of remedies provisions, including statutory penalties, attorney fees, and damages and costs available to aggrieved job applicants and workers.

Employers with Colorado workers are now juggling the legitimate business needs of protecting their confidential and trade secret information against the legislature's public policy encouraging the free flow of workers (particularly those earning lower wages).

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When Is a Non-Compete Allowed and What Does a Compliant One Look Like?

As an initial matter, the Colorado legislature has removed the management and executive personnel exception for non-compete covenants and augmented the trade secrets exception with an additional compensation requirement. Under the new rubric, a non-compete covenant is only permissible with a worker or prospective worker who, at the time the non-compete is entered into and at the time it is enforced, earns an amount of "annualized cash compensation" (as defined and described in the statute)[3] equivalent to or greater than the threshold amount for highly compensated workers. This amount is determined annually by the Colorado Department of Labor and Employment, Division of Labor Standards and Statistics (Division) via its publication and yearly calculation of annual labor compensation order (PAY CALC Order). The Division's 2023 PAY CALC Order sets the current salary threshold at $112,500.[4] To be valid, the non-compete agreement must also be for the protection of trade secrets and can be no broader than reasonably necessary to protect the employer's legitimate interests in protecting trade secrets.[5] In effect, employers now may only impose non-competes on workers earning over the salary threshold who have access to actual trade secrets and who could legitimately use the trade secrets to improperly compete.

What About Non-Solicitation of Customers/Business Covenants?

Non-solicitation of customer and/or business provisions are now explicitly contemplated by the statute—another big change. Non-solicitation covenants are only valid and enforceable against workers who earn 60% of the threshold amount for highly compensated workers ($67,500 for 2023). Further, the trade secret requirement remains—the non-solicitation covenant may not be broader than reasonably

necessary to protect the employer's legitimate interest in protecting trade secrets.

What Are the New Rules for Other Types of Restrictive Covenants?

The statute also calls out specific types of restrictive covenants in employment agreements that remain permitted under Colorado law but are now subject to the purview of the statute, including:

- reasonable confidentiality provisions;[6]
- covenants not to compete renewed on or after August 10, 2022;
- agreements providing for the recovery of certain reasonable training costs for workers who leave employ within two years after the training occurs;
- covenants for the purchase and sale of a business or business assets; and
- provisions requiring the repayment of a scholarship if the individual fails to comply with the conditions of the scholarship.

What Do the New Notice Requirements Mean for Employers?

Colorado employers must timely provide workers and prospective workers with a separate notice containing specific information before the restrictive covenants can become enforceable.

The notice must be presented to current workers at least 14 days before the earlier of (1) the effective date of the restrictive covenant or (2) a change of the condition of employment providing consideration for the covenant(s). Prospective workers must receive the notice before accepting their offer of employment, so it is advisable to include the notice and proposed covenants with the offer letter.

In addition to timely distribution, the employer must also:

- provide the notice as a stand-alone document, along with a copy of the agreement containing the restrictive covenants;
- use "clear and conspicuous terms" in language commonly used to communicate with the worker about their performance;
- name the restrictive covenant in the notice and state that "the agreement contains a covenant not to compete that could restrict the worker's options for subsequent employment following their separation from the employer" and direct the worker to the specific provisions containing the covenants; and
- have the worker sign the notice.

An employer's failure to provide sufficient notice of the non-compete agreement will result in the restrictive covenant being deemed void and may subject the employer to statutory penalties.

One issue that has arisen is whether the notice provision applies to non-disclosure, confidentiality, and non-solicitation agreements. The notice subsection states that "[a]ny covenant not to compete that is otherwise permissible under subsection (2) or (3) of this section is void unless notice of the covenant not to compete" is provided under the statute's rubric.[7] While the aforementioned provisions are not strictly "non-compete agreements," that term is undefined in the statute and is at times used interchangeably with the term "restrictive covenants." Parties to any type of restrictive covenant should pay close attention to the notice requirement and assess whether it applies (and has been complied with) in their specific case.

Another issue is whether and to what extent the statutory revisions will effectively nullify preexisting restrictive covenants that are renewed after August 10, 2022, especially to the extent such covenants are not revised to comply with the current statutory requirements.

What Are the Liabilities for Employers Under the New Statute?

Liabilities for employers mostly come from the new civil enforcement framework. Under the new subsection 8(a) of the statute, an employer that enters into, presents to a worker or prospective worker as a term of employment, or attempts to enforce any void non-compete agreement is liable for actual damages and a statutory penalty to the aggrieved worker or prospective worker. Enforcement actions may now be brought by individuals, the Division, and the attorney general, who has new enforcement authority over the statute.

Available remedies for a violation of subsection 8(a) will now include:

- actual damages;
- declaratory judgment;
- injunctive relief;
- reasonable costs and attorney fees; and
- statutory penalty of $5,000 per worker or prospective worker harmed by the conduct.

The Act also attempts to eliminate confusion caused by language added to the statute during the 2021 Colorado legislative session. Previously, a violation of any portion of the restrictive covenants statute was a class 2 misdemeanor. Now, it is a class 2 misdemeanor for an employer or individual "to use force, threats or other means of intimidation" to prevent any person from engaging in lawful work.[8]

For workers "primarily" residing or working in Colorado at the time of their separation of employment, the statute now requires the choice of law and venue provision to be Colorado. That is, irrespective of the parties' drafted language, the terms of any restrictive covenant will be statutorily governed by Colorado law and litigation arising from the enforceability of the restrictive covenant must take place in Colorado.[9]

Finally, the statute contains a "safe harbor" for employers or prospective employers acting in good faith and who had reasonable grounds to believe they were not violating the statute.[10] However, the safe harbor only protects the employer or prospective employer against the imposition of the full statutory penalty and not from other enforcement or remedies. Proving an employer acted in good faith may require using attorney-client communications at trial or calling the employer's drafting attorney as a fact witness. Further, any reduction of the penalty is entirely at the court's discretion.

What Happens With Restrictive Covenants in Effect Before August 10, 2022?

The Act's prohibitions and requirements are not retroactive: "This Act applies to covenants not to compete entered into or renewed on or after the applicable effective date of this Act."[11] This means that restrictive covenants entered into before August 10, 2022, will be evaluated under the prior statutory and common law framework.

Even so, we have already observed some attorneys argue the provisions are retroactive. We anticipate this question of retroactivity to be raised with the Colorado judiciary before too long (if not already).

What Now?

Employers with Colorado employees, applicants, and independent contractors subject to restrictive covenant provisions now have an entirely new paradigm within which to draft and ensure protection of their trade secrets and confidential information. Below are some suggested best practices for employers to follow when revising restrictive covenants.

Sharp Drafting

Employers should use precise language that incorporates statutory requirements and adheres to statutory definitions, as described below.

Confidentiality and trade secrets. Include clear definitions of these terms in agreements, and expressly carve out the information that, statutorily, cannot be covered by confidentiality or trade secret provisions (that is, "information that arises from the worker's general training, knowledge, skill, or experience, whether gained on the job or otherwise; information that is readily ascertainable to the public; or information that a worker otherwise has a right to disclose as legally protected conduct.").[12] The restrictions should be tethered to the protection of the information and should be "no broader than is reasonably necessary to protect the employer's legitimate interest in protecting trade secrets."[13] Overly broad provisions risk the restrictive covenant being deemed unenforceable.

Notice. Employers should strictly follow the timing and letter of the notice requirements contained in subsection (4).

Acknowledgements. Employers should not add language in an attempt to bind an employee to a non-compete that is no longer lawful. Some employers try to include acknowledgements in their non-compete agreements that an employee is a highly compensated worker under Colorado law. Unless that is true, inserting such a provision does not render an unenforceable non-compete enforceable and could subject the employer to statutory penalties and damages.

Compensation and Trade Secret Access

Employers will have to carefully determine which workers have access to trade secrets and understand that only those earning above the required compensation thresholds—at the time they execute the covenants and at the time of enforcement—may be bound by a non-compete or non-solicitation of business/customer provision. Employers should carefully study the annualization of compensation requirements described in subsections (2)(b) and (2)(c).

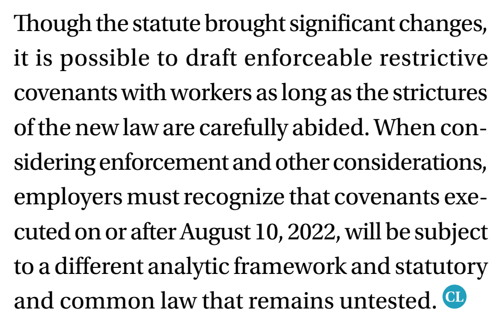
Multijurisdictional Compliance

Colorado's restrictive covenant requirements are now some of the strictest in the nation, so what is drafted and deployed for Colorado workers may be materially different from what is required in the employer's other jurisdictions. Employers of remote workers who live in Colorado anytime during the working relationship should be aware of Colorado's new requirements.

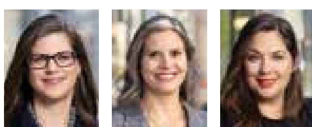
Good Faith

Consider how to best demonstrate the employer's good faith, pursuant to subsection (8)(c), while preserving attorney-client privilege or work product protection.

Conclusion



Though the statute brought significant changes, it is possible to draft enforceable restrictive covenants with workers as long as the strictures of the new law are carefully abided. When considering enforcement and other considerations, employers must recognize that covenants executed on or after August 10, 2022, will be subject to a different analytic framework and statutory and common law that remains untested. CL



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NOTES

1. HB 22-1317.
2. Pratt et al., "Non-Compete Agreements in Colorado—A New Era," 51 *Colo. Law.* 30 (Nov. 2022), https://cl.cobar.org/features/non-compete-agreements-in-colorado.
3. CRS § 8-2-113(2)(b).
4. Colo. Dep't of Lab. & Emp., Div. of Lab. Standards & Stat., Publication and Yearly Calculation of Adjusted Labor Compensation Order (2023), https://cdle.colorado.gov/sites/cdle/files/7%20CCR%201103-14%202023%20PAY%20CALC%20Order%20%282023%29.pdf.
5. CRS § 8-2-113(2)(b).
6. To be valid and allowable under the statute, confidentiality provisions may not "prohibit disclosure of information that arises from the worker's general training, knowledge, skill, or experience, whether gained on the job, or otherwise" nor prohibit a worker's disclosure of "information that is readily ascertainable to the public, or information that a worker otherwise has a right to disclose as legally protected conduct." *Id.*
7. CRS § 8-2-113(4)(a).
8. CRS § 8-2-113(1.5)(a).
9. CRS § 8-2-113(6).
10. CRS § 8-2-113(8)(c).
11. HB 22-1317.
12. CRS § 8-2-113(3)(b).
13. *Id.*