SEYFARTH SHAW

Management Alert

Top 10 Developments and Headlines in Trade Secret, Non-Compete, and Computer Fraud Law in 2018/2019

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Continuing our annual tradition, we have compiled our top developments and headlines for 2018–2019 in trade secret, non-compete, and computer fraud law.

1. Government Agencies Increasing Scrutiny of Restrictive Covenants

In mid-2018, the Attorneys General of ten states investigated several franchisors for their alleged use of "no poach" provisions in their franchise agreements. In a July 9, 2018 letter, the Attorneys General for New Jersey, Massachusetts, California, Washington, D.C., Illinois, Maryland, Minnesota, New York, Oregon, Pennsylvania, and Rhode Island requested information from several franchisors about their alleged use of such provisions. Less than twenty-four hours later, some franchisors (mostly different ones than those who received the information demands) entered into agreements with the Washington State Attorney General's Office to remove such clauses from their franchise agreements. The recent focus by state law enforcement on franchisors is a new twist, given that restrictive covenant agreements in the franchise industry are typically given more leeway than in the employment context.

In a settlement with the office of New York Attorney General, a large employer agreed to drop its non-compete requirement for all employees except high-level executives, consistent with a policy in favor of employee mobility.

On the federal level, Assistant Attorney General Makan Delrahim announced in 2018 that the DOJ had been "very active" in reviewing potential antitrust violations stemming from agreements among employers not to compete for workers. Employers should remain vigilant and confirm their compliance with these laws, as employers may face DOJ enforcement actions and class action litigation.

2. Supreme Court Grants Cert. to Interpret Meaning of "Confidential" or "Trade Secret" Under FOIA

On January 11, 2019, the Supreme Court accepted certiorari in *Food Marketing Institute v. Argus Leader Media* to reconcile fractured circuit tests on when the government may withhold information from a Freedom of Information Act ("FOIA") request based on responsive information being confidential or a trade secret. The case has major potential ramifications for the protections given to sensitive information submitted by companies to the government, whether voluntarily, under

compulsion (say, via grand jury or administrative subpoena) or as part of reporting obligations. For anyone or entity that does business or interfaces with the government, the Supreme Court's decision in *Food Marketing Institute* will be one to closely watch.

3. Whistleblower Protection

In what appeared to be a first under the DTSA, the Eastern District of Pennsylvania federal court in *Christian v. Lannett Co.*, Inc. threw out claims against an alleged trade secret thief on the basis of the DTSA's immunity for confidential disclosures to attorneys in the course of investigating a suspected violation of the law.

In *MMM Holdings, Inc. v. Reich*, a California Court of Appeal held that the receipt, retention, and dissemination of confidential information by a whistleblower's attorney is protected under the state's anti-SLAPP statute, adding to the protections for attorneys who in similar factual circumstances, use or disclose confidential documents in related actions.

In *Anheuser-Busch Companies, LLC, et al v. James Clark*, a Ninth Circuit panel heard oral arguments in late 2018 concerning the denial of a former employee's anti-SLAPP motion in a trade secret misappropriation and breach of contract case. This is the second time the case has made its way up to the Ninth Circuit. The panel has not yet issued its decision but the Ninth Circuit's decision could have far reaching implications for trade secret and data theft cases involving purported whistleblowing activities.

4. Notable Trade Secrets Cases

On the civil side, a Texas jury awarded over $700 million in damages to a technology start-up regarding the alleged misappropriation of its real estate valuation trade secrets.

On the criminal side, a Chinese scientist was sentenced to over 10 years in prison for conspiring to steal proprietary rice seeds for representatives of a Chinese crop institute.

In a matter of first impression under the DTSA, the Fifth Circuit held that a dismissal without prejudice of a DTSA case does not support an award of prevailing party attorney's fees.

The Fifth Circuit's decision in *Brand Services v. Irex*, combined with prior Louisiana appellate court rulings, largely settles the scope of the LUTSA's preemption for future disputes. The LUTSA only preempts claims based on actual trade secrets, not claims based on confidential information outside the definition of a trade secret.

The Texarkana Court of Appeals took the extraordinary measure of affirming an award of plaintiff attorney's fees against a defendant for willful and malicious misappropriation of trade secrets in an amount that was ultimately more than 50 times higher than the plaintiff's actual awarded damages.

For further information about the DTSA, please see our desktop reference: "The Defend Trade Secrets Act: What Employers Should Know Now."

5. Expansions of California's Business & Professions Code § 16600

A California Court invalidated a non-solicitation of employees provision as an unlawful restraint of trade in violation of section 16600 (i.e., California's non-compete statute), where the employees at issue were travel nurse recruiters who left their employer for a competitor. In *AMN Healthcare, Inc. v. Aya Healthcare Services, Inc. et al.*, No. D071924, 2018 WL 5669154 (Cal. App. 2018), the court rejected a "reasonableness" approach to employee non-solicitation provisions, emphasizing the plain language of section 16600 and the California Supreme Court's decision in *Edwards v. Anderson*—placing further into question the viability of employee non-solicitation provisions.

California's notorious section 16600 may even reach non-parties to a contract, according to a California Superior Court. The court applied section 16600 to invalidate the "show cause order" provisions in the NCAA bylaws, endangering the NCAA's ability to enforce its rules by voiding one of its "go-to" sanctions. The court reasoned that the "show cause" penalty requiring NCAA member schools to demonstrate to the Committee why they should not be penalized for the rule violations of a sanctioned individual is essentially a "career-terminating sanction" that restricts the individual's ability to practice his profession nationwide.

Back in 2015, we covered the divided holding of the Ninth Circuit in *Golden v. California Emergency Physicians Medical Group*, that a "no re-hire" provision in a settlement agreement could constitute a restraint of trade in violation of California law. After a second round at the Ninth Circuit, the case has been reversed and remanded yet again, based on the panel majority's conclusion that the "no re-hire" provisions at issue were overbroad and unenforceable.

These decisions demonstrate the extent to which some California courts will go to invalidate restraints on employees and promote "open competition and employee mobility."

In contrast, a Delaware Chancery Court found that a non-compete provision may be enforced against a California executive because the employee was represented by counsel concerning the Delaware choice of law and forum selection provisions contained in the agreement.

6. Other Notable State Cases Regarding Restrictive Covenants

The **Wisconsin** Supreme Court in *Manitowoc Company v. Lanning*, 2018 WI 6 (2018), extended the reach of the state's highly restrictive non-compete statute to invalidate an employee non-solicitation clause, finding that the non-solicitation clause prevented the employee from soliciting any of the company's 13,000 employees worldwide, and therefore was essentially a non-compete subject to the state's strict statutory requirements.

In *Farm Bureau Life Insurance Co. v. Dolly*, 2018 S.D. 28 (2018), the **South Dakota** Supreme Court invalidated a life insurance agent's non-compete agreement because it did not meet the requirements set forth in South Dakota's state statute regarding non-competes.

In *Capistrant v. Lifetouch*, 916 N.W.2d 23 (2018), the **Minnesota** Supreme Court determined that the return of property provision at issue in the case was a condition precedent of the employee's receipt of post-employment payments, but remanded to the district court based on its adoption of "inequitable forfeiture."

The Northern District of **Illinois** applied the "janitor rule" in *Medix Staffing Solutions Inc. v. Dumrauf*, No. 1:2017cvo6648 (N.D. Ill. 2018), to invalidate a former sales director's non-compete agreement as overbroad and unenforceable.

Establishing a new cautionary tale of joint representation of employer and employee, a federal judge in **Kentucky** allowed claims for tortious interference with contract and aiding and abetting breach of fiduciary duty to proceed against the defendant law firm, based on allegations that the defendants told the plaintiff's former employees that they could make more money on their own and directed the employees to breach their contracts.

7. New State Legislation Regarding Restrictive Covenants

On July 31, 2018, the **Massachusetts** legislature finally passed a non-compete bill, which went into effect on October 1, 2018, and changed the landscape of non-compete enforcement in the state. The Massachusetts Noncompetition Agreement Act ("MNAA") imposes new restrictions on non-competes entered into on or after the effective date of the Act, governing everything from the length of permissible non-compete provisions to the enforceability of non-compete agreements. With this bill, Massachusetts also became the 49th state in the Union (with only New York lagging) to adopt a version of the Uniform Trade Secret Act. A more detailed discussion of the MNAA, and what it means for Massachusetts and other states that face increased difficulty in enforcing non-compete agreements, can be found here.

In March 2018, **Idaho** amended its non-compete law to put the burden of establishing irreparable harm back on employers—effectively nixing a previous amendment in 2016 entitling companies to a rebuttable presumption of irreparable harm upon a finding that the defendant-employee violated the non-compete.

In March 2018, **Utah** passed a new law modifying its Post-Employment Restricts Act to bar the enforcement of non-compete agreements for employees in the broadcasting industry who earn less than a set salary amount per year and where certain conditions are present.

In April 2018, **Colorado** passed an amendment to a law governing non-compete agreements for physicians, excluding physicians treating patients with "rare disorders" from the requirement to pay damages for joining a competitor.

Other states, including **New Jersey** and **Washington**, have proposed legislation curbing employers' ability to enforce non-compete agreements and other restrictive covenants. Although the proposed restrictions did not pass, such proposals reveal the continuing trend of limiting the availability and enforceability of restrictive covenants. **Vermont** recently proposed legislation as well to curb the use of non-compete agreements.

For a 50 state survey of non-compete laws, please see our recently updated: "50 State Desktop Reference: What Businesses Need To Know About Non-Compete and Trade Secrets Laws."

8. Federal Legislation Regarding Restrictive Covenants

On April 26, 2018, Democratic U.S. Senators Warren, Murphy, and Wyden introduced the "Workforce Mobility Act," which would prohibit the use of covenants not to compete, nationwide. The text of the bill provides, in pertinent part, that "No employer shall enter into, enforce, or threaten to enforce a covenant not to compete with any employee . . . who in any workweek is engaged in commerce or in the production of goods for commerce (or is employed in an enterprise engaged in commerce or in the production of goods for commerce)." However, the bill also states that "Nothing in this Act shall preclude an employer from entering into an agreement with an employee to not share any information (including after the employee is no longer employed by the employer) regarding the employer or the employment that is a trade secret, as defined in section 1839 of title 18, United States Code."

Florida Senator Marco Rubio recently introduced the "Freedom to Compete Act" (the "Act") proposing to amend the Fair Labor Standards Act (FLSA) of 1938 to ban non-competes for most non-exempt workers. The Act is broadly drafted to void any agreement that restricts "any work for another employer," "any work in a specified geographical area," and "any work for another employer that is similar" to the employee's prior work. While it purports to void only non-compete agreements, the bill's use of the sweeping language "any work" could be interpreted to ban not only non-compete agreements, but other post-employment restrictive covenants such as customer and employee non-solicitation agreements. Further, the Act (if passed) would purportedly apply retroactively to agreements entered into before its enactment.

9. New Trade Secrets Law for France

Continuing as one of the EU's first few members to protect trade secrets on a local front, France recently adopted loi n°2018-670, which offers companies protection for their economic and strategic information, implements the Directive 2016/943/EU, and puts French companies on a more equal footing with foreign competitors who already benefit from regulated business secrecy (e.g., U.S. and Chinese companies).

10. Blockchain Technology Intersecting with Trade Secrets

The rise in blockchain technology has created new challenges for trade secret disputes as courts struggle to apply existing trade secret law to new types of digital property and information. *Founder Starcoin v. Launch Labs, Inc.* was one of the

first trade secret decisions involving blockchain technology. There, the Southern District of California federal court denied the plaintiff's request for a preliminary injunction regarding the idea for cryptocollectible cats bearing the likeness of sports athletes and other celebrities. But the case's conceptual confusion around blockchain technologies—the attempt to draw a clear distinction between commodity/coin tokens and unique collectibles, where no such distinction really exists—is indicative of the danger cutting-edge companies may run into in trying to enforce (or even defend against) trade secret claims.

We will continue to provide up-to-the-minute information on the latest legal trends and cases in the U.S. and across the world, as well as important thought leadership and resource links and materials.

We recently kicked off the 2019 Trade Secrets Webinar Series with a program entitled "2018 National Year in Review: What You Need to Know About Recent Cases and Developments in Trade Secrets, Non-Competes and Computer Fraud," and you can find a recording of the webinar here. For anyone who may have missed any of the 2018 webinar programs on trade secret, computer fraud, and non-compete law, we have also compiled a list of the topics covered and takeaways for each program here.

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