NORTH CAROLINA'S STRICT BLUE PENCIL DOCTRINE IS WRITTEN IN INK: THE SUPREME COURT RULES THAT COURTS CANNOT REVISE NONCOMPETE AGREEMENTS

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The North Carolina Supreme Court (the "Supreme Court") recently reiterated that North Carolina courts may not revise overly broad restrictions in noncompetition agreements, overturning a Court of Appeals decision that had enforced a contract provision allowing judicial reformation. Rejecting the appellate decision in *Beverage Systems of the Carolinas, LLC v. Associated Beverage Repair, LLC*, the Supreme Court affirmed North Carolina's longstanding adherence to the "strict blue pencil" doctrine, which allows courts to *strike through—but not rewrite*—unenforceable language in a noncompete, even when the noncompete purports to provide the court the power to do so.

THE BLUE PENCIL MAKES ITS MARK AT THE TRIAL COURT

Beverage Systems involved a noncompete in an asset purchase agreement intended to prevent the sellers from pursuing similar business activities in North Carolina and South Carolina for five years. The agreement included a "reformation" clause, which provided that, if a court found any of the noncompete restrictions to be unreasonably overbroad, "the maximum period, scope or geographical area that are reasonable under such circumstances shall be substituted…and the court shall be allowed to revise the restrictions…to cover the maximum period, scope and area permitted by law."

Just two years after the deal closed, the sellers started a competing company and began to solicit the buyer's customers. The buyer filed suit seeking an injunction and damages based on breach of contract, tortious interference with contract, and unfair and deceptive trade practices claims. The sellers moved for summary judgment on all claims, arguing that the noncompete was overly broad and unenforceable because it covered all of North Carolina and South Carolina although the business did not have customers throughout both states.

North Carolina courts apply a reasonableness test, which requires restrictions to be no wider in scope, time, or territory than necessary to protect a buyer's (or employer's) business interests. A noncompete's geographic scope will be found reasonable if it imposes restrictions in the territory where the business's customers are located, but broader restrictions are routinely found to be unenforceable. The restriction in this case was found to be too broad. As a result, the noncompete was unenforceable as written, and the trial court had to determine whether it could be saved in light of North Carolina's adoption of the blue pencil doctrine.

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Under the blue pencil doctrine, courts may only strike offending and distinctly separable provisions and enforce reasonable provisions that remain; they are powerless to rewrite overreaching noncompetes. For example, courts may not replace an overbroad geographic territory with a reasonable subdivision of that territory. The trial court could save the *Beverage Systems* noncompete only if the parties themselves drafted reasonable provisions that could stand independently after the court struck any unreasonable provisions.

In this instance, the noncompete contained only one territorial restriction. If the court struck that restriction, the noncompete would be unenforceable because no geographical limitations would remain. Adhering to the blue pencil doctrine, the trial court declined to exercise the authority granted by the reformation clause, refused to redraft the noncompete, and granted the seller's motion for summary judgment in its entirety. The buyer appealed.

THE COURT OF APPEALS REVERSES: PARTIALLY ERASING THE BLUE PENCIL DOCTRINE

A divided panel of the North Carolina Court of Appeals reversed the trial court's order. Although the majority agreed that the noncompete was overly broad, it determined that the trial court should have exercised the authority granted in the reformation clause to reshape the restricted territory as necessary to protect the buyer's business interests. The majority held that the blue pencil doctrine's limitations were inapplicable because the parties, "at arms-length with equal bargaining power," expressly agreed to give the trial court the authority to rewrite the noncompete. The majority reasoned that exceeding the restrictions of the blue pencil doctrine, specifically in a sale-of-business context, would allow trial courts greater flexibility in adjudicating noncompete disputes, made "good business sense and better protect[ed] both a seller's and purchaser's interests in the sale of a business." The Court of Appeals remanded the case to the trial court to revise the noncompete's offending geographic restriction and revived the buyer's claims. However, because the decision was not unanimous, the seller had a right to appeal the appellate court's break from established precedent to the Supreme Court.

THE NORTH CAROLINA SUPREME COURT TRACES THE BLUE PENCIL IN INK

Rejecting the Court of Appeals' attempt to gain greater flexibility in adjudicating noncompete disputes, the Supreme Court reversed. In an opinion authored by Justice Edmunds, the Supreme Court agreed that blue-penciling would not save the noncompete because if the unreasonable portion was stricken, the noncompete was no longer enforceable. But, the Supreme Court swiftly rejected the noncompete's reformation clause, holding that "the parties cannot contract to give a court power that it does not have." The Supreme Court explained its rationale for refusing to redraft the parties' agreement:

> Allowing litigants to assign to the court their drafting duties as parties to a contract would put the court in the role of scrivener, making judges postulate new terms that the court hopes the parties would have agreed to be reasonable at the time the covenant was executed or would find reasonable after the court rewrote the limitation. We see nothing but mischief in allowing such a procedure.

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Having invalidated the noncompete, the Supreme Court held that the trial court correctly allowed the seller's motion for summary judgment as to all claims.

HOW TO DRAFT NONCOMPETES FOR THE BLUE PENCIL

Beverage Systems eliminates all doubt that reformation clauses cannot circumvent the blue pencil rule: they are unenforceable in North Carolina. Because courts are limited to striking—as opposed to revising—offending provisions, savvy practitioners often draft noncompetes governed by North Carolina law with discrete, grammatically severable, "step-down" components that provide for alternative restraints of staggered scope. Each component covers an increasingly lesser increment of time or territory to allow a trial court to strike what it deems unreasonable but ensure the survival of at least some minimum restraint on competition by the employee. Had the *Beverage Systems* noncompete contained such discrete components, the trial court could have used the blue pencil rule to select the geographic restriction it believed was reasonable. Without them, there was no way to save the noncompete.

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