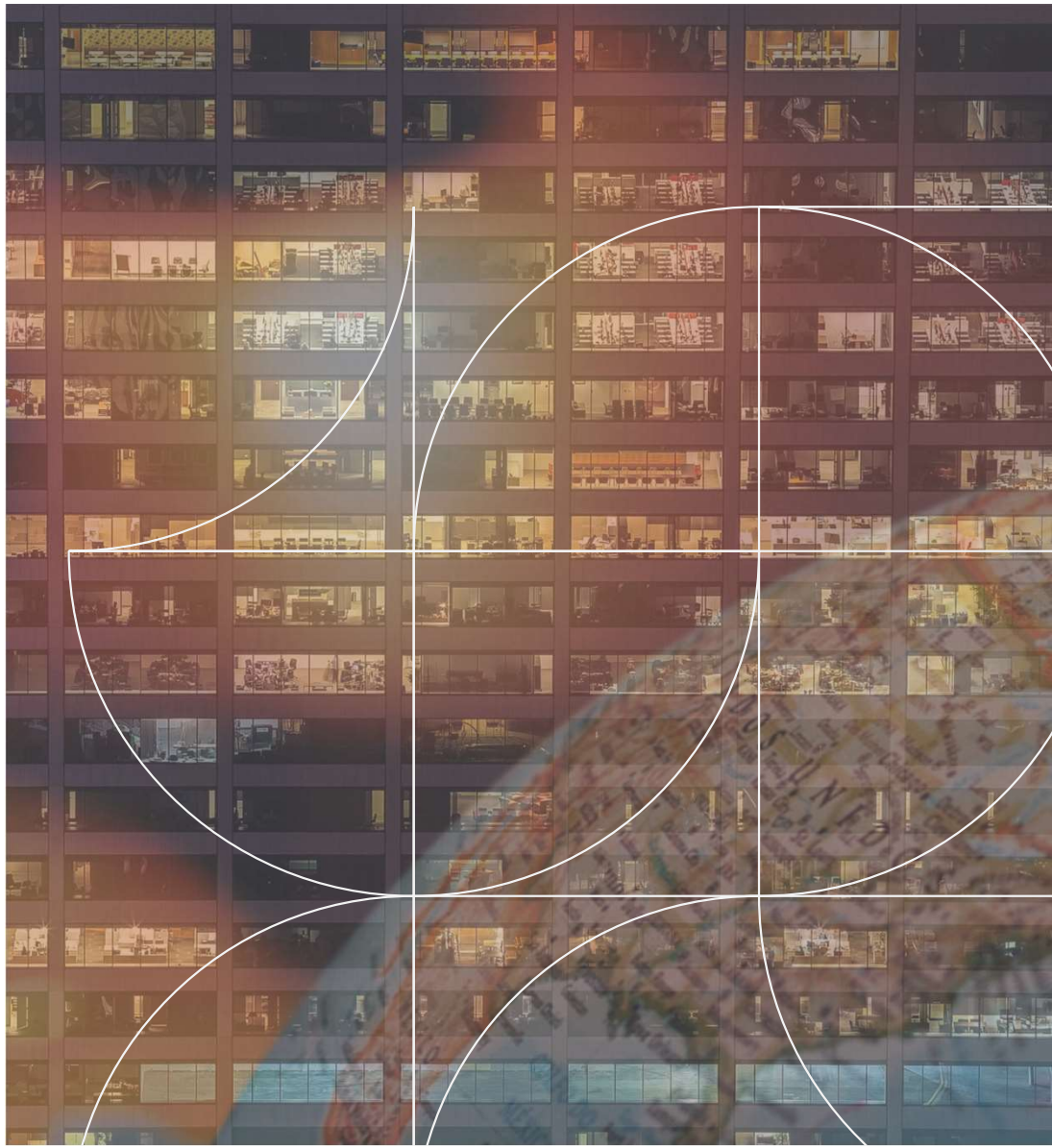
Seyfarth

What Employers Need to Know Regarding Non-Compete Changes in 2023

November 29, 2023



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Today's Panel

Dawn Mertineit
Eastern Region

Marcus Mintz
Midwestern Region

Dan Hart
Southern Region

Robert Milligan
Western Region

Agenda

01 Introduction and Overview

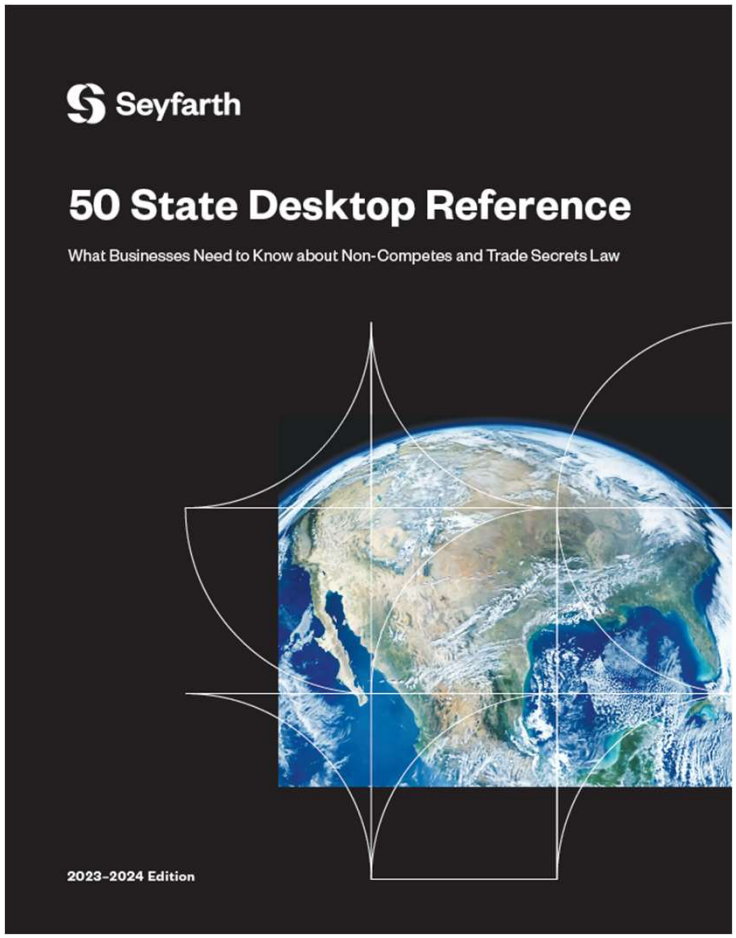
02 Federal Updates

03 2023 Regional Changes

04 California’s New Laws

05 Key Takeaways

06 Q&A

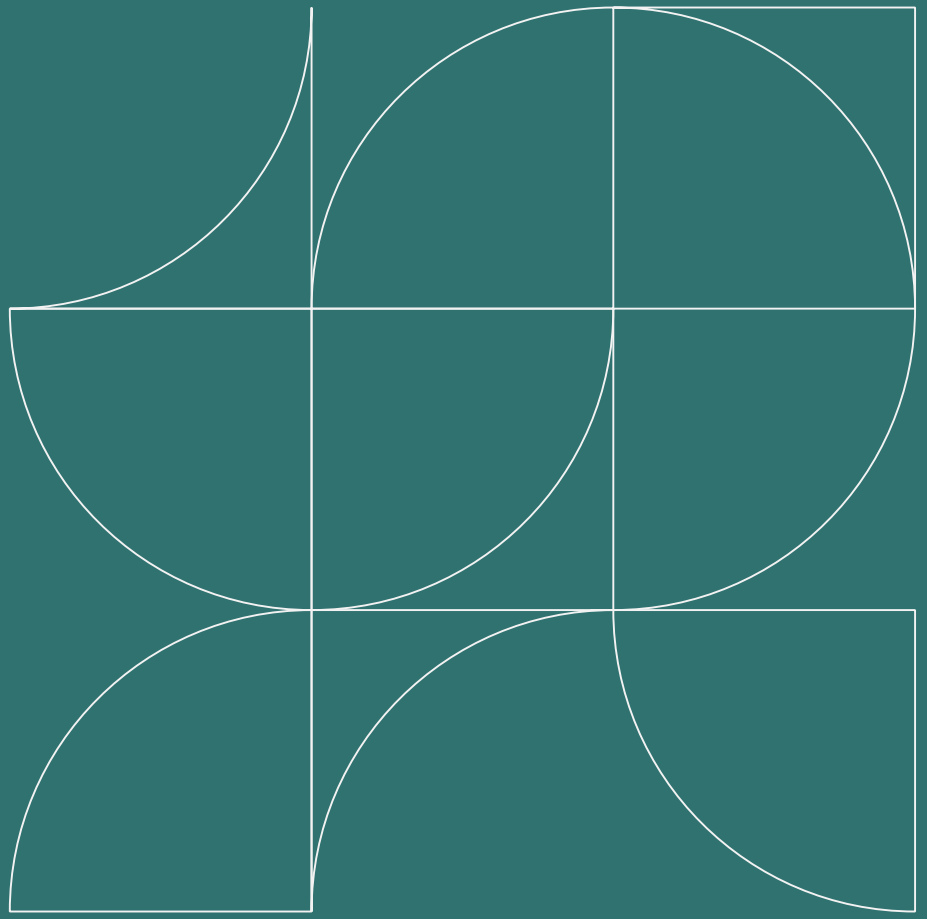


2023-2024 EDITION NOW AVAILABLE!

Seyfarth's 50-State
Non-Compete Desktop Reference

- **Comprehensive Updates:** Covering key jurisdictions such as California, New York, and more.
- **In-Depth Topics:** Covers vital aspects such as penalty frameworks, wage thresholds, and notice requirements.
- **Expert Contributions:** Draw from the knowledge of our Trade Secrets, Computer Fraud, and Non-Competes practice group.

Federal Update



FTC Rulemaking

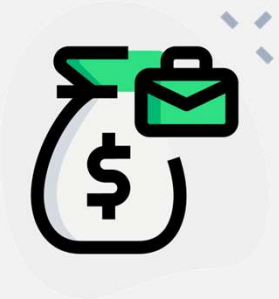
- **January 5, 2023**, the Federal Trade Commission ("FTC") published a proposed rule banning all non-compete agreements
- Proposed ban unlikely to affect non-solicitation and non-disclosure covenants
- Comment period was extended through **April 19, 2023**
- Received over 27,000 public comments
- Hosted public forum
- Employer protections vs. employee mobility
- Vote on proposed rule likely delayed to **April 2024**
- If passed, likely to face an immediate challenge
- More information and analysis is available at www.tradesecretslaw.com

NLRB GC Memorandum

- May 30 memo claims that non-competes in employment and severance agreements interfere with workers' rights under Section 7 of the Act, which protects employees' right to self-organize, join labor organizations, bargain collectively, and "engage in other concerted activities for the purpose of collective bargaining or other mutual aid or protection."
- Concludes that non-competes typically violate Section 8(a)(1) of the Act, which makes it an unfair labor practice for an employer to interfere with an employee's Section 7 rights.

NLRB GC Memorandum: Rationale

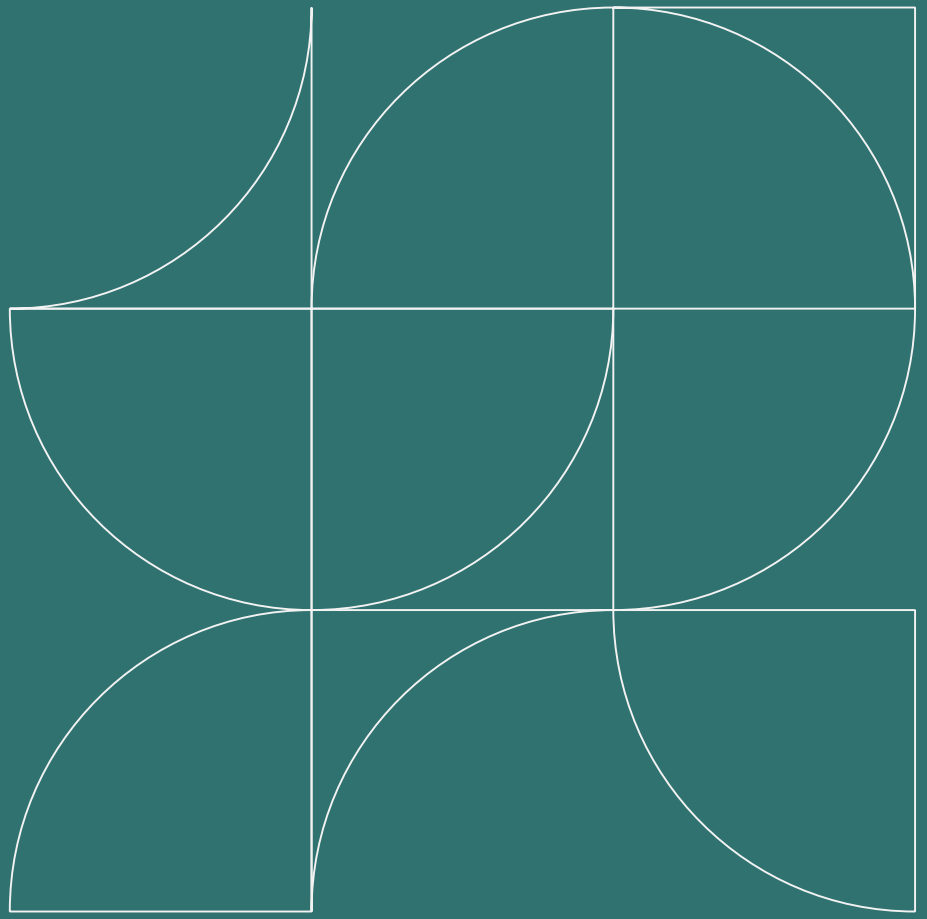
- Claims that non-competes "are overbroad" and can be construed by employees as "deny[ing] them the ability to quit or change jobs by cutting off their access to other employment opportunities that they are qualified for based on their experience, aptitudes, and preferences as to type and location of work."
- Claims that non-competes chill protected activity, because employees who perceive that they cannot seek new employment may be discouraged from threatening to resign *en masse,* concertedly seeking to join a competitor, and more.



Fluctuating Wage Thresholds

- **Colorado**: salary at the time of execution and enforcement is equal to or greater than "the threshold amount for highly compensated workers as determined by the Division of Labor Standards and Statistics in the Dep't of Labor and Employment" (**$112,500**)
- **Maine**: 400% of the federal poverty level (**$58,320**)
- **Maryland**: 150% of state minimum wage (**$41,350**; set to rise to **$46,800** in 2024)
- **Oregon**: annual gross salary and commissions at termination "exceeds the median family income for a four-person family, as determined by the United States Census Bureau" (**$108,575.64**)
- **Rhode Island**: 250% of the federal poverty level (**$36,450**) or non-exempt under FLSA
- **Virginia**: Average weekly wage for workers in the commonwealth (**$69,836**)
- **Washington**: "adjusted annually in accordance with RCW 49.62.040: (**$116,593.18**)

Eastern Region



2023 Non-Compete Changes

- **Connecticut:**
  - New restrictions on non-competes for healthcare workers
  - Non-competes entered, amended, extended, or renewed on or after 10/1/23 are unenforceable if the physician doesn't agree to "a proposed material change to compensation terms"
  - "Primary site of practice" (for 15-mile radius limitation) must be mutually defined by parties
  - Doesn't apply to group practices with fewer than 35 physicians in which majority ownership is physicians
  - Non-compete protections (1 year, 15-mile radius) now extended to APRNs and PAs as well as physicians (but no exception for small group practice)

Legislation on the Horizon

- **New York:**
  - Proposed non-compete **ban**
  - Applies to any worker, employee, or independent contractor
  - Employers who violate the proposed ban would be subject to damages of $10,000 per violation and be required to pay lost compensation, damages, attorneys' fees, and costs
  - Ambiguous as to the applicability to the sale of a business
  - Approved by the New York legislature on June 20, 2023
  - Governor Hochul has until the end of the year to sign

Key Cases and Precedents

- **Delaware:**
  - A group of cases out of Delaware signal an uphill battle for those using Delaware law for restrictive covenants, even in the context of the sale of a business

    - *Kodiak Building Partners, LLC v. Adams*
      - Restrictive covenants in acquisition were overbroad; declining to reform

    - *Ainslie v. Cantor Fitzgerald L.P.*
      - Forfeiture-for-competition clause in the partnership agreement was “unreasonable and therefore unenforceable” due to the worldwide scope and overbroad scope of prohibited conduct; again, declining to reform the covenants

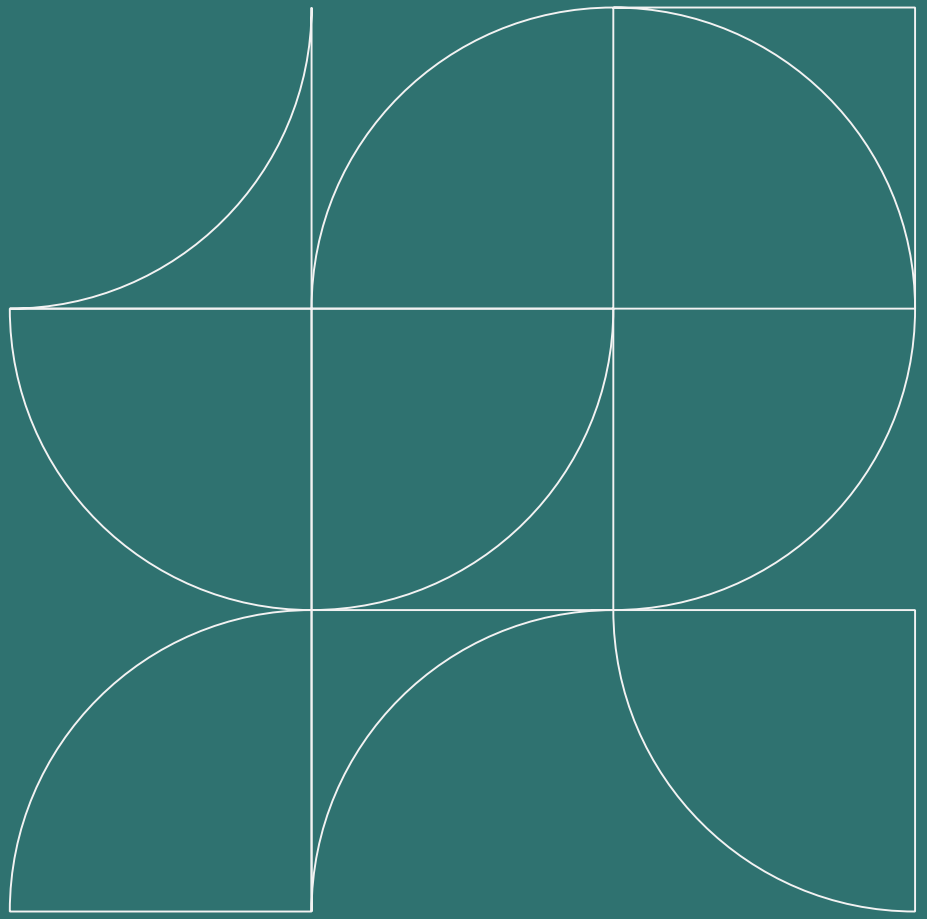
Key Cases and Precedents

- **Delaware (cont'd):**
  - *Intertek Testing Sys. v. Eastman*
    - Stock purchase agreement's worldwide non-compete was overbroad; refusing to blue pencil the covenants as doing so would "save Intertek – a sophisticated party – from its overreach [which] would be inequitable."
  - *Centurion Service Grp. LLC v. Wilensky*
    - Two-year, nationwide non-compete in VP's employment agreement struck down based on overbroad geographic and temporal scope
    - DE choice of law invalidated in favor of IL law
    - The court again declined to blue pencil the covenants to render them enforceable
  - *Hightower Holding LLC v. Gibson*
    - Invalidated DE choice of law and applying AL law
    - Refused to issue an injunction, finding duration, geographic scope, and scope of proscribed conduct was all overbroad

Key Cases and Precedents

- **Massachusetts:**
  - *Cynosure, LLC v. Reveal Lasers LLC*
    - Finding that DE choice of law does not obviate non-compete requirements under the MNAA for MA residents
    - Stock options constitute mutually agreed-upon consideration
    - Start of employment is sufficient consideration
- Second Circuit:
  - *Syntel Sterling Best Shores Mauritius Ltd. v. TriZetto Grp.*
    - Unjust enrichment damages cannot be awarded under the DTSA for avoided development costs absent evidence that the trade secret's value was diminished by misappropriation.
- Fourth Circuit:
  - *Synopsys, Inc. v. Risk Based Security, Inc.*
    - The trade secret's value must come from its ***secrecy***

Southern Region



Key Cases and Precedents

- **Georgia**
  - *North American Senior Benefits, LLC v. Wimmer*, 368 Ga. App. 124 (2023): Georgia Court of Appeals held that a geographic limitation is required for an employee non-solicit to be enforceable
  - *Motorsports of Conyers, LLC v. Burbach*, 317 Ga. 206 (2023): Supreme Court of Georgia held that a Georgia court must determine if a restrictive covenant is enforceable under Georgia law before determining whether to enforce a choice

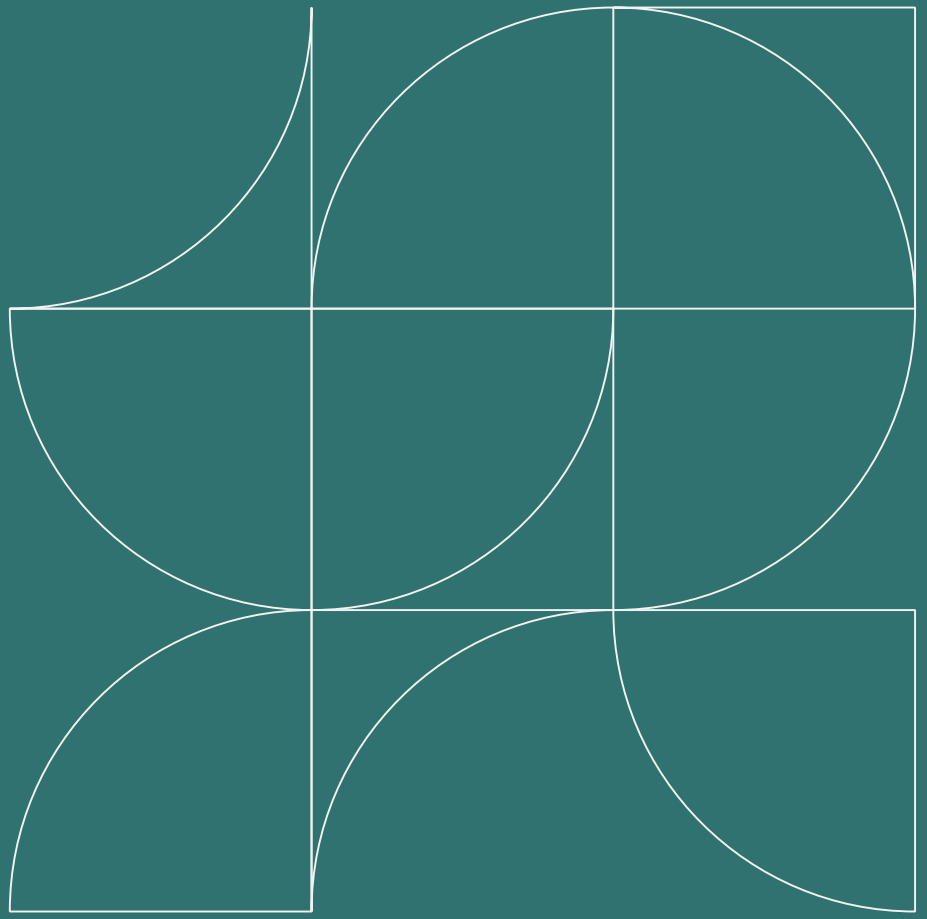
Legislation on the Horizon

- **Arkansas:** HB 1628 (died in House committee) -- Would have enacted near-total ban on employee non-competes

- **Oklahoma:** SB 697 (pending in Senate) – Would enact Uniform Restrictive Employment Agreement Act.

- **Texas:** HB 1043 (died in House without floor vote) -- Would have banned non-competes for low-wage workers (workers who earn not more than the greater of: (1) the federal minimum wage or (2) $15 an hour))

Midwestern Region



2023 Non-Compete Changes

- **Minnesota** – All employee non-compete agreements banned going forward effective July 1, 2023.
  - Sale of business is exempted.
  - Non-solicit and non-disclosure covenants expressly allowed
  - Foreign choice-of-law and venue provisions are prohibited
- **Missouri** – New presumptions of enforceability for restrictive covenants between businesses and owners of businesses effective 8/28/2023
  - Employee non-solicits are presumed enforceable if 2 years or less
  - Customer non-solicits are presumed enforceable if 5 years of less
  - Courts expressly authorized to reform overbroad restraints
- **South Dakota** – Non-competes banned for healthcare practitioners for contracts entered into after July 1, 2023.

Legislation on the Horizon

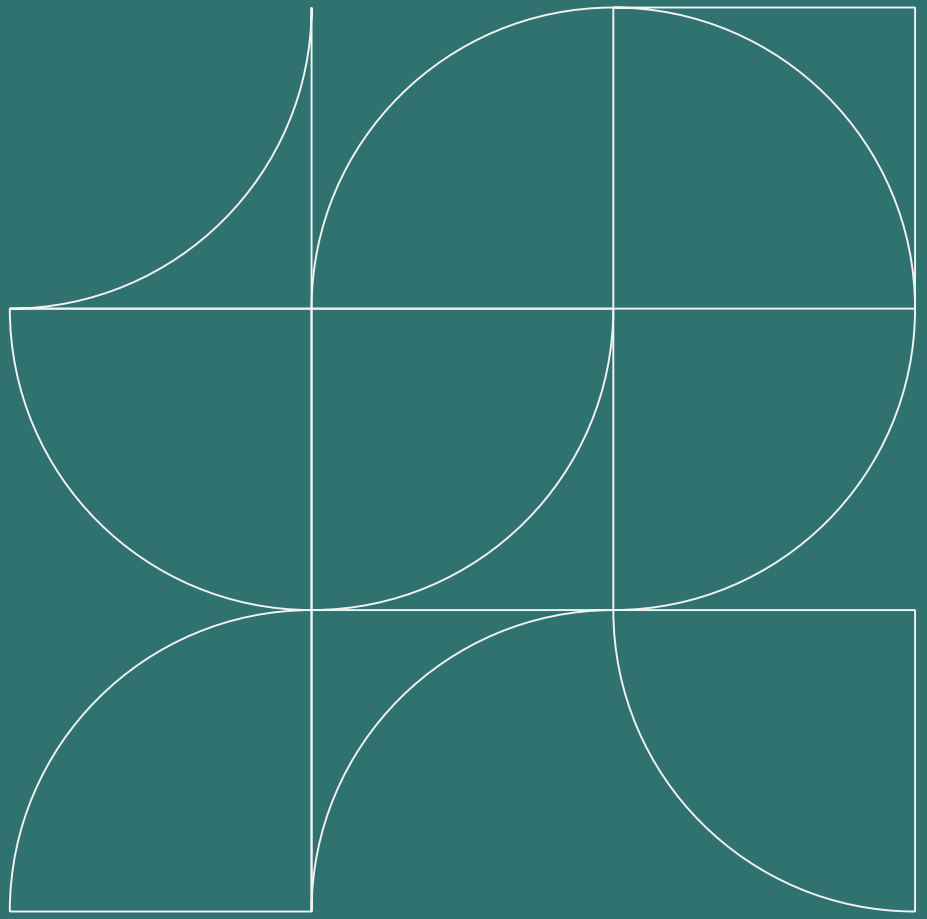
- **Michigan** – House Bill 6031, pending since April 24, 2022
  - Prohibits non-competes for low-wage employees (earning 138% or less of the federal poverty line)
  - Notice requirements
  - $5,000 penalty for each violation
- **Wisconsin** – AB 481, introduced October 12, 2023
  - Prohibit post-employment non-compete agreements
  - Open question of whether the legislation would also apply to non-solicit covenants
  - Likely no effect on sale-of-business covenants

Key Cases and Precedents

Illinois

- *Midwest Lending Corp. v. Horton*, 2023 IL App (3d) 220132
  - the Appellate Court affirmed the trial court's dismissal of the plaintiff's complaint pursuant to which the plaintiff sought to enforce certain post-employment restrictive covenants.
  - Defendant, who was employed for only seven months, challenged the enforceability of the restrictive covenant agreement because he was not employed for at least two years and received no other consideration.
  - In response, plaintiff relied upon a $25,000 sign-on bonus that defendant received as part of his offer letter and claimed that this bonus was "adequate consideration." The court disagreed because the offer letter never identified the restrictive covenant agreement nor any of its terms. As such, the plaintiff failed to demonstrate that the bonus was consideration expressly provided in exchange for the defendant agreeing to the terms of the restrictive covenant agreement.

Western Region



2023 Non-Compete Changes

- Two new laws passed in **California** that make non-compete provisions with employees unlawful and require employers to notify current and former employees (going back to January 1, 2022) that they are void. Prohibit employers from attempting to enforce a contract that is void regardless of whether the contract was signed and the employment was maintained outside of California.
- **Montana** passes law banning non-competes for certain medical professions (psychologists and counselors)
- Increase in salary thresholds for non-competes in **OR** and **WA**. The thresholds for noncompete agreements will rise to **$120,559.99** for employees and approximately **$301,399.98** for independent contractors in WA.

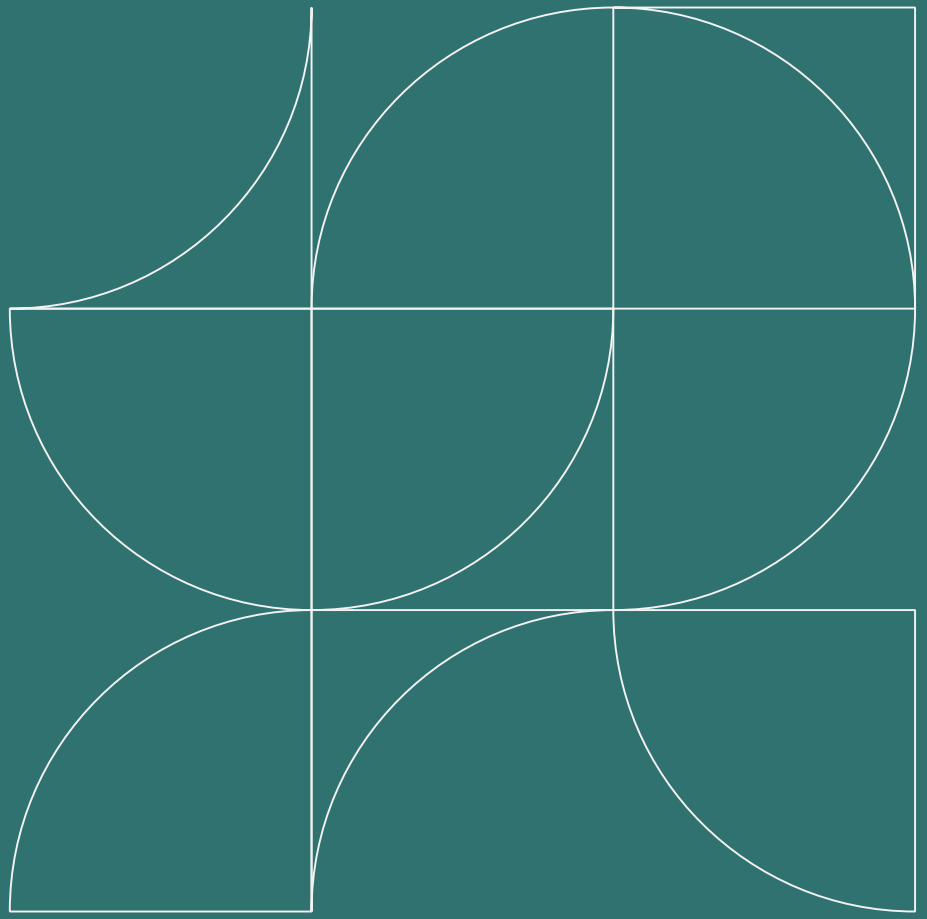
Legislation on the Horizon

- **Utah**, attempt in 2023 to curtail the use of non-competes with healthcare providers
- **Nevada**, attempt to ban physician non-competes passed both houses but Governor vetoed
- **New Mexico**, attempt to ban non-solicitation provisions with physicians and prohibit out-of-state choice of law and forum clauses did not go forward
- **Hawaii**, attempt to ban noncompetes with workers in a restaurant, retail store, newspaper, magazine, news agency, press association, wire service, or radio or television transmission station or network
- ***California, always something…***

Key Cases and Precedents

- ***Nevada**, Tough Turtle Turf, LLC v. Scott*, 139 Nev. Adv. Op. 47 (Nov. 2, 2023).
- NRS 613.195(6) provides that a district court" shall revise . . . to the extent necessary" a noncompete that unreasonably limits the time, geographical area, or scope of activity; a greater restraint than is necessary to protect the employer; or imposes undue hardship on the employee.
- NRS 613.195(1) which declares a noncompete "void and unenforceable" if it imposes a restraint greater than necessary to protect the employer; any undue hardship on the employee; or restrictions that are not appropriate in relation to the valuable consideration supporting the agreement.
- In *Tough Turtle*, the Nevada Supreme Court read these provisions together to hold that while a district court is not always required to modify an overbroad noncompete agreement, it must do so "when possible."

California's New Non-Compete Laws



SB 699

Adds Section 16600.5 to the Business and Professions Code

THE PEOPLE OF THE STATE OF CALIFORNIA DO ENACT AS FOLLOWS:

SECTION 1. The Legislature finds and declares the following:

- (a) Noncompete clauses in employment contracts are extremely common in the United States. Research shows that one in five workers are currently subject to a noncompete clause out of approximately 30 million workers nationwide. The research further shows that California employers continue to have their employees sign noncompete clauses that are clearly void and unenforceable under California law. Employers who pursue frivolous noncompete litigation has a chilling effect on employee mobility.
- (b) California's public policy provides that every contract that restrains anyone from engaging in a lawful profession, trade, or business of any kind is, to that extent, void, except under limited statutory exceptions. California has benefited significantly from this law, fueling competition, entrepreneurship, innovation, job and wage growth, equality, and economic development.
- (c) Over the past two decades, research on the harm of noncompete clauses and other contract clauses involving restraint of trade to pursue one's profession has been accelerating. Empirical research shows that noncompete clauses stifle economic development, limit firms' ability to hire and depress innovation and growth. Noncompete clauses are associated with suppressed wages and exacerbated racial and gender pay gaps, as well as reduced entrepreneurship, job growth, firm entry, and innovation.
- (d) Recent years have shown that employers utilizing broad noncompete agreements attempt to subvert this longstanding policy by requiring employees to enter void contracts that impact employment opportunities once an employee has been terminated from the existing employer. Moreover, as the market for talent has become national and remote work has grown, California employers increasingly face the challenge of employers outside of California attempting to prevent the hiring of former employees.
- (e) The California courts have been clear that California's public policy against restraint of trade law trumps other state laws when an employee seeks employment in California, even if the employee had signed the contractual restraint while living outside of California and working for a non-California employer.
- (f) California has a strong interest in protecting the freedom of movement of persons whom California-based employers wish to employ to provide services in California, regardless of the person's state of residence. This freedom of employment is paramount to competitive business interests.

SB 699

Adds Section 16600.5 to the Business and Professions Code

- **SEC. 2. Section 16600.5 is added to the Business and Professions Code, to read:**
  - 16600.5. (a) Any contract that is void under this chapter is unenforceable regardless of where and when the contract was signed.
  - (b) An employer or former employer shall not attempt to enforce a contract that is void under this chapter regardless of whether the contract was signed, and the employment was maintained outside of California.
  - (c) An employer shall not enter into a contract with an employee or prospective employee that includes a provision that is void under this chapter.
  - (d) An employer that enters into a contract that is void under this chapter or attempts to enforce a contract that is void under this chapter commits a civil violation.
  - (e) (1) An employee, former employee, or prospective employee may bring a private action to enforce this chapter for injunctive relief or the recovery of actual damages, or both.
  - (2) In addition to the remedies described in paragraph (1), a prevailing employee, former employee, or prospective employee in an action based on a violation of this chapter shall be entitled to recover reasonable attorney's fees and costs.

SB 699

Legislative History

LEGISLATIVE HISTORY of SB 699:

- The bill was author sponsored and supported by Maravail Life Sciences, the California Employment Lawyers Association, and a number of law school professors. Also supported by California Hispanic Chambers of Commerce.
- Maravail Life Sciences stated, the "use of noncompete clauses in employment contracts, can have a chilling effect on employee mobility and stifle economic development. Research has shown that noncompete clauses limit firms' ability to hire and depress innovation, growth, and are **associated with suppressed wages and exacerbated racial and gender pay gaps."**
- The author further states that the bill promotes **economic equity** because it "allows employees or potential employees to recover attorney's fees and other related costs, which is sometimes the difference between pursuing litigation and not, for folks who do not have the means. SB 699 not only increases the incentives not to restrict employees' freedom of movement in the employment sense, but also ensures benefits to employees who prevail, helping to recover for the time they were left unemployed due to the noncompete as well."

SB 699

Legislative History

Legislative History of SB 699:

"Despite California's strong laws and public policy against noncompetition agreements, **companies that do business in California continue to attempt to enforce noncompete agreements against California residents.** As the market for talent has become national and remote work has grown, **California employers increasingly face the challenge of employers outside of California attempting to prevent the hiring of former employees. Employers who pursue frivolous noncompete litigation can have a chilling effect on employee mobility.** SB 699 seeks to strengthen penalties for employers who attempt to utilize non-competes, making them liable for actual damages and penalties. The bill would also authorize a prospective employee to bring an action for injunctive relief and for the recovery of those damages and penalties, and would provide that a prevailing employee is entitled to recover reasonable costs and attorney's fees."

AB 1076

Amends Section 16600 and adds Section 16600.1 to the Business and Professions Code

- **SECTION 1. Section 16600 of the Business and Professions Code is amended to read:**
  - 16600. (a) Except as provided in this chapter, every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void.
  - (b) (1) This section shall be read broadly, in accordance with *Edwards v. Arthur Andersen LL*P (2008) 44 Cal.4th 937, to void the application of any noncompete agreement in an employment context, or any noncompete clause in an employment contract, no matter how narrowly tailored, that does not satisfy an exception in this chapter.
  - (2) This subdivision does not constitute a change in, but is declaratory of, existing law.
  - (c) This section shall not be limited to contracts where the person being restrained from engaging in a lawful profession, trade, or business is a party to the contract.

AB 1076

Amends Section 16600 and adds Section 16600.1 to the Business and Professions Code

- **SEC. 2. Section 16600.1 is added to the Business and Professions Code, to read:**
  - 16600.1. (a) It shall be unlawful to include a noncompete clause in an employment contract, or to require an employee to enter a noncompete agreement, that does not satisfy an exception in this chapter.
  - (b) (1) For current employees, and for former employees who were employed after January 1, 2022, whose contracts include a noncompete clause, or who were required to enter a noncompete agreement, that does not satisfy an exception to this chapter, the employer shall, by February 14, 2024, notify the employee that the noncompete clause or noncompete agreement is void.
  - (2) Notice made under this subdivision shall be in the form of a written individualized communication to the employee or former employee, and shall be delivered to the last known address and the email address of the employee or former employee.
  - (c) A violation of this section constitutes an act of unfair competition within the meaning of Chapter 5 (commencing with Section 17200).

AB 1076

Legislative History

Legislative History of AB 1076

The bill was author sponsored and is supported by Attorney General Rob Bonta, The California Employment Lawyers Association, the California Nurses Association/National Nurses United, the California Teamsters, and Economic Security Project Action.

According to the author, “AB 1076 protects employees by prohibiting the inclusion of noncompete agreements in an employee’s contract. Although noncompete agreements are not enforceable in California, employers continue to include them in contracts which misleads employees and threatens their job prospects. **These noncompete agreements were originally meant to protect businesses’ trade secrets, but they have disproportionately harmed women and people of color. The exploitative practice of including noncompete agreements deprives workers of fair compensation, stifles innovation, and deters entrepreneurism.** This bill ensures that no employee is faced with signing away their rights as a condition of employment.”

The California Nurses Association/National Nurses United (CNA) was in support and stated:

> "While businesses with high pay or high levels of education are generally more likely to use noncompete agreements, noncompetes are also common in workplaces with low pay and where workers have fewer education credentials. According to the Economic Policy Institute approximately 30% of establishments offering an average hourly wage below $13 require noncompete agreements for all their workers."

AB 1076

Legislative History

Legislative History of AB 1076

Attorney General Rob Bonta noted that "approximately 45% of businesses still include noncompete clauses in employment contracts in the state." The Attorney General explains that these "agreements generally require workers to refrain from accepting new employment opportunities in a similar line of work or establishing a competing business, usually for a specified period of time and within a geographic area." The Attorney General further explains that while **"Edwards confirmed that such clauses are unenforceable, putting an unenforceable term in a contract is not necessarily unlawful."**

According to Bonta, the bill strengthens California's restraint of trade prohibitions by making it unlawful to include a noncompete clause in an employment contract, or to require an employee to enter a noncompete agreement, that does not satisfy a statutory exception.

Staff Comments: It is unknown how many additional actions would be brought as a result of the implementation of this bill. **The DOJ anticipates that there will be a significant increase in complaints about violations of law should AB 1076 pass.** The DOJ estimates it would need 2.0 deputy attorney general positions and the complement of 2.0 legal secretaries, at an annual, ongoing rate of approximately $800,000.

The California Employment Lawyers Association, in support of AB 1076, explained that "although noncompete clauses have been unlawful in California since 1872, our attorneys routinely see these clauses included in employment agreements with California employees. **These clauses restrict workers from freely switching jobs, which lowers overall wages, and undermines fair competition. These clauses can have a significant chilling effect on workers who may not understand that such agreements are void under California law.**

SB 699
AB 1076

Amend Sections 16600 of and add Sections 16600.1 and 16600.5 to the Business and Professions Code

- Makes any contract that is void as a restraint on trade (including non-competes) unenforceable regardless of where and when the employee signed the contract
  - No matter how narrowly tailored, with limited exceptions, even when the person restrained is not a party to the contract
- Prohibits employers from entering contracts with current or prospective employees that contain non-compete provisions
- Employers entering into these agreements or attempting to enforce them are liable for injunctive relief, damages, and attorneys' fees/costs under SB 699
- AB 1076 requires **affirmative notice** to current and former employees by February 14, 2024, that any noncompete clause/agreement previously signed is now void
- States a violation constitutes an act of unfair competition under BPC 17200 *et seq.*

Impact on Labor Code 925 and Constitutional Issues

- How will the new laws interact with California Labor Code Section 925, which prohibits employers from requiring employees who primarily reside and work in California to agree **as a condition of employment** to adjudicate claims outside of the state or deprive the employee of the substantive protection of California law, **unless the employee was represented by legal counsel.**

- It is also unclear what effect a judgment secured outside of California enforcing a noncompete would have within the state and whether full faith and credit would be honored by a CA court. SB 699 raises constitutional issues as well, including whether the law poses an undue burden on interstate commerce (e.g. dormant commerce clause) or impairs the obligation of contracts entered outside the state.

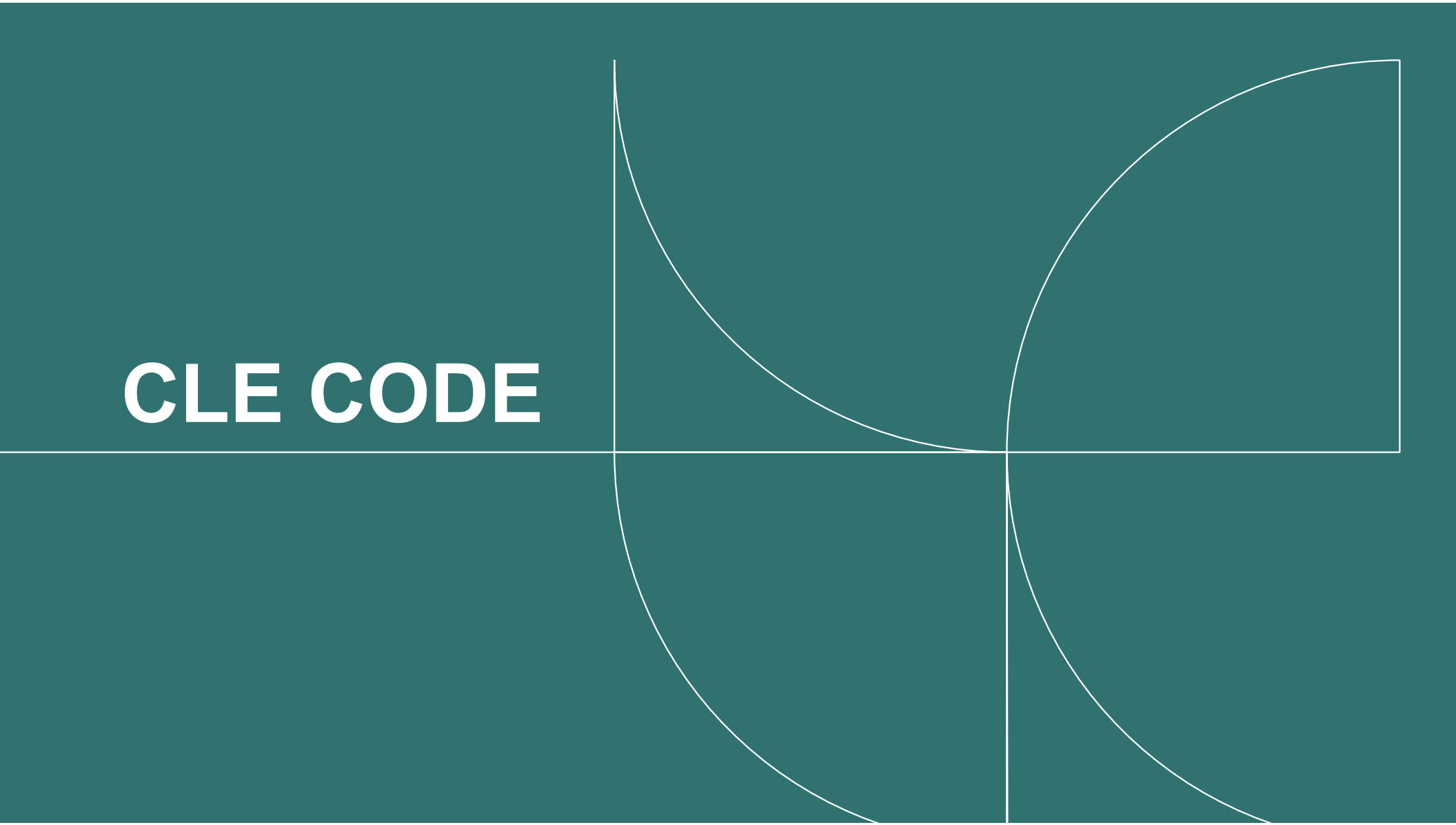
What this means for employers.

1. Identifying Covered Employees
2. Analyzing Restrictive Covenants
3. Providing Individualized Notification
4. Updates and Amendments to Agreements
5. Applicability to Out-of-State Employees
6. Removal of Post-Termination Employee Non-Solicit Provisions?
7. Potential Lawsuits and PAGA Considerations
8. Exceptions under CA law to the ban?
9. FAQ from Clients

Key Takeaways

1. **Review and Enhance Restrictive Covenant Agreements**
   - Conduct a comprehensive review of existing agreements
   - Implement updates to align with current legal standards
2. **Customize Restrictions for Maximum Protection**
   - Tailor restrictions to address specific needs:
     - Non-solicit clauses for sales representatives
     - Non-compete clauses for C-Suite and executives
     - Non-disclosure clauses for mid-level employees and below who are non-customer facing
3. **Consideration of State-Specific Nuances**
   - Recognize the importance of adapting strategies to accommodate state-specific legal requirements
   - Ensure compliance with regional regulations for comprehensive protection

Q&A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For further details, reach out to a member of our Trade Secrets, Computer Fraud, and Non-Competes Practice Group, and explore our blog at

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