CONTRACTS—RESTRAINT OF TRADE OR COMPETITION IN TRADE—FORUM-SELECTION CLAUSES & NON-COMPETE AGREEMENTS: CHOICE-OF-LAW AND FORUM-SELECTION CLAUSES PROVE UNSUCCESSFUL AGAINST NORTH DAKOTA'S LONGSTANDING BAN ON NON-COMPETE AGREEMENTS

Osborne v. Brown & Saenger, Inc., 2017 ND 288, 904 N.W.2d 34 (2017)

ABSTRACT

North Dakota's prohibition on trade restriction has been described by the North Dakota Supreme Court as "one of the oldest and most continuous applications of public policy in contract law." In a unanimous decision, the court upheld North Dakota's longstanding public policy against non-compete agreements by refusing to enforce an employment contract's choice-of-law and form-selection provisions. In *Osborne v. Brown & Saenger, Inc.*, the court held: (1) as a matter of first impression, dismissal for improper venue on the basis of a forum-selection clause is reviewed *de novo*; (2) employment contract's choice-of-law and forum-selection clause was unenforceable to the extent the provision would allow employers to circumvent North Dakota's strong prohibition on non-compete agreements; and (3) the non-competition clause in the employment contract was unenforceable. This case is not only significant to North Dakota legal practitioners, but to anyone contracting with someone who lives and works in North Dakota. This decision affirms the state's enduring ban of non-compete agreements while shutting the door on contracting around the issue through forum-selection provisions.

I. FACTS

In 2011, Brown & Saenger Inc. ("Brown") hired Dawn Osborne ("Osborne") to serve as a sales representative for the company.[1] Brown is a South Dakota company that operates as a licensed foreign corporation in the state

1. Osborne v. Brown & Saenger, Inc., 2017 ND 288, ¶ 2, 904 N.W.2d 34.

of North Dakota, with an office located in Fargo.[2] Osborne, at all relevant times, was a North Dakota resident working out of Brown's Fargo office.[3]

As a sales representative of Brown, Osborne was tasked with selling office supplies to various businesses.[4] This was an area Osborne had experience in as she had been in the industry of selling office supplies since 2002.[5]

When Osborne was hired by Brown she was presented with an employment contract containing several restrictive covenants.[6] As the sole provider for her family, Osborne felt pressured to have a stable source of income; and so, she signed the employment contract.[7]

At the end of each year, Osborne was required to sign a new employment contract with Brown.[8] Each year, the new employment contract became more restrictive in nature.[9] In December of 2015, Osborne was presented a new employment agreement ("2015 Employment Agreement") to sign for the following year.[10] The 2015 Employee Agreement contained a non-competition clause stating that for two years after her last day of employment with Brown, Osborn could not "directly or indirectly" compete with Brown or solicit Brown's customers within 100 mile radius of Fargo.[11] Additionally, the 2015 Employment Agreement contained a choice-of-law and forum-selection clause which read, "[t]he parties agree that this agreement is governed by the laws of the State of South Dakota and that the state circuit court situated in Minnehaha County, South Dakota, shall be the exclusive jurisdiction of any disputes related to this Agreement."[12]

In 2017, Brown terminated Osborne.[13] Prior to her termination, Osborne raised issues concerning her compensation, deductions, payment to customers, and the non-competition clause. After she was fired, Osborne sued Brown, "alleging retaliation, improper deductions, and breach of contract."[14] Moreover, Osborne moved for a preliminary injunction to prevent Brown from enforcing the non-competition clause and sought a declaratory judgment asserting the non-competition clause as void.[15] Brown moved to

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2. *Id*.
3. Appellant's Brief at ¶ 10, *Osborne*, 2017 ND 288, 904 N.W.2d 34 (No. 20170254).
4. *Osborne*, 2017 ND 288, ¶ 2, 904 N.W.2d 34.
5. Appellant's Brief at ¶ 10, *Osborne*, 2017 ND 288, 904 N.W.2d 34 (No. 20170254).
6. *Id*. at ¶ 11.
7. *Id*. at ¶¶ 10-11.
8. *Id*. at ¶ 14.
9. *Id*.
10. *Id*. at ¶ 18.
11. *Id*. at ¶ 19.
12. Appellee's Brief at ¶ 10, *Osborne*, 2017 ND 288, 904 N.W.2d 34 (No. 20170254).
13. *Id*. at ¶ 11.
14. *Osborne*, 2017 ND 288, ¶ 4, 904 N.W.2d 34.
15. *Id*.

dismiss the action, arguing the choice-of-law and forum-selection clause in the employment agreement was valid; making the North Dakota court an improper venue.[16] Brown contended the forum-selection clause required the case to be heard by a South Dakota court, as specified in the agreement.[17] Subsequently, Brown sued Osborne in Minnehaha County, South Dakota, seeking a preliminary injunction to enforce the non-competition clause against Osborne.[18] Minnehaha County had previously upheld and enforced Brown's non-competition clause against North Dakota citizens.[19]

The North Dakota district court, without ruling on the motion for preliminary injunction, agreed with Brown and granted the motion to dismiss.[20] Osborne appealed the district court's order.[21]

II. LEGAL BACKGROUND

To fully appreciate the Court's decision and the impact of this case, it is necessary to look back at the history of non-compete agreements. Section II will begin by addressing the broad history of non-compete agreements. That analysis will be followed by a discussion focusing solely on North Dakota's case law and legislative history concerning non-competition issues.

A. BROAD HISTORY OF NON-COMPETE AGREEMENTS

"One of the oldest and one of the most continuous applications of public policy in the sphere of contract law is its application to contracts in restraint of trade."[22] Historically, common law has been supportive of free competition.[23] From the Middle Ages up until the Seventeenth Century, all contracts restraining trade were considered unlawful in Western society.[24]

Laws concerning contractual restraints on trade have continuously evolve and be molded by changing societal ideals and moral values.[25] As public sentiment on trade restriction began to shift, so too did it become appropriate to impose reasonable restraints, such as limiting the duration and geographic reach of non-compete agreements.[26]

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16. *Id*.
17. *Id*.
18. *Osborne*, 2017 ND 288, ¶ 5, 904 N.W.2d 34.
19. Appellant's Reply Brief at ¶ 14, *Osborne*, 2017 ND 288, 904 N.W.2d 34 (No. 20170254).
20. *Osborne*, 2017 ND 288, ¶ 4, 904 N.W.2d 34.
21. *Id*.
22. Werlinger v. Mutual Service Casualty Ins. Co., 496 N.W.2d 26, 29 (N.D. 1993).
23. *Id*.
24. *Id*.
25. *Id*.
26. *Id*.

B. NORTH DAKOTA'S HISTORY ADDRESSING NON-COMPETE AGREEMENTS

What is now codified as the opening clause of North Dakota Century Code section 09-08-06,[27] was drawn from the Field Code and originally enacted as a part of the Dakota Territory Civil Code of 1865.[28] Section 09-08-06 provides: "[a] contract by which anyone is restrained from exercising a lawful profession, trade, or business of any kind is to the extent void."[29]

1. Case law

During the course of the last century, the North Dakota Supreme Court has examined the validity of non-compete agreements on numerous occasions. Overall, the court has consistently broadened the interpretation and reach of section 09-08-06. Therefore, the ability to enforce non-compete agreements in North Dakota has decreased while the right to employment in the state has increased.

a. Olson v. Swendiman

First, contracts providing that an employee may "purchase his freedom" in order to compete have been found void by the North Dakota Supreme Court.[30] In *Olson v. Swendiman*, a dentist employed a fellow practitioner, to serve in his office for a five-year term.[31] Under the contract, if the employed dentist left before his term expired, he could not practice dentistry in Grand Forks, North Dakota, or East Grand Forks, Minnesota, for a period of two years.[32] The contract also provided for liquidated damages in the amount of $2,000 if the dentist violated the agreement and practiced during the two year period.[33] The court found this liquidated damages provision to be an unreasonable restraint on trade.[34]

b. Werlinger v. Mutual Services Casualty Insurance Co.

Likewise, the court in *Werlinger v. Mutual Services Casualty Insurance Co.*[35] found section 09-08-06 invalidated the non-competition clause of an

27. N.D. CENT. CODE § 09-08-06 (2019).
28. *Werlinger*, 496 N.W.2d at 30.
29. N.D. CENT. CODE § 09-08-06 (2019).
30. Olson v. Swediman, 244 N.W. 870, 870-71 (1932).
31. *Id.* at 870.
32. *Id.*
33. *Id.*
34. *Id.* at 871.
35. 496 N.W.2d 26 (N.D. 1993).

insurance agent's employment contract.[36] The contract provided that post employment, an employee would be entitled to a certain sum of termination compensation.[37] However, when the agent, after being fired, violated the non-competition clause, the employer withheld the agent's termination compensation.[38] The court found the non-competition clause at issue to be an unlawful restraint on trade as it essentially required the agent to purchase his freedom to compete by forfeiting money that he was contractually entitled to receive.[39]

c. Spectrum Emergency Care, Inc. v. St. Joseph's Hospital and Health Center

Next, section 09-08-06 has been found to apply equally to employers and employees.[40] The court in *Spectrum Emergency Care, Inc. v. St. Joseph's Hospital and Health Center*, noted that the purpose of section 09-08-06 would be frustrated if the court were to allow the statute to apply differently to employers and employees.[41] Therefore, the court announced section 09-08-06 applies to both employers and employees.[42]

d. Warner and Co. v. Solberg

Lastly, section 09-08-06 has been interpreted to invalidate non-solicitation provisions in employment contracts.[43] In *Warner and Co. v. Solberg*, the court voided a non-solicitation clause prohibiting an employee from accepting or writing any policy of insurance in replacement of a policy issued by the employer.[44] The non-solicitation clause also banned the employee from otherwise being involved in or assisting with any replacement policies.[45] The court recognized the clause inappropriately prohibited the employer from working with a client who freely came to her and, therefore, was a restraint of trade.[46]

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36. *Werlinger*, 496 N.W.2d at 30.
37. *Id.* at 27.
38. *Id.*
39. *Id.* at 30.
40. Spectrum Emergency Care, Inc. v. St. Joseph's Hosp. and Health Ctr., 479 N.W.2d 848, 852 (N.D. 1992).
41. *Id.*
42. *Id.*
43. Warner and Co. v. Soldberg, 2001 ND 156, ¶ 24, 634 N.W.2d 65.
44. *Id.*
45. *Id.*
46. *Id.*

2. *North Dakota Legislative History Addressing Non-compete Agreements*

On several occasions, the North Dakota Legislature has been asked to pass laws recognizing the validity of non-solicitation provisions.[47] For example, at the Fifty-Seventh Legislative Assembly, S.B. 2355 was introduced as a proposed amendment to section 09-08-06.[48] Senate Bill 2355 would have "permit[ted] an employee to agree with an employer not to '[s]olicit any existing customer of the employer existing at the date of termination within a specified county or counties or such other specified area for a period of up to two years from the date of termination of the agreement if the employer continues to carry on a like business in the area.'"[49] However, Senate Bill 2355 failed to become law.[50]

This was not the first time the North Dakota Legislature had contemplated a bill with this type of language.[51] In 1998, S.B. 2402, a bill similar to S.B. 2355, was introduced at the Fifty-Sixth Legislative Assembly.[52] Likewise, in 1995, another similar bill, H.B. 1389, was presented at the Fifty—Fourth Legislative Assembly.[53] Ultimately, neither of these bills became enacted law.[54] While legislative intent is primarily determined by action, "[w]hen the courts have construed a statute, the legislature's long acquiescence in the interpretation, continued use of the same language, or failure to amend the interpreted language is evidence the court's interpretation is in accordance with the legislative intent."[55]

III. ANALYSIS

In *Osborne*, the North Dakota Supreme Court was asked to expand the state's prohibition against non-compete agreements by rejecting the enforcement of forum-selection clauses that would allow employers to circumvent North Dakota law–specifically North Dakota Century Code section 09-08-06.[56] The court, in a unanimous decision, held as a matter of first impression, dismissal for improper venue on the basis of a forum-selection clause is to be

47. *Id*. at ¶ 20.
48. *Id*.
49. *Id*. (quoting S.B. 2355, 57th Legis, Assemb., Reg. Sess. (N.D. 2001)).
50. *Id*.
51. *See id*.
52. *Id*.
53. *Id*.
54. *Id*.
55. Clarys v. Ford Motor Co., 1999 N.D. 72, ¶ 16, 592 N.W. 2d 573.
56. Osborne v. Brown & Saenger, Inc., 2017 ND 288, ¶ 10, 904 N.W.2d 34.

reviewed *de novo*.[57] Further, the court found the employment contract's choice-of-law and forum-selection clause was unenforceable to the extent it would allow employers to circumvent North Dakota's public policy prohibiting non-compete agreements.[58] Finally, the court determined the non-competition clause within the employment contract was unenforceable.[59]

A. STANDARD OF REVIEW REGARDING DISMISSAL FOR IMPROPER VENUE

The first issue addressed by the court concerned the appropriate standard of review of a district court's granting of a North Dakota Rules of Civil Procedure Rule 12(b)(3) motion on the basis of a forum-selection clause.[60] Because Rule 12(b)(3) of the North Dakota Rules of Civil Procedure is derived from the Federal Rules of Civil Procedure, the court viewed federal interpretations of Federal Rule 12(b)(3) as highly persuasive authority.[61] The court adopted a *de novo* standard of review, noting the Second, Fourth, Seventh and Eleventh Circuits have determined *de novo* as the proper standard for a Rule 12(b)(3) motion to dismiss on the basis of a forum-selection clause.[62]

B. RULING ON THE FORUM-SELECTION & NON-COMPETITION CLAUSES

Next, the court examined the enforceability of Osborne's 2015 Employment Agreement.[63] In particular, when making its decision, the court examined the non-competition and forum-selection clauses within the 2015 Employment Agreement.[64] The non-competition clause stated, in relevant part, Osborne could not "directly or indirectly" compete with Brown or solicit Brown's customers within a 100 mile radius of Fargo, for two years after her last day of employment.[65] The forum-selection clause in the 2015 Employment Agreement read, "[t]he parties agree that this agreement is governed by the laws of the State of South Dakota and that the state circuit court situated

57. *Id*. at ¶ 7.
58. *Id*. at ¶ 16.
59. *Id*.
60. *Id*. at ¶ 6.
61. *Id*.
62. *Id*. at ¶ 7 (citing Global Seafood Inc. v. Bantry Bay Mussels Ltd., 659 F.3d 221, 224 (2d Cir. 2011); Pee Dee Health Care, P.A. v. Sanford, 509 F.3d 204, 209 (4th Cir. 2007); Continental Ins. Co. v. M/V Orsula, 354 F.3d 603, 606-07 (7th Cir. 2003); Rucker v. Oasis Legal Finances, L.L.C., 632 F.3d 1231, 1235 (11th Cir. 2011)).
63. *Id*. at ¶ 8.
64. *Id*. at ¶ 3.
65. Appellant's Brief at ¶ 19, *Osborne*, 2017 ND 288, 904 N.W.2d 34 (No. 20170254).

in Minnehaha County, South Dakota, shall be the exclusive jurisdiction of any disputes related to this Agreement."[66]

Osborne argued the district court erred in granting Brown's motion to dismiss for improper venue.[67] Specifically, she reasoned the forum-selection clause within the employment agreement was unenforceable under North Dakota Century Code section 28-04.1-03 to the extent it would allow Brown to circumvent section 09-08-06.[68] Section 28-04.1-03 provides:

> If the parties have agreed in writing that an action on a controversy may be brought only in another state and it is brought in a court of this state, the court will dismiss or stay the action, as appropriate, unless . . . 5. It would for some other reason be unfair or unreasonable to enforce the agreement.[69]

A forum-selection clause "may be set aside if enforcement would contravene a strong public policy of the forum in which suit is brought."[70] Furthermore, as previously stated, North Dakota's public policy on restraining trade is fixed by section 09-08-06 which states, "[a] contract by which anyone is restrained from exercising a lawful profession, trade, or business of any kind is to the extent void."[71] Section 09-08-06 provides for two narrow exceptions to the rule which are not applicable here.[72]

Osborne articulated to the court that if the forum-selection clause was enforced and a South Dakota court was able to hear the case, the South Dakota court would most certainly apply its own law and uphold the non-competition clause.[73] To support this argument, Osborne cited two cases from other jurisdictions in her brief, which the court ultimately incorporated into its opinion.[74]

The Court of Appeals of Georgia in *Lapolla Industries, Inc. v. Hess*[75] addressed an employment contract with forum-selection and non-competition clauses similar to those in Osbornes employment agreement.[76] The forum-selection and choice-of-law provisions in *Lapolla* called for the application of Texas law in a Texas court.[77] Under Georgia law, non-competition

66. Appellee's Brief at ¶ 10, *Osborne*, 2017 ND 288, 904 N.W.2d 34 (No. 20170254).
67. *Id*. at ¶ 8.
68. *Osborne*, 2017 ND 288, ¶ 10, 904 N.W.2d 34; N.D. CENT. CODE § 28-04.1-03 (2019).
69. N.D. CENT. CODE § 28-04.1-03 (2019).
70. *Id*. at ¶ 9.
71. N.D. CENT. CODE § 09-08-06 (2019).
72. *Id*.
73. *Id*. at ¶ 11.
74. Appellant's Brief at ¶ 10, *Osborne*, 2017 ND 288, 904 N.W.2d 34 (No. 20170254).
75. Lapolla Industries, Inc. v. Hess, 750 S.E.2d 467, 476 (2013).
76. *Osborne*, 2017 ND 288, ¶ 11, 904 N.W.2d 34.
77. *Id*.

clauses are unenforceable and go against public policy.[78] Because the court found it was likely that a Texas court applying Texas law would enforce the non-competition clause, the Georgia court protected its public policy against non-compete agreements by refusing to enforce the forum-selection and choice-of-law clauses.[79]

The Court of Appeals of Wisconsin came to a similar conclusion in *Beilfuss v. Huffy Corp.*.[80] In *Beilfuss*, the employment agreement contained restrictive covenants governing the treatment of confidential information and non-competition.[81] On appeal, the Court of Appeals of Wisconsin reversed the trial court, concluding the choice-of-law and forum-selection clauses violated Wisconsin's public policy against non-compete agreements.[82] In particular, the court concluded that a Wisconsin court would be best equip to deal with and interpret Wisconsin's law and public policy on non-compete agreements.[83]

The North Dakota Supreme Court agreed with Osborne that if the forum-selection clause was held to be enforceable, section 09-08-06 may be circumvented.[84] The court laid out three reasons to support this conclusion.[85] First, Osborne's employment contract had a choice-of-law provision requiring South Dakota law to be used.[86] Next, South Dakota law permits limited non-compete agreements.[87] Lastly, in 2012, the state circuit court in Minnehaha County, South Dakota, actually granted Brown a preliminarily injunction against one of its former North Dakota employees, preventing that employee from competing with Brown in North Dakota.[88]

The forum-selection clause, if enforced, would be unfair and unreasonable as it would limit a North Dakota citizen of her right to work and compete within the state.[89] Therefore, the forum-selection clause was found to be unenforceable.[90]

> Simply put, one may not contract for application of another state's law or forum if the natural result is to allow enforcement of a non-

78. *Id.*
79. *Id.*
80. 685 N.W.2d 373 (Wis. 2004).
81. *Osborne*, 2017 ND 288, ¶ 15, 904 N.W.2d 34.
82. *Id.*
83. *Id.*
84. *Id.* at ¶ 12.
85. *Id.*
86. *Id.*
87. *Id.*
88. *Id.*
89. *Id.* at ¶ 16.
90. *Id.*

> compete agreement in violation of North Dakota's longstanding and strong public policy against non-compete agreements. Because North Dakota has an interest in protecting this public policy from evasion and North Dakota courts are more familiar with North Dakota law and public policy on non-compete agreements, we hold the Choice of Law/Forum clause is unenforceable in the context of Osborne's declaratory judgment claim.[91]

Ultimately, the court held the non-competition clause was unenforceable under section 09-08-06 to the extent it limited Osborne, "from exercising a lawful profession, trade or business in North Dakota."[92] In holding the two clauses as unenforceable, the court reversed the district court's order granting Brown's motion to dismiss and remanded the case for further proceedings.[93]

IV. IMPACT

The court's decision in *Osborne* affirms North Dakota's longstanding public policy against non-compete agreements and shuts down the possibility of contracting around the issue through choice-of-law and forum-selection clauses. *Osborne* has, and will continue to have, a substantial impact on employment law in North Dakota. This decision also raises concerns as to future applicability of forum-selection provisions in other contractual settings.[94]

A. EMPLOYMENT IN NORTH DAKOTA

First, this ruling makes it difficult for an employer to subject a North Dakota resident and employee to the laws of another jurisdiction. The decision impacts both future employment relationships as well as many existing relationships between employees and employers. Each day countless companies are hiring new employees. If the new hire lives and works in North Dakota, this ruling impacts what their employment contract with the company will look like.

Similarly, many employees across the state are currently in non-compete agreements that purport to apply out-of-state laws. By invalidating such provisions, the *Osborne* decision may leave some employers without any means to prevent former employees from competing.

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91. *Id*.
92. *Id*.
93. *Id*. at ¶ 17.
94. Berg v. North Dakota State Bd. of Registration of Prof'l Eng'rs and Land Surveyors, 2018 ND 274, 920 N.W.2d 896 (N.D. 2018)

B. FUTURE OF FORUM-SELECTION PROVISIONS

Next, the *Osborne* decision raises concerns as to applicability of forum-selection clauses in other contractual settings. While courts are often asked to apply the laws of another state, the North Dakota Supreme Court, implies through this decision, that out-of-state courts may be unable, or perhaps unwilling, to apply North Dakota laws.[95] Whether this is just an issue in employment related matter or a broader concern of the court is yet to be tested. Furthermore, this case leaves open the question of how the court would handle mandatory arbitration clauses.

C. ALTERNATIVE SOLUTIONS FOR EMPLOYERS

Despite the ruling in *Osborne*, there are alternative ways an employer can prevent an employee from competing. One method an employer may be interested in pursuing is making the employee a partial owner of the business.[96] Connecting a non-compete agreement to an ownership interest in the company should trigger section 09-08-06(2), which reads:

> A contract by which anyone is restrained from exercising a lawful profession, trade, or business of any kind is to that extent void, except . . . 2. Partners, members, or shareholders, upon or in anticipation of a dissolution of a partnership, limited liability company, or corporation; upon or in anticipation of a dissociation of a partner or member; or as part of an agreement addressing the dissociation or sale of a partner, member, or shareholder's ownership interest, may agree that all or any number of them will not carry on a similar business within a reasonable geographic area where the partnership, limited liability company, or corporation business has been transacted, or within a specified part of the area.[97]

A second alternative is for the employer to draft strict confidentiality and non-disclosure provisions restricting a former employee's ability to compete in the same field in the future.[98] It is important for employers to be mindful of their option to pursue claims such as trade secret violation or breach of fiduciary duty.

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95. Sean T. Foss, *ND Prohibition against Non-Competition Agreements Prevails Over Choice of Law and Forum Selection Clauses*, THE LEGAL EXAMINER (Dec. 7, 2017), https://fargo.legalexaminer.com/uncategorized/nd-prohibition-against-non-competition-agreements-prevails-over-choice-of-law-and-forum-selection-clauses/.

96. *Id.*

97. N.D. CENT. CODE § 9-08-06 (2019).

98. *Id.*

V. CONCLUSION

The decision in *Osborne*. makes clear that out-of-state companies doing business in North Dakota cannot circumvent the state's law by simply requiring employees to sign an employment agreement requiring the laws of another jurisdiction to apply. The court protected the state's right to "promote commercial activity" by keeping "one of the oldest and most continuous applications of public policy in contract law" alive.[99] The holdings of this case will certainly impact employment law in North Dakota, as well as, the future treatment of forum-selection provisions.

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99. Earthworks, Inc. v. Sehn, 553 N.W.2d 490, 493 (1996).

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