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Non-Compete Agreements with Arbitration Clauses Get Boost From US Supreme Court

By: Cullen Seltzer. *Tuesday, November 27th, 2012*

Employers and employees often enter into non-compete agreements that limit an employee's ability to compete with an employer during, or after, the employee's employment. These agreements are often the subject of intense litigation and their validity, and enforceability, varies from state to state. Many of these agreements also have arbitration provisions in them which require that any dispute under the agreement be decided by a private arbitrator instead of litigated in court. In *Nitro-Lift Technologies, LLC v. Howard*, decided by the Supreme Court of the United States on November 26, 2012, the Court made clear that an arbitration provision, enforceable by federal law, will be given effect even in cases where that means a dispute concerning a non-compete provision disfavored by state law will be kept out of the state courts.
http://www.supremecourt.gov/opinions/12pdf/11-1377_3e04.pdf

The Federal Arbitration Act "declares a national policy in favor of arbitration." When an Oklahoma trial court, and later the Oklahoma Supreme Court, ruled that a non-compete agreement could be reviewed by state courts, instead of by an arbitrator as contemplated by the parties' employment contract, Oklahoma ran afoul of settled law from the Supreme Court of the United States. In doing so, Oklahoma courts violated the the Supremacy Clause of the United States Constitution. In short, an arbitrator, not a state court judge, will decide whether a non-compete provision is lawful if the provision stems from an agreement with a valid arbitration clause.

In *Nitro-Lift,* the Oklahoma Courts that reviewed the employment agreement at issue determined that the arbitration provision in the contract was permissible. Rather than remand the employee's lawsuit to invalidate the non-compete provision for arbitration, or dismiss the lawsuit so that the dispute might be arbitrated privately, the Oklahoma state court went on to examine the non-compete provisions in question. The Oklahoma courts determined that the non-compete contained in the agreement violated Oklahoma state law. The Oklahoma courts went on to rule that the non-compete provisions were unenforceable.

In response, the employer, Nitro-Lift, argued that the Oklahoma state courts could not reach the question of the validity of the non-compete provisions in the first place. That was because the parties' agreement required disputes under the agreement be resolved by private arbitration, not by the state courts. Turning aside that argument, the Oklahoma Supreme Court relied on its own previous "exhaustive" review of Federal Arbitration Act cases and held that the FAA did not "inhibit [the Oklahoma courts'] review of the underlying contract's validity."

In an unsigned *per curiam* opinion, the US Supreme Court disagreed unequivocally. The Court held that Oklahoma was wrong to characterize the employment dispute as solely a matter of state law – the FAA, and the arbitration agreement, made the enforceability of the employment agreement subject to the federal law that enforces arbitration clauses. Moreover, the FAA is every bit as enforceable in state courts as it is in federal courts.

Oklahoma state courts must give effect to the Federal Arbitration Act, which gives effect to arbitration clauses. State courts must also give effect to US Supreme Court interpretations of the scope and effect of the Federal Arbitration Act. Both the FAA and US Supreme Court interpretations of it are the supreme law of the land.

In a final, biting ruling, the US Supreme Court rejected a particular statutory-construction argument advanced by the Oklahoma Supreme Court opinion. The Oklahoma Supreme Courts had reasoned that because Oklahoma had a specific state-law provision concerning non-compete agreements, that specific provision ought to trump the general provisions of the Federal Arbitration Act which apply to arbitration clauses generally. The Supreme Court agreed that specific statutes generally do trump general ones ("the ancient interpretive principle … *generalia specialibus non derogant"*), but that principle only applies only to conflicts of "*laws of equivalent dignity*" (emphasis added). Oklahoma's state law, disfavoring non-compete provisions, is an inferior law to Congress's supreme law of the land favoring the enforcement of arbitration clauses.

The *Nitro-Lift* case, in addition to having one of the best case names in recent memory, stakes out important contractual and Constitutional principles that bear considering when drafting agreements and seeking to enforce them. First, arbitration provisions are, as required by the FAA, "valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." Second, the FAA's protection of arbitration provisions will trump state law attempts to narrow the FAA's scope and effect. Third, state courts that find employment agreements, even non-compete agreements, offensive, or even unlawful, have no authority to tinker with them if the agreement has in it a valid arbitration clause. If you need any assistance with drafting non-compete agreements, the **Virginia employment law attorneys** at **Sands Anderson** would be pleased to provide assistance.