



Featured News

BUSINESS ALERT

**Sellers and Purchasers of Businesses Should
Beware of Non-Solicitation Provisions**

Blue Mountain Enterprises, LLC v. Owen (January 10, 2022) _____ Cal. 4th _____.

The *Blue Mountain Enterprises, LLC v. Owen* opinion (published on January 22, 2022) reminds us that, although non-compete and non-solicitation provisions are invalid *per se* in California, that nonetheless, exceptions to this rule do exist. One exception, codified in Business & Professions Code section 16601, provides that (i) when a person sells one hundred percent (100%) of his or her interest in a business, including over time, (ii) where the person is inferred to have also sold the business's goodwill and (iii) where the person has a non-solicitation agreement but solicits the new buyer's customers (*i.e.*, the seller's former customers), in writing; that under such a scenario, the person will be held liable under the non-solicitation agreement, notwithstanding the bright-line rule against such covenants. The facts of *Blue Mountain*, along with the legal principles therefrom, are set forth below.



In 2011, the defendant, Owen ("Owen") formed a joint venture with Acolyte Limited and Polymathic Properties, Inc. (collectively, "Polymathic"). Owen transferred his complete ownership interests in several HVAC companies, via a Contribution Agreement, to Blue Mountain Enterprises, LLC ("Blue Mountain"). Thereafter, Acolyte held a fifty percent (50%) interest in Blue Mountain, with Owen owning the other fifty percent (50%) and serving as its initial Chief Executive Officer. Blue Mountain provided Owen with an employment contract that provided, *inter alia*, that he would not solicit Blue Mountain's customers for a period of three (3) years after his employment with Blue Mountain terminated.

Of note, California law generally prohibits non-competition and non-solicitation covenants. However, Business & Professions Code section 16601 provides an exception to this general prohibition, by providing, in sum, that when a person (i) sells the goodwill of a business, and/or (ii) sells his or her full ownership in a business, and/or (iii) sells substantially all of the business's (or a subsidiary/division within the business's) assets together with the good will of the business, that in any such case, the seller and the buyer of the business may agree that the seller will not compete within a specified geographic

area in which the business so sold, so long as the buyer carries on a like business therein. In sum, therefore, when one sells a business in California, an exception to the general rule prohibiting non-compete agreements exists, such that the seller may lawfully agree not to compete with the buyer.

When Blue Mountain terminated Owen for cause five (5) years later in 2016, as part of the settlement agreement, Owen agreed to sell his interest in Blue Mountain to Polymathic, thereby transferring the remaining fifty percent (50%) of his interests in Blue Mountain. Further, the settlement agreement provided that although Polymathic would waive the non-compete provision in Owen's employment agreement, Polymathic did not waive the non-solicitation and covenant against disclosure provisions in Owen's employment agreement—Owen agreed to this arrangement.

Having been terminated but while the non-solicitation provision was still in operation, and after having also conveyed, in aggregate, his one hundred percent (100%) interest in Blue Mountain (via two (2) transfers several years apart), Owen then formed a new construction company, Silvermark, in order to compete directly with Blue Mountain. In so doing, Owen sent correspondence to a number of other HVAC companies, some of whom were Blue Mountain customers. Owen's correspondence commenced with the words, "To my friends; past and potential future clients; and the general public". Owen's letter went on to advise that Owen had recently sold his interests in Blue Mountain, that he had "made the decision to launch a new enterprise with greater perspective, more resources and a much stronger team", and it introduced, by name, two (2) former Blue Mountain employees who had joined Silvermark, and "who combined, bring over 100 years of experience in the HVAC industry." The letter concluded with the sentence, "I thank everyone who supports us in this transition and look forward to the remarkable opportunities we have ahead with our new company, Silvermark Construction Services, Inc." In response, at least four (4) of Blue Mountain's customers invited Silvermark to bid on jobs.

Blue Mountain filed suit, obtained temporary then permanent injunctive relief prohibit Owen from further soliciting Blue Mountain's customers, and ultimately succeeded on its summary adjudication for breach of contract. Although unsuccessful at the trial court level, Owen nonetheless argued that his solicitation, if any, was permitted because the non-solicitation provision in his above-referenced employment agreement failed to meet the requirements of Business & Professions Code section 16601. Specifically, Owen argued that because he had only recently sold fifty percent (50%) of his interest in Blue Mountain, and thus, neither his "full ownership" in, nor the goodwill of the business, that the provision in his employment agreement, which remained viable and prohibited him from soliciting Blue Mountain's customers for a period of three (3) years, was unenforceable.

The trial court, in granting injunctive relief, noted that contrary to Owen's argument otherwise, Owen had, in fact, conveyed one hundred percent (100%) of his interest in his former companies, via Contribution Agreement with Blue Mountain. Thus, it did not matter that Owen held fifty percent (50%) of Blue Mountain or not, nor did it matter when he conveyed back his interest in Blue Mountain. This "global business deal", along with the "interfere[ence]" that, in selling his interests, Owen conveyed the good will belonging to the entities he conveyed to Blue Mountain, rendered the non-solicitation provision in his employment agreement, to be fully enforceable. The Court of Appeal upheld the trial court's decision, holding that it would be unfair to permit someone to directly solicit the

customers of the business that the person had just sold—especially where, here, Owen received consideration in exchange for promising not to solicit Blue Mountain’s customers. The trial court also concluded that the above-referenced solicitation letter was, indeed, a solicitation as a matter of law.

The above case demonstrates the nuances and intricacies involved in purchasing and selling businesses, including with respect to future rights arising from the purchase or sale of business. If you are purchasing or selling a business, and you would like to obtain more information about non-solicitation and/or non-compete provisions vis-à-vis that purchase or sale, please contact this office for assistance.



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