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## Delaware Court Grapples With Enforcement of Choice of Law Provisions in Restrictive Covenant Agreements

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When implementing restrictive covenant agreements in their workforces, companies often grapple with how best to handle the wide variation in the law from one state to the other. One solution is to include a choice of law provision that calls for all agreements to be construed under the laws of a single state. Still, there is no guarantee that courts will honor a choice of law provision, particularly where the purpose of the agreement conflicts with the public policy interests of a different state that shares an interest in the subject matter at issue.

Twice in recent months, the Delaware Chancery Court addressed the enforceability of Delaware choice of law provisions in restrictive covenant agreements involving out-of-state employees. In [\*Cabela's LLC v. Wellman et al.\*, Case No. 2018-0607-TMR \(Oct. 26, 2018\)](#), the plaintiff, a Delaware corporation with headquarters in Nebraska, sued four former director-level employees from its Nebraska headquarters. Meanwhile, the plaintiff in [\*NuVasive, Inc. v. Miles\*, Case No. 2017-0720-SG \(Sept. 28, 2018\)](#) was also a Delaware corporation but with business operations in California, and was suing to enforce a non-compete agreement against a similarly high-level employee in California. In both *Cabela's* and *NuVasive*, the defendant employees resided, worked, and ultimately sought to compete with their former employers in Nebraska and California, respectively. In other words, virtually all relevant activities at issue in the cases occurred outside of Delaware. Nevertheless, the plaintiff former employers asked the Court to enforce their agreements under Delaware law, based on their inclusion of Delaware choice of law provisions in the relevant agreements.

While Delaware courts generally honor contractual choice of law provisions, the Court noted an important public policy exception to that rule. As the court explained in *Cabela's*, “[w]here the parties enter a contract which, except for the choice of law provision, would be governed by the law of a [different] state, and that state has a public policy under which a contractual provision would be limited or void, the Restatement recognizes that allowing the parties to contract around that public policy would be an unwholesome exercise of freedom of contract.” (Internal citations omitted). To determine whether that exception should apply to the *Cabela's* and *NuVasive* agreements, the Court examined the following questions:

- Would another state’s laws apply in the absence of a choice of law provision?
- If so, would enforcing the non-compete covenant violate a fundamental public policy of that other state?
- If so, are the other state’s applicable public policy interests materially greater than the applicable public policy interests of Delaware?

In *Cabela's*, the Court found that Nebraska law would apply in the absence of the Delaware choice of law provision, given Nebraska’s stronger contacts with the agreements. Second, the Court concluded that the defendants’ agreements, which were broadly drafted to prohibit ordinary competition, violated Nebraska’s fundamental public policy, which strictly prohibits such agreements unless they are narrowly tailored to prevent misappropriation of customer goodwill, confidential information, or trade secrets. Third, the Court held that Nebraska’s specific public policy against restraints on trade was materially greater than Delaware’s general public policy interest in freedom of contract. As the Court explained, where the contract at issue “is abhorrent



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and void” under Nebraska public policy, “and where, as here, the formation and enforcement of the contract relate overwhelmingly to [Nebraska], a general interest in freedom of contract is unlikely to be the equal of that public policy[.]” On those grounds, the Court refused to honor the Delaware choice of law provision.

Applying the same criteria, the Delaware Chancery Court reached the opposite conclusion in the *NuVasive* decision. Just as the facts in *Cabelo’s* related overwhelmingly to Nebraska, the facts in *NuVasive* related just as strongly to California. Further, it is generally understood that California law prohibits restrictive covenant agreements broadly. Section 16600 of the California Business and Professional Code strictly prohibits *all* restraints on competition in the employment context. Further, Section 925 of the California Labor Code prohibits employers from implementing choice of law or choice of forum provisions that circumvent California’s statutory protections or restrict access to a California judicial forum. The Court noted that these provisions reflect strong public policies against the enforcement of non-compete agreements against California residents.

Nevertheless, the *NuVasive* Court ultimately approved the choice of Delaware law provision due to one important distinguishing factor – the former employee was represented by an attorney in the negotiation of the non-compete agreement. The Court noted that although California Labor Code Section 925 generally prohibits parties from contracting around California substantive laws and California judicial forums, it carves out an exception with respect to employees who are represented by their own legal counsel during the contract negotiations. That carve-out exception, the Court concluded, demonstrated the California Legislature’s recognition “that in the limited subset of cases where the inequality of bargaining strength of the parties to an employment contract is buffered by the employee being represented by independent counsel, and where counsel participated in negotiation of the terms of a choice of law provision, California’s interest in freedom of contract outweighs interest in freedom of employment.” On that basis, the Court held that enforcement of the Delaware choice of law provision would not violate a public policy interest held by California.

The above decisions make clear that Delaware’s public policies may be outweighed by the public policies of a state with a materially greater interest in the litigation. If enforcement of the contract in the manner requested would be abhorrent to the public policies of the latter state, then Delaware courts will not enforce a choice of law provision requiring application of Delaware law. In *Cabelo’s* and *NuVasive*, the Court found that Delaware had a lesser interest in the subject matter than Nebraska and California, respectively. However, while the Court also concluded that Nebraska’s interest in the *Cabelo’s* litigation overrode the parties’ contractually-designated choice of law provision, the same could not be said for California’s interest in the *NuVasive* litigation, given that the *NuVasive* defendant negotiated the choice of law provision with the assistance of legal counsel.

Ultimately, the validity of a choice of law provision in a restrictive covenant agreement depends on a number of factors, including the facts at issue as well as the public policies of states that may have a material interest in the subject matter. This analysis should be performed with the assistance of counsel. And, in certain instances, it may be wise for the company to recommend that its prospective employees retain counsel when negotiating their agreements.

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