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Post-Employment Convenants Not to Compete--The Oklahoma View: Bayly, Martin & Fay Inc. v. Pickard

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POST-EMPLOYMENT COVENANTS NOT TO COMPETE — THE OKLAHOMA VIEW: *BAYLY, MARTIN & FAY INC. v. PICKARD*

I. INTRODUCTION

A post-employment restrictive covenant limits a party's ability to pursue his or her profession.[1] Historically, these covenants have been considered against the public's best interest because they reduce competition in the market place.[2] Once identified as against public policy, the covenants were regarded as illegal restraints on trade[3] and prohibited by both legislative and judicial action.[4] This rigid approach created an unjust hardship for parties with legitimate employment interests.[5] Upon recognizing the injustice, courts began to preserve those covenants found to be *reasonable* restraints on trade. This type of judicial preservation has evolved into what is now the majority view in the United States.[6] Today, most courts allow post-employment restrictive covenants to be judicially modified in an effort to preserve reasonable contractual restrictions.[7]

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1. The purpose of post-employment restrictive covenants:

> is not to prevent the competitive use of the unique personal qualities of the employees - either during or after the employment - but to prevent competitive use, for a time, of information or relationships which pertain peculiarly to the employer and which the employee acquired in the course of the employment.

Blake, *Employee Agreements Not to Compete*, 73 HARV. L. REV. 625, 647 (1960). *See also* D. ASPELUND & C. ERIKSEN, EMPLOYEE NONCOMPETITION LAW (3d ed. 1990) (comprehensive information on post-employment restrictive covenants).

2. Comment, *Post Employment Restraints: An Analysis of Theories of Enforcement, and a Suggested Supplement to the Covenant Not to Compete*, 17 TULSA L.J. 155, 155-56 (1981).

3. 14 S. WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 1633 (3d ed. 1972) states:

> Any bargain or contract which purports to limit in any way the right of either party to work or to do business, whether as to the character of the work or business, its place, the manner in which it shall be done, or the price which shall be demanded for it, may be called a bargain or contract in restraint of trade.

Id. at 78. *See also* Carpenter, *Validity of Contracts Not to Compete*, 76 U. PA. L. REV. 244 (1928).

4. Examples of a legislative and a judicial action invalidating post-employment restrictive covenants are OKLA. STAT. tit. 15, § 217 (Supp. 1990); H & R Block Inc. v. Lovelace, 208 Kan. 538, 493 P.2d 205 (1972), respectively.

5. Comment, *supra* note 2, at 155-56.

6. *See* 14 S. WILLISTON, *supra* note 3, § 1635; RESTATEMENT (SECOND) OF CONTRACTS § 188 comment c (1979); Comment, *supra* note 2, at 156.

7. *See* 14 S. WILLISTON, *supra* note 3, § 1633.

> The old rule as to limitations of time and space with respect to contracts involving restraint of trade has given way to the modern doctrine of reasonableness and the real test is never

Since 1970, the trend in Oklahoma, like the majority of jurisdictions, has been to preserve reasonable post-employment restrictions. This trend, however, is contrary to the language of title 15, section 217.[8] This statute, with two exceptions, defines all contracts restricting lawful professions as invalid. In *Bayly, Martin & Fay, Inc. v. Pickard*,[9] the Oklahoma Supreme Court *appears* to have disregarded the majority's trend of judicial modification and, although not specifically stating such, in effect reverted back to invalidating post-employment restrictive covenants.[10] The language in *Pickard* is confusing because it implies acceptance of the judicial modification approach but limits its use to a degree that renders it virtually meaningless. The court determined that judicial modification is prohibited if "essential terms" have to be added for the covenant to be reasonable.[11] The case is confusing because the court so broadly interpreted "essential terms",[12] that *any* alteration could be defined as an addition of an essential term. Therefore, any covenant could potentially be considered unmodifiable and invalid. Because of the ambiguous language in *Pickard* it is unclear how to draft lawful post-employment restrictive covenants in Oklahoma.

This article analyzes *Pickard* and its possible effects on Oklahoma law regarding post-employment restrictive covenants. A comparison of the *Pickard* decision with the more commonly used judicial modification approach illustrates that the latter approach is more equitable in determining the validity of post-employment restrictive covenants. Therefore, the judicial modification approach which uses a rule of reason should be statutorily adopted in Oklahoma. This can be accomplished by revising the present statute to prevent only "unreasonable" contractual restrictions against trade.

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whether there is any restraint but always whether the restraint is reasonable under the facts and circumstances of the particular case.

Id. at 80-81 (quoting Okerberg v. Crable, 185 Kan. 211, 214, 341 P.2d 966, 971 (1959)). *See also* Bayly, Martin & Fay, Inc. v. Pickard, 780 P.2d 1168, 1171 n.4 (Okla. 1989) (list of 27 jurisdictions that use the judicial modification approach; of these 27, only two jurisdictions have a statutory base—South Dakota and Hawaii); Comment, *supra* note 2, at 165-66 (listing jurisdictions that use the judicial modification approach).

8. OKLA STAT. tit. 15, §§ 217-19 (Supp. 1990).
9. 780 P.2d 1168 (Okla. 1989).
10. *Id.* at 1173, 1175.
11. *Id.* at 1175.
12. *Id.* at 1170, 1173.

II. STATEMENT OF THE CASE

A. *Facts*

The controversy in *Pickard* concerned the validity of a series of post-employment restrictive covenants between Bayly, Martin & Fay, Inc. ("BMF") and Daniel D. Pickard.[13] Pickard was president of the Oklahoma division of BMF's insurance subsidiary.[14] In order to advance within the company, Pickard entered into three contracts during his employment: a covenant not to compete, an employment agreement and a buy-sell agreement.[15] Each contract incrementally increased Pickard's post-employment restrictions, thus limiting his ability to continue his chosen trade should he leave BMF.[16] An important aspect of all three contracts was that each contained a provision stating that it was the parties' intent to abide by the restrictive covenants to the fullest extent permissible within the bounds of the law.[17] Furthermore, the contracts

13. *Id.* at 1169. Initially Pickard was employed by Harlan Agents and Brokers, Inc. an affiliate of Harlan Holding Company. Bayly, Martin & Fay, Inc. (BMF), an affiliate of Bayly, Martin & Fay Services, Inc., bought Harlan and became the assignee of Pickard's covenant not to compete. The other two restrictive covenants Pickard signed as BMF's employee. These covenants restricted Pickard from rendering any services in competition with BMF or NBS. (NBS is an affiliate of Harlan that was also purchased by BMF.) *Id.*

14. Brief for Appellant at 5-6, *Pickard*, (No. 70076); Telephone interview with Wm. Brad Heckenkemper Esq., BMF's attorney for the appeal (January 23, 1991).

15. *Pickard*, 780 P.2d at 1173-75. The first contract Pickard signed was a covenant not to compete. Pickard signed this contract as an incentive for a prospective buyer to buy his stock in Harlan Agents and Broker's Inc. ("Harlan"). After the prospective purchaser bought the stock, it was subsequently assigned to BMF. The covenant not to compete restricted Pickard from working in the insurance industry in any capacity for three years after the termination of his current employment. In addition, the covenant limited the geographical scope of the restrictions to Oklahoma, Texas, and Colorado. Under the covenant, Pickard was forbidden from servicing any client of his former employer. The term "client" was broadly defined to include any of BMF's customers during the last three years of Pickard's employment or those who would become a client during the immediate three years after Pickard's termination. *Id.* at 1173-74.

Two days after Pickard signed the covenant not to compete, he entered into an employment agreement with Harlan Agents and Broker's Inc., which was also subsequently assigned to BMF. This agreement included restrictive covenants expanding the scope of clients with whom Pickard was forbidden from conducting postemployment business. Thus, Pickard was not only restricted from servicing clients that the company serviced for three years before and after Pickard's employment was terminated, but also from any customer that had conducted business with the company during the time of his employment *and* any prospective customers contacted by the company before Pickard was terminated. *Id.* at 1174.

The third contract was a buy-sell agreement signed on November 15, 1984. In this agreement Pickard had the opportunity to buy eight-tenths of one percent (.8%) of BMF stock in exchange for agreeing to further post-employment restrictions. Under the terms of the buy-sell agreement, the postemployment restrictions on Pickard's activity were expanded beyond the insurance business to any type of business in which BMF or its subsidiaries were involved. In addition to the restrictive provisions in the previous contracts, this covenant prohibited the solicitation of any BMF clients or employees which would likely cause them to discontinue activity with the company. *Id.* at 1174.

16. *Id.* at 1174.

17. *Id.* at 1175. The buy-sell agreement between Pickard and BMF Services, Inc. states that

specifically invited judicial modification in order to prevent invalidation if it were found that the covenants did not comply with applicable state laws.[18] Notwithstanding that it was the explicit intent of the parties to allow for judicial modification of the covenants, the court still chose to invalidate the restrictive covenants.[19]

Combined, the three restrictive covenants covered a broad geographical, temporal and occupational scope. When Pickard left BMF he had collectively agreed to refrain from soliciting, selling or servicing any of BMF's previous, current or prospective clients for a period of three years following his termination.[20] The occupational restriction not only encompassed clients in the insurance industry, but also included clients in any of BMF's wide variety of subsidiaries.[21]

A few months after Pickard quit, BMF filed suit alleging that he had violated the restrictive covenants.[22] Although Pickard denied breaching the provision of the covenants which prohibited him from soliciting BMF's clients, he admitted selling and servicing insurance to BMF's clients after his termination.[23] Even though Pickard admitted to engaging in these activities, the extent of the breach was never determined because the trial court stayed discovery pending its decision on the legality of the restrictive covenants.[24] Despite the provision in the contracts inviting judicial modification, the trial court held that the covenants were overly

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"[i]t is the intention of each Employee Shareholder that the provisions of this paragraph shall be enforced to the fullest extent permissible . . . ." Buy-Sell Agreement, § 7(d) at 15 (November 15, 1984) (copy of the buy-sell agreement is on file at the *Tulsa Law Journal* Offices).

18. Brief of Appellant at 7-8, *Pickard* (No. 70076). The language in the buy-sell agreement inviting judicial modification states:

> Each Employee Shareholder and the Company recognize that the laws and public policies of the various states of the United States may differ as to the validity and enforceability of covenants and undertakings similar to those set forth in this paragraph. It is the intention of each Employee Shareholder that the provisions of this paragraph shall be enforced to the fullest extent permissible under the laws and public policies of each state and jurisdiction in which such enforcement is sought, and that the unenforceability (or the modification to conform to such laws or public policies) of any provision thereof shall not render unenforceable, or impair, the remainder of the provisions thereof. Accordingly, if any provision of this paragraph shall be determined to be invalid or unenforceable, either in whole or in part, under the laws or public policies of any state or jurisdiction in which enforcement is sought, as to such state or jurisdiction the provisions of this paragraph shall be deemed amended to delete or modify, as necessary, the offending provision and to alter the balance thereof in order to render it valid and enforceable in such state or jurisdiction.

Id. (emphasis omitted).

19. *Pickard*, 780 P.2d at 1175.

20. *Id.* at 1174.

21. *Id.* at 1173-4.

22. *Id.* at 1169.

23. Brief of Appellant at 8, *Pickard*, (No. 70076).

24. *Pickard*, 780 P.2d at 1170.

restrictive and granted Pickard's motion for summary judgment.[25] In so ruling, the trial court failed to examine external facts relevant to the case.

The Oklahoma Court of Appeals agreed that the covenants were overly restrictive, but rather than finding the covenants entirely invalid modified them in a manner it thought would leave the contracts lawful.[26] On certiorari, the Oklahoma Supreme Court did not explicitly disagree with the court of appeals' approach. Instead it determined that the broad occupational restrictions were still unreasonable.[27] Rather than modifying the remaining defective portions of the occupational restrictions the Oklahoma Supreme Court held that all three of the covenants were invalid.[28]

B. *Issue*

At issue in *Pickard* was "whether a court may modify an otherwise void covenant not to compete so that the covenant constitutes a reasonable restraint on trade"[29] under Oklahoma's restraint of trade statutes.[30]

C. *Holding*

Although the Oklahoma Supreme Court appeared to recognize the practicality of using the rule of reason to preserve some restrictive contract provisions, it refused to apply the rule in *Pickard*.[31] The court held that covenants not to compete cannot be judicially modified to comply with Oklahoma's restraint of trade statute if "essential elements" of the contract must be provided in order to bring the covenant within the scope of the rule of reason.[32]

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25. *Id.*

26. *Id.* at 1170, 1173. The court of appeals only modified the geographical scope of the covenant leaving the overly broad occupation restrictions in place. *Id.*

27. *Id.* at 1173.

28. *Id.* at 1175.

29. *Id.* at 1169.

30. OKLA. STAT. tit. 15, § 217 (Supp. 1990). The statute states that "[e]very contract by which any one is restrained from exercising a lawful profession, trade or business of any kind, otherwise than as provided by Sections 218 and 219 of this title, is to that extent void." *Id. See infra* note 36 for the text of the two exceptions, Sections 218 and 219 respectively.

31. *Pickard*, 780 P.2d at 1175.

32. *Id.* at 1170.

III. OKLAHOMA'S LAW OF POST-EMPLOYMENT RESTRICTIVE COVENANTS BEFORE *BAYLY, MARTIN & FAY, INC. V. PICKARD*

Oklahoma's restraint of trade statute,[33] enacted in 1910, reflects the anti-laissez faire approach to employer-employee relationships in the early part of this century.[34] The statute states that "[e]very contract by which any one is restrained from exercising a lawful profession, trade or business of any kind, otherwise than as provided by the next two sections is to that extent void."[35] The two statutory exceptions to this general rule involve the sale of good will and the dissolution of partnerships.[36] Although the goodwill exception was raised on appeal, neither exception was found to apply in *Pickard*.[37] Even though the language of Section 217 has not changed since 1910, interpretation of the statute by Oklahoma courts has fluctuated over the years with changes in society.

A. *The Traditional Approach*

The 1948 case of *E.S. Miller Laboratory Inc. v. Griffin*[38] represents the traditional approach to post-employment restrictive covenants. In *Griffin*, the Oklahoma Supreme Court interpreted the restraint of trade

33. OKLA. STAT. tit. 15, § 217 (Supp. 1990). The invalidity of *any* restraint on trade is evidence of the movement away from the laissez-faire doctrine.

34. BLACK'S LAW DICTIONARY 827 (6th ed.1991). Laissez-faire is a political and economic philosophy opposing governmental interference in economics beyond what is necessary to keep the peace. This practice is characterized by a deliberate abstention of governmental interference in order to allow the market place to operate freely. One emphasis of this theory is to allow individuals the freedom to contract.

35. OKLA. STAT. tit. 15, § 217 (Supp. 1990). The language in § 217 has remained unchanged since 1910.

36. OKLA. STAT. tit. 15, §§ 218 & 219 (Supp. 1990). Section 218 is entitled "Restraint of trade—Exception as to sale of goodwill" and states in part:

> One who sells the goodwill of a business may agree with the buyer to refrain from carrying on a similar business within a specified county . . . city or town or any part thereof, so long as the buyer, or any person deriving title to the goodwill from him carries on a like business therein.

Id. Section 219 is entitled "Restraint of trade—Exception as to partners" and states in part:

> Partners may, upon or in anticipation of a dissolution of the partnership, agree that none of them will carry on a similar business within a specified county . . . city or town or any part thereof.

Id.

37. *Pickard*, 780 P.2d at 1170. The statutory exceptions involving the sale of a business and the dissolution of a partnership did not apply. Section 218 was argued by BMF in the district court and in the court of appeals because of the .8% of stock Pickard had received when he signed a buy-sell agreement. Both courts rejected this argument and it was not presented on appeal to the Oklahoma Supreme Court. *Id.*

38. 200 Okla. 398, 194 P.2d 877 (1948).

statute literally and held that any contractual provision restraining a person from the pursuit of a lawful profession was invalid. Accordingly, former employers could not restrict competition from former employees.[39] The court justified its literal statutory interpretation by concluding that the language of the statute was clear — only those situations involving the sale of a business or the dissolution of a partnership were exempt from the statute's scope.[40] In contrast, the traditional common law rule recognized five exceptions to restrictive post-employment covenants, one of which allowed an employer to restrict a former employee from competing in a similar business.[41] Because this exception was available to the Oklahoma legislature, the *Griffin* court reasoned that the legislature had not intended to include it with the two statutory exceptions.[42] This traditional approach exemplifies the original restraint of trade doctrine, which has as its goal the preservation of competition.[43]

B. *The Rule of Reason Approach*

In 1970, the Oklahoma Supreme Court modified its previous position in *Griffin* and utilized a rule of reason analysis for evaluating post-employment restrictive covenants.[44] The rule of reason involves the modification of geographical, temporal, and occupational provisions in a contract so that it can be enforced to the extent necessary to protect an employer's legitimate needs without causing an undue hardship on the employee or the general public.[45] In *Tatum v. Colonial Life & Accident Insurance Co.*,[46] the court determined that there are instances where limited post-employment restrictive covenants may be enforced.[47] Here, the court used a rule of reason to hold that a covenant restricting Tatum from soliciting his former employer's clients for a period of two years

39. *Id.* at 399, 194 P.2d at 879.

40. *Id. See supra* note 36.

41. 14 S. WILLISTON, *supra* note 3, § 1637, at 104-05. *See also* Addyston Pipe & Steel Co. v. United States, 175 U.S. 211 (1899) (five common law exceptions to invalidation of post-employment restrictive covenants are discussed).

42. *Griffin*, 200 Okla. at 399, 194 P.2d at 878-79. The court recognized the common law exceptions to restraint of trade, but chose not to apply the exceptions that did not have a statutory base. *Id.*

43. 14 S. WILLISTON, *supra* note 3, § 1635, at 82-88.

44. Tatum v. Colonial Life & Accident Ins. Co., 465 P.2d 448 (Okla. 1970).

45. Central Adjustment Bureau, Inc. v. Ingram, 678 S.W.2d 28, 37 (Tenn. 1984).

46. 465 P.2d 448 (Okla. 1970).

47. *Id.* at 452.

was enforceable, meaning that only *unreasonable* restrictions are unlawful under Oklahoma's restraint of trade statute.[48] *Tatum* thus began Oklahoma's use of the rule of reason in post-employment restrictive covenants.

C. *Further Definition of the Rule of Reason*

The Oklahoma Supreme Court further explained the rule of reason in two cases following the *Tatum* decision. Although the primary issue in *Board of Regents v. NCAA*[49] and *Crown Paint Co. v. Bankston*[50] involved Oklahoma's antitrust statutes,[51] both cases also implicated the same restraint of trade statute at issue in *Pickard*.[52]

In *NCAA* and *Crown Paint*, the court stressed the need to examine the particular circumstances of each case in order to determine the reasonableness of a restrictive covenant.[53] The *NCAA* court further defined the parameters of the rule of reason by identifying the public interest as the primary element to be considered when evaluating the reasonableness of a restrictive covenant.[54] With public policy as the overriding concern,

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48. *Id.* at 451.

Tatum and *Pickard* are similar in that both cases involve the relationship between salesmen and insurance companies. The *Tatum* court identified the restrictive covenant as *reasonable* because it contained only minimal occupational, temporal, and geographic limitations which did not entirely limit Tatum from pursuing a lawful profession. The contract restricted only the solicitation of the insurance company's clients for a period of two years. The court stated that this type of restriction did not prevent Tatum from exercising a lawful profession, but rather was designed to maintain a "hands-off" policy with respect to those whom Tatum *knew* to be insured by his former employer.

49. 561 P.2d 499 (Okla. 1977).

50. 640 P.2d 948 (Okla. 1981), *cert. denied*, 455 U.S. 946 (1982).

51. OKLA. STAT. tit. 79, § 1 (1981) states that "[e]very act, agreement, contract, or combination in the form of trust, or otherwise, or conspiracy in restraint of trade or commerce within this state is hereby declared to be against public policy and illegal." *Id.* The *Crown Paint* court notes that:

> Because a liberal application of the provisions of [OKLA. STAT. tit. 79, § 1 (1971)] would outlaw every conceivable contract or combination which could be made concerning trade or commerce, courts have read into [such] statutes . . . a 'rule of reason', under which only those acts, contracts, agreements or combinations which prejudice public interests by unduly restricting competition, or unduly obstructing the due course of trade, or which injuriously restrain trade, are unlawful.

Crown Paint, 640 P.2d at 950 (citations omitted).

52. OKLA. STAT. tit. 15, § 217 (Supp. 1990). *NCAA*, 561 P.2d at 508; *Crown Paint*, 640 P.2d at 951-52.

53. *NCAA*, 561 P.2d at 508. (The court determines if a statute invalidates contracts in restraint of trade by examining the reasonableness of the contract in view of the particular circumstances. After an examination of the circumstances, if the court finds a contract unduly restrains trade, then it is void, but if a contract is a reasonable restraint of trade, it is valid). *See also Crown Paint*, 640 P.2d at 952 (including the same emphasis on circumstances).

54. *NCAA*, 561 P.2d at 508. Public policy determines if contracts that are a restraint of trade are valid and enforceable. If a contract is inimical to public interest, it is illegal. *Id. See also* Tatum v. Colonial Life & Accident Ins. Co., 465 P.2d 448, 452 (Okla. 1970).

the court analyzed both the needs and interests of the contracting parties in an effort to reach a just conclusion. After examining the circumstances of the case, the *NCAA* court determined that limiting the number of assistant coaches in Division I schools was a reasonable restriction and did not thwart public policy.[55]

In *Crown Paint*, the court addressed the validity of restrictive covenants on vertical competition in an industry.[56] The court held that restrictive covenants between a manufacturer and a retailer that designate a specific limited area as the exclusive territory of the retailer is reasonable.[57] This example of vertical competition — competition "between two parties operating on different market levels"[58] — has been found to be a reasonable restraint of trade. As in *NCAA*, the *Crown Paint* opinion placed emphasis on applying the rule of reason only after an examination of the specific circumstances of the case.[59]

IV. THE *PICKARD* DECISION

In *Pickard*, the Oklahoma Supreme Court set out a two-part test for determining the enforceability of post-employment restrictive covenants. First, the covenant must protect a legitimate interest of the employer while at the same time not unduly restrain trade.[60] Second, the court requires that reformation of an overly restrictive covenant which does not protect a legitimate interest and unduly restrains trade not involve the addition of essential terms or elements.[61] Even though the court failed to clarify what it meant by the "addition of essential terms", it nevertheless determined that the covenants at issue failed both prongs of the test.[62]

The covenants in *Pickard* failed the first prong because portions of

55. *NCAA*, 561 P.2d at 508.
56. *Crown Paint*, 640 P. 2d at 952.
57. *Id.*
58. *Id.* at 951.
59. *Id.* at 952.
60. *Pickard*, 780 P.2d at 1172-73. The court's reasoning was based on H & R Block, Inc. v. Lovelace, 208 Kan. 538, 493 P.2d 205 (1972). In *Lovelace*, the court decided that a post-employment restrictive contract was analogous to a liquidated damages clause because of its one-sided restrictions. In arriving at this conclusion, the court examined the specific circumstances involved in the income tax-preparation business, the amount of competition in the restricted area and the reasonableness of the party's obligations. *Id.* at 543, 493 P.2d at 211.
61. *Pickard*, 780 P.2d at 1170. *See* RESTATEMENT (SECOND) OF CONTRACTS § 185 comment b (1979). If the term is an essential part of the agreement, "the court will hold that the promise itself, and perhaps the entire agreement, is unenforceable on grounds of public policy under the rule stated in § 178." *Id.*
62. *Id.* at 1172-73.

the covenants imposed overly restrictive, and therefore unjustified limitations on the employee's ability to continue his profession.[63] A justifiable restriction is one which allows the employer to compete on equal footing with his or her former employee who is now in a similar business in the same geographical area.[64] If a former employee obtains clients because of connections with his or her former employer, then it is only fair that the former employer should have a reasonable opportunity to try to retain his or her original customers.[65] The *Pickard* court refers to a Kansas Supreme Court case as support for its decision. In *H & R Block, Inc. v. Lovelace*[66] the court concluded that the franchisor, author of the covenant, fully intended to unreasonably restrict the franchisee's geographical sales area. Because the restriction was unnecessary and unjustified for the protection of the franchisor's interest, the covenant was found to be unreasonable.[67]

The *Pickard* court determined that the second prong of the test was also not met, as it found that the covenants would have to be rewritten instead of modified to be made reasonable.[68] In *Lovelace*, as well as in *Pickard*, the court declined to rewrite the contract on the basis that its terms were *unjustifiably* broad and therefore restricted the employee more than was needed to protect the employer's legitimate interests.[69] The *Pickard* court, however, did note that "judicial modification is justified if the contractual defect can be cured by imposition of reasonable limitations concerning the activities embraced, time, or geographical limitations."[70] Despite its apparent approval of the judicial modification approach, the *Pickard* court refused to modify the covenants because material elements would have to be added.

All three unmodifiable "essential elements" referred to by the court in *Pickard* were occupational related defects. The provisions involved: 1) client servicing or solicitation; 2) restriction from competing in unrelated lines of business; and 3) restrictions on the sale of different types of insurance.[71] Although the geographical modification made by the court

63. *Id.* at 1173-74.

64. RESTATEMENT (SECOND) OF CONTRACTS § 188 comment d (1979). *See also infra* notes 99-101 for examples of courts decisions which have placed parties on equal footing so neither had an unfair advantage.

65. RESTATEMENT (SECOND) OF CONTRACTS § 188 comment d (1979).

66. 208 Kan. 538, 493 P.2d 205 (1972).

67. *Id.* at 547, 493 P.2d at 212-13.

68. Bayly, Martin & Fay, Inc. v. Pickard, 780 P.2d 1168, 1173 (Okla. 1989).

69. 208 Kan. at 547, 493 P.2d at 212-13.

70. *Pickard*, 780 P.2d at 1173.

71. *Id.*

of appeals was accepted by the Oklahoma Supreme Court, it was deemed insufficient to cure the occupational related defects.[72] Thus, the Oklahoma Supreme Court concluded that the court of appeals erred in its modification of the *Pickard* covenants.[73] This conclusion was not based on rejection of the judicial modification theory, but rather because modification was inappropriate due to the covenant's unjustifiably broad occupational restrictions.[74] Additionally, although each covenant expressly invited the court to reshape overly restrictive terms into an acceptable form, the court declined to accept the invitation.[75] The court held that in order to cure the occupational related defects the covenants would have to be rewritten rather than modified and thus were invalid.[76]

IV. ANALYSIS

A. *Background*

The judicial modification approach is the most widely accepted view with regard to post-employment restrictive covenants.[77] This approach allows a court to use a rule of reason to judicially modify post-employment restrictive covenants in order to balance the parties' and public's legitimate interests so as to arrive at a reasonable agreement between the parties.[78]

Although section 217 prohibits *any* restraints on a lawful profession,[79] the Oklahoma Supreme Court in *Pickard* interpreted the statute to mean that "[c]ovenants not to compete may not be modified judicially to bring the contract within the rule of reason if the court would be required to supply essential contractual terms."[80] In applying this limitation, the court gave a broad reading to what constitutes providing "essential elements" by holding that the overly restrictive occupational covenants could not be modified.[81] Because the court failed to clarify what is or is not an "essential element," *Pickard* offers little guidance to attorneys attempting to draft lawful post-employment covenants.

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72. *Id.*
73. *Id.* at 1175.
74. *Id.* at 1172, 1175.
75. *Id.* at 1175. *See supra* note 18 for language of the invitation.
76. *Id.* at 1175.
77. *Id.* at 1171 n.4 (listing the states and their applicable cases which have adopted the majority view of judicial modification for post-employment restrictive covenants).
78. RESTATEMENT (SECOND) OF CONTRACTS § 188, at 41 (1979).
79. *See supra* note 34 and accompanying text.
80. *Pickard*, 780 P.2d at 1172 (this decision does not affirmatively state that judicial modification would be allowed if essential terms did not have to be supplied).
81. *Id.* at 1175.

Although the court did not expressly abandon the rule of reason standard, the practical effect of *Pickard* seems to do just that. If this was the court's intent, it could have based its decision on a literal interpretation of the statute alone.[82] Instead, the court implied that a rule of reason could be applicable in some instances, but then failed to define those particular occasions.[83] Thus, the practical effect of *Pickard* is no different than if the court had applied section 217 in a literal sense. That is, the standard is now so uncertain that any restrictive covenant will likely be invalid; a result similiar to a literal interpretation of the statute.

B. *Application of the Rule of Reason*

Rather than applying the rule of reason, the *Pickard* court invalidated the post-employment restrictive covenants on the basis that they were incapable of saving because "essential terms" would have to be added.[84] Once the court determined the covenants were unjustifiably restrictive it disregarded the explicit provision in the contract identifying the parties' intent to allow judicial modification if necessary to bring the covenants within the bounds of the law.[85] The parties' invitation to modify the covenant along with a standard application of the rule of reason indicates a simple and perhaps more equitable method to resolve this case. Furthermore, overly broad occupational covenants such as the one at issue are exactly the type of restrictions the rule of reason was developed to address.[86] As discussed earlier, the rule of reason is a method of analysis to define the reasonableness of a contract by examining the geographical, temporal and occupational factors in the covenant.[87] Therefore, in light of the invitation to modify the contract provisions, the court would not be inappropriately providing essential terms, but rather would be equalizing the covenant's effect on the parties by modifying the existing terms so as to better accommodate the parties' interests and intentions.[88]

As previously noted, the three disputed restrictions addressed by the court were: 1) client servicing or solicitation; 2) restrictions from competing in unrelated lines of business; and 3) restrictions on the sale of

82. *See supra* text accompanying note 35.
83. *Pickard*, 780 P.2d at 1172-73.
84. *Id.* at 1175.
85. *See supra* note 18.
86. *Pickard*, 780 P.2d at 1172-73.
87. *See supra* note 45 and accompanying text.
88. *See supra* note 18.

different types of insurance.[89] These restrictions relate directly to the occupational component of the rule of reason. Therefore, to correct the three occupational related elements that were unacceptable to the *Pickard* majority, a court could modify the unsatisfactory portion and make it a type of "lesser included" provision.[90] This would not be a creation of essential terms, but merely modification of an existing occupational provision.

Once modified, a previously broad term should reflect reasonable limits, resulting in acceptable restrictions.[91] For instance, the first occupational related provision the *Pickard* court rejected involved a restriction which prohibited Pickard from servicing or soliciting BMF's *past, present,* and *future* clients. In some instances, a covenant preventing clients from choosing with whom they will conduct business is unreasonable, whereas a covenant restricting the solicitation of a former employer's current clients is considered reasonable.[92] This provision could be cured by judicially modifying the covenant to restrict Pickard only from soliciting BMF's current clients. Pickard would then be allowed to service BMF's clients that solicit him, but would be prohibited from soliciting BMF's current clients that were known to Pickard through his association with BMF. This limitation would allow BMF a reasonable chance to renew its association with the clients that it had once assigned to Pickard. To comply with the rule of reason, all occupational restrictions must be limited by reasonable time and geographic boundaries. Neither the three-year time period nor the county-wide geographical limitation was challenged by the Oklahoma Supreme Court in *Pickard*.[93]

The second and third provisions the court rejected involved restrictions from competing in unrelated lines of business and from selling dissimilar types of insurance. All that is required to modify the second and third provisions[94] is the revision of two words: "unrelated" to "related"

89. *Pickard*, 780 P.2d at 1173.

90. "Lesser included" refers to retaining a segment of an existing contractual term and eliminating the offensive portion in order to make the covenant less restrictive. This approach is similar to the "Blue Pencil Approach" used in many jurisdictions which are opposed to either re-writing or adding new elements to contracts in order to make them reasonable and therefore legal. *See generally* Comment, *supra* note 2, at 160.

91. Crown Paint Co. v. Bankston, 640 P.2d 948 (Okla. 1981), *cert. denied*, 455 U.S. 946 (1982); Tatum v. Colonial Life and Accident Ins. Co., 465 P.2d 448 (Okla. 1970).

92. *Tatum*, 465 P.2d at 451.

93. *Pickard*, 780 P.2d at 1173-75. Although the Oklahoma Supreme Court did not render a ruling as to the reasonableness of the geographical and temporal limitations, it implied that they were acceptable.

94. *Id.* at 1173.

and "dissimilar" to "similar." Therefore, a covenant is reasonable if it restricts the former employee only from related types of business or, more specifically, from selling the same product.

Although these suggested limitations are based on what has been considered reasonable restrictions in other jurisdictions,[95] an examination of the particular circumstances surrounding a restrictive covenant must be conducted in order to equitably modify restrictive covenants. The primary purpose of the judicial modification approach is to devise a fair resolution to overly restrictive covenants.[96] This can only be done if the facts of the case are evaluated to determine what is reasonable under the circumstances of the particular case.

C. *Discovery*

An examination of the facts of the case was necessary to enable the proper evaluation of the parties' and the public's legitimate interests.[97] The specific circumstances surrounding *Pickard* were never examined because the trial court's summary judgment decision precluded an evidentiary hearing.[98] Thus, granting summary judgment eliminated the possibility of a thorough investigation into the circumstances of the case. Such an investigation was necessary to properly apply the rule of reason and its equitable balances.[99] The court should have reversed the summary judgment and remanded the case so that a complete inquiry could have been made into the external circumstances surrounding the contract.

Oklahoma's restraint of trade cases prior to *Pickard* allowed discovery so that a thorough examination of the circumstances surrounding the case could be made in order to properly implement the rule of reason and its equitable balances.[100] For example, in both *Board of Regents v. NCAA*[101] and *Crown Paint Co. v. Bankston*,[102] the court undertook a complete examination of the respective industries involved to determine whether the restrictive covenants were reasonable. The fact that the

95. Whittenberg v. Williams, 135 P.2d 228 (Colo. 1943); Short v. Fahrney, 502 P.2d 982 (Colo. Ct. App. 1972); Colonial Life & Accident Ins. Co. v. Kappers, 488 P.2d 96 (Colo. Ct. App. 1971); System Concepts, Inc. v. Dixon, 669 P.2d 421 (Utah 1983); Tench v. Weaver, 374 P.2d 27 (Wyo. 1962).

96. 14 S. WILLISTON, *supra* note 3, §§ 1637-38, at 103.

97. 14 S. WILLISTON, *supra* note 3, § 1638, at 108.

98. *Pickard*, 780 P.2d at 1178 (Opala, V.C.J., dissenting).

99. *See supra* note 46 and accompanying text.

100. *See supra* notes 44-59 and accompanying text.

101. 561 P.2d 499 (Okla. 1977).

102. 640 P.2d 948 (Okla. 1981), *cert. denied*, 455 U.S. 946 (1982).

Pickard court cited both of these cases as examples of Oklahoma's use of the rule of reason lends validity to the requirement of discovery in order to properly evaluate the reasonableness of post-employment restrictive covenants. However, even though the *Pickard* court acknowledged use of discovery in previous cases, it nonetheless affirmed a summary judgment prior to the examination of external facts. This decision clearly circumvented the purpose of the rule of reason.

Even in *H & R Block Inc. v. Lovelace*,[103] a case cited favorably by *Pickard*,[104] a thorough examination of the surrounding circumstances was performed before determining that the restriction was unjustified.[105] In *Lovelace*, an investigation of the income tax-preparation industry was done by examining the amount of competition in the restricted geographical area.[106] The court concluded that the rule of reason should not be implemented because the circumstances revealed that the restrictive covenants were unnecessarily and unjustifiably broad.[107]

In contrast, the *Pickard* court looked only to the contract language. The court could not analyze any external circumstances because it did not allow discovery. If discovery had been allowed, relevant circumstances could have been considered to arrive at a more informed result. Judicial modification after discovery is the method used by the majority of jurisdictions.[108] Hence, attorneys in these jurisdictions are able to draft post-employment covenants without the type of confusion that stems from the *Pickard* case.

D. *A Renewed Emphasis on the Traditional Approach*

In *Scott v. Snelling & Snelling, Inc.*,[109] the Federal District Court for the Northern District of California placed renewed emphasis on a literal interpretation of the states restraint of trade statute, a statute similar to that of Oklahoma's.[110] The court rejected the judicial modification approach on public policy grounds.[111] The court followed the general rule

103. 208 Kan. 538, 493 P.2d 205 (1972). *See also* text accompanying notes 67-68.
104. 780 P.2d at 1172-73.
105. *Lovelace*, 208 Kan. at 544, 493 P.2d at 210-11.
106. *Id.* at 542, 493 P.2d at 209.
107. *Id.* at 547, 493 P.2d at 212-13.
108. *See* 14 S. WILLISTON, *supra* note 3, § 1633, at 80.
109. 732 F. Supp. 1034 (N.D. Cal. 1990).
110. CAL. BUS. & PROF. CODE § 16600 (West 1987 & Supp. 1990).
111. 732 F. Supp. at 1042.

of contruction that statutes should not be interpreted in a manner inconsistent with the ordinary meaning of their language unless a clearly expressed legislative intent exists.[112] *Scott* cites *Pickard* in support of its decision to invalidate a post-employment covenant on the basis that such a covenant is contrary to the state's public policy.[113] Although the *Pickard* court did not explicitly discuss public policy as a basis for its decision, the two cases are similar in their outcome.[114]

Pickard and *Scott* both acknowledged that the rule of reason may at times apply only to partial restrictions on competition; however, geographical and temporal categories are not necessarily recognized as partial restrictions.[115] Unlike *Pickard*, however, the *Scott* court further clarified the use of this statute by defining that the only appropriate deviations from the literal interpretation of the statute are the statutorily created exceptions.[116] In contrast, the language in *Pickard* implies that the rule of reason may be applied to any covenant so long as essential terms do not have to be provided.[117]

Even though *Scott* cites *Pickard* in support of its decision to invalidate post-employment covenants,[118] the *Pickard* court does not *explicitly* emphasize the same public policy argument against limiting competition as does the *Scott* case. The language in *Pickard* emphasizes the reluctance to provide essential terms of a contract rather than the public policy of pro-competition.[119] That the *Pickard* court so broadly interprets "providing essential terms," however, suggests that *any* post-employment covenant could be ruled invalid. This, in turn, gives the impression that the Oklahoma Supreme Court places more emphasis on the traditional public policy of promoting competition that a cursory reading of *Pickard* suggests. That is, the court has effectively returned to a pro-competition interpretation of section 217 without expressly doing so. Inasmuch as the Oklahoma Supreme Court did not address the issue of

112. American Tobacco Co. v. Patterson, 456 U.S. 63, 68 (1982).

113. *Scott*, 732 F. Supp. at 1042 n.11.

114. In *Pickard* and *Scott*, the trial courts found post-employment restrictive covenants to be against public policy. The Oklahoma Supreme Court affirmed the trial court's decision in *Pickard*. However, its decision was based on the inability of the court to add essential elements to the contract. Because of the court's broad interpretation of what constituted adding essential terms, the *effect* of the Oklahoma Supreme Court's decision is parallel with that of *Scott*. *Pickard*, 780 P.2d at 1170; *Scott*, 732 F. Supp. at 1045.

115. *Scott*, 732 F. Supp. at 1043. *Pickard*, 780 P.2d at 1175.

116. *Scott*, 732 F. Supp. at 1040-42.

117. *Pickard*, 780 P.2d at 1170.

118. *Scott*, 732 F. Supp. at 1042.

119. *Pickard*, 780 P.2d at 1170.

public policy, it is difficult to be certain as to the accuracy of this impression.

E. *Problems and Approaches*

As a result of *Pickard*, drafting lawful post-employment restrictive covenants is a difficult task. The plain language in section 217[120] may mislead unwary researchers to assume that the statute's clear and unambiguous language is valid. Whereas, the Oklahoma Supreme Court's latest interpretation of the statute allows judicial modification unless essential elements need to be supplied.[121] Even after uncovering Oklahoma's recent interpretation of the restraint of trade statute there is no reason to assume, based on past fluctuation,[122] that this will be the permanent interpretation. Thus, the Oklahoma legislature should address and correct this confusing issue.

Moreover, an attorney drafting post-employment restrictive covenants in Oklahoma can only speculate as to the covenants validity. Even an overly restrictive covenant that *appropriately* gives added consideration for the restriction would likely be unenforceable.[123] Depending on the circumstances, this could lead to an unconscionable and inequitable result for the contracting parties. Unconscionability is usually associated with an employee's unequal bargaining power.[124] According to Oklahoma's view, however, the employer has the disadvantage. The employee could foreseeably get an unjustifiable windfall by receiving compensation in return for agreeing to overly restrictive post-employment

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120. *See supra* text accompanying note 35.

121. *See supra* note 35 and accompanying text for language of the restraint of trade statute. *See also Pickard*, 780 P.2d at 1172.

122. *See supra* notes 38-59 and accompanying text for examples of Oklahoma's fluctuation in this area.

123. RESTATEMENT (SECOND) OF CONTRACTS § 188 comment b (1979) states that not all restrictive covenants should be invalid. *See also supra* note 98 for examples of when overly restrictive covenants should be allowed in order to protect legitimate interests.

124. Comment, *"Common Callings" and the Enforcement or Postemployment Covenants in Texas*, 19 ST. MARY'S L.J. 589, 597 (1987) (describing the theory of unconscionability).

> The modern notion of unconscionability is codified in section 2-302 of the Uniform Commercial Code, where the commentary suggest as a test 'whether, in light of the general commercial background and the commercial needs of the particular trade or case, the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract.' In *Williams v. Walker-Thomas Furniture Co.*, [350 F.2d 445 (D.C. Cir. 1965)], the [court] described unconscionability as 'an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party.'

Id.

covenants that would later be invalidated.[125] This treatment of restrictive covenants could promote "bad faith" agreements made by employees who *know* that the overly broad post-employment covenants will be invalidated rather than reasonably modified. Furthermore, employers may not be able to adequately protect themselves because if the covenants are too detailed the contract may be struck down simply as boilerplate. To combat this problem, full disclosure of the facts needs to be made. Regardless of whether the theory of unconscionability[126] is used to the favor of employees or employers, reaching an equitable result depends heavily upon a full factual development. Anything less can easily lead to an inequitable result. Additionally, the uncertainty in the law created by the *Pickard* version of the judicial modification approach might entice attorneys to become more creative when drafting employment covenants. Possible options include an approach exemplified in the Montana case of *Dobbins, Deguirer & Tucker, P.C. v. MacDonald & Olson*,[127] which involved interpretation of a restraint of trade statute identical to Oklahoma's.[128] The contract at issue allowed former employees to solicit their former employer's clients.[129] In *Dobbins*, an accounting firm specifically allowed its former employees to solicit the firm's clients in return for a "reasonable" fee for each client taken.[130] The fee consisted of one hundred percent of the gross fees billed by Dobbins during the last year of association with the client.[131] This amount could be paid out in monthly installments for three years at eight percent interest or in a lump sum payment.[132] The Montana Supreme Court, in an unanimous decision, held that the covenant was not against Montana's restraint of trade statute.[133] Historically, remedies at law have been found inadequate for breaches of post-employment agreements;[134] however, this approach might prove an acceptable alternative.

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125. *Id.*

126. *See supra* note 124.

127. 218 Mont. 392, 708 P.2d 577 (1985).

128. *See supra* text accompanying note 35 for Oklahoma's restraint of trade statute. *See* MONT. CODE ANN. § 28-2-703 (1987) for Montana's restraint of trade statute which has the same wording as Oklahoma's restraint of trade statute.

129. *Dobbins*, 218 Mont. at 393, 708 P.2d at 578.

130. *Id.*

131. *Id.*

132. *Id.* at 394, 708 P.2d at 578.

133. *Id.* at 397, 708 P.2d at 580.

134. *See generally* A. CORBIN, CORBIN ON CONTRACTS 91-117 (1964) (discussion of specific performance and adequacy of remedy); J. JACKSON, CONTRACT LAW IN MODERN SOCIETY at 183 (1973). *See also supra* note 95 (court decisions in accordance with equitable remedies for post-employment restrictive covenants); H & R Block v. Lovelace, 208 Kan. 538, 493 P.2d 205 (1972).

Another possible method to circumvent the *Pickard* decision would be to incorporate a "choice of law" provision in the contract. A choice of law provision, identifying an appropriate state, could allow the drafting attorney to be certain of the validity of the substance of his or her contract. The inherent problem with the choice of law option is that courts may not give force to provisions that violate the forum state's public policy.[135]

The best option, however, would be for the legislature to revise the 1910 language in the restraint of trade statute in order to reflect the modern equitable view on post-employment restrictive covenants. The statute could be modified to reflect the equitable view by adding the word "unreasonable"; specifically inviting reformation; and including a provision that would grant the parties a reasonable opportunity to present evidence that would aid the court in making a determination. An example of the revision is as follows:

1) Every contract by which any one is *unreasonably* restrained from exercising a lawful profession, trade or business of any kind, otherwise than as provided by the next two sections is to that extent void.
2) If the court as a matter of law finds the contract or any clause of the contract to have been unreasonable, the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unreasonable clause, or it may so limit the application of any reasonable clause as to avoid any unreasonable result.
3) When it is claimed or appears to the court that the contract or any clause thereof may be unreasonable, the parties shall be afforded a reasonable opportunity to present evidence as to the industry setting, purpose and effect to aid the court in making the determination.[136]

If such a revision was made the courts would be free to judicially modify restrictive covenants by using the rule of reason and could therefore avoid the interpretation problems and the resulting confusion that has arisen from *Pickard*.

Although this proposal invites judicial modification, the final decision whether to modify would be left to the courts in order to guard against intentional overreaching or unconscionability by either party.

135. Scott v. Snelling & Snelling, Inc., 732 F. Supp. 1034 (N.D. Cal. 1990).

136. This recommendation is based on the language in OKLA. STAT. tit. 12A, § 2-302 (1981 & Supp. 1990). Section 2-302 is Oklahoma's adoption of the Uniform Commercial Code's treatment of unconscionability; therefore, alterations have been made in order for the language to apply to post-employment covenants.

The courts are in a better position than the legislature to make the most equitable decision on a case by case basis. Therefore, a great deal of discretion will be allotted to the courts in order to make its determinations. Because of the discretion there will still be some confusion surrounding the outcome of cases involving these types of covenants. Even though there still can be some uncertainty as to the covenants' enforceability, drafters of such covenants will know of the courts' choices and will likely draft post-employment covenants accordingly.

V. CONCLUSION

The rule of reason has been used by most courts when confronted with determining the reasonableness of post-employment restrictive covenants. The judicial modification approach allows the court to evaluate the facts of a particular case in order to modify excessive occupational, temporal, and geographical restrictions. Even if a statute prohibits such covenants, allowing judicial modification would lead to a more equitable result. In *Pickard* the court chose not to use the rule of reason because, in its view, essential terms of the contract would have to be supplied in order to make the covenants reasonable. Because the "essential elements" in question fall within the parameters of the occupational category provided for in the rule of reason analysis, it is clear that the more equitable rule of reason is a more appropriate rule of decision as opposed to simply finding the entire covenant unreasonable and invalid.

A more equitable outcome could have been achieved through remand of the case to the trial court for discovery. Once all of the circumstances surrounding the contract and the insurance industry had been revealed, the court could have better determined whether the covenants were reasonable. If after examining the facts of the particular case, the court should find that the covenants are unreasonable or against public policy, a rule of reason analysis should ensue. Because the rule of reason analysis produces more equitable results, it should be the approach adopted in Oklahoma — either by the courts or preferably, by the legislature.

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