

A Case in Point — When and How to Use Non-Compete Agreements for Bank Executives and Key Managers

By Susan K. Eggum

Consumer and commercial banks have interests that may legitimately be protected by a non-compete agreement. Such banks are in the business of using a sales force, direct mail, telemarketing, branches, the Internet and other channels to acquire or manage commercial and consumer banking products (e.g., commercial and industrial loans, commercial real estate loans, middle market and small business loans, and commercial and consumer deposits).

With a properly scoped non-compete agreement, banking business interests can be protected from encroachment by departing executives and key managers.

An example of this fact is a recent Capital One Financial Corporation (“Capital One”) lawsuit against its former president and executive vice president for conduct in violation of their non-competition agreements. The suit named John Kanas and John Bohlsen, and was filed in the U.S. District Court for the Eastern District of Virginia.

Capital One’s non-compete agreements acknowledged that these sophisticated executives received confidential business information concerning legitimate business interests, including strategies for growing certain business lines and the protection of Capital One’s good will and other intangibles, such as reputation, position in the community and consumer relationships. The non-compete agreements further recited very significant monetary consideration received by the executives at the time of, and in partial consideration for, the covenants.

Those agreements also defined what banking activities would be permissible following separation from employment, such as hedge fund operations, and also defined, as follows, what specific “Competitive Business” of Capital One the non-compete was to protect:

“...the consumer and commercial banking business engaged in by the Company or any Affiliated Entity as of the Separation Date, including the business of acquiring and/or managing (whether by use of a sales force, agents, direct mail, the branch, telemarketing, the Internet or any other channel) all commercial and consumer banking products (including but not limited to, commercial and industrial loans, commercial real estate loans, middle market and small business loans, whether originated directly or indirectly through other lending institutions, and commercial and consumer deposits), in New York, New Jersey and Connecticut.”

Two years into the five-year non-competition period, the former executives formed their own bank in Florida, outside the prohibited geographic area of New York, New Jersey and Connecticut. The new bank acquired mortgage loan portfolios from the FDIC and on the secondary market. But, certain portions of each portfolio were secured by property or equipment located in New York, New Jersey and Connecticut. And, a portion of the new bank’s deposits were from customers with addresses within the three-state area.

Given the clear and specific definition of the business lines Capital One sought to protect, the limited geographic scope, the sophistication of the employees who signed the non-competition agreements and their ability to earn a livelihood in unrelated banking and investment lines, the federal court for the District of Virginia agreed that Capital One could fully enforce its non-competition agreements against the two former employees.

While many jurisdictions tend to disfavor non-competition agreements, where the agreement is narrowly and specifically constructed against a well-compensated employee who had access to, and knowledge of, protected business information, the non-compete is very likely to be enforced.



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