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Management Alert

At Long Last, Non-Compete Legislation: Massachusetts Finally Passes Non-Compete Bill After Nearly a Decade

By Katherine Perrelli, Dawn Mertineit, and Erik Weibust

Late on July 31st, after close to a decade of "will they or won't they" nail biters, the Massachusetts legislature finally passed a non-compete bill, just minutes before the end of the 2018 legislative session. (For a recap of the many twists and turns over the years, here is just a smattering of blog posts on the topic).

The new bill, which will become effective on October 1, 2018, if signed by Governor Baker, codifies certain aspects of existing common law, but makes some significant changes to non-compete jurisprudence in the Bay State that employers will need to be mindful of.

*Note: this bill applies to both employees **and** independent contractors, despite the many fundamental differences between employees and independent contractors under Massachusetts law. For clarity purposes we will simply refer to "employees" in this post.*

Applicability to certain types of restrictive covenants

This bill applies to most non-compete agreements, including forfeiture-for-competition agreements (allowing an employee to compete, but requiring him or her to forfeit some benefit to which he or she would otherwise be entitled), but does *not* apply to other restrictive covenants agreements, such as customer or employee non-solicits, non-disclosure agreements, or anti-raiding agreements, nor does it apply to non-competes arising out of the sale of a business.

Duration

The bill limits the duration of a non-compete agreement to 12 months following the employee's departure, unless he or she has breached a fiduciary duty to the employer or engaged in misappropriation, in which case the duration can be up to 2 years following separation. This is a significant departure from existing law—common law decisions have regularly upheld non-competes of 2 years or even more in appropriate circumstances.

Of course, even though the bill allows a non-compete restriction beyond a year where an employee breaches a fiduciary duty or engages in misappropriation, one wonders how often courts will be willing to grant injunctions beyond the one-year period. Many of these disputes are "won" or "lost" at the motion for temporary restraining order and/or preliminary injunction stage, before extensive evidence has been heard by the court. Thus, a court may be reluctant to extend the restriction without the benefit of a full-blown evidentiary hearing on the alleged breach of fiduciary duty or misappropriation.

Requirements for agreements entered into at the commencement of employment

Agreements entered into at the commencement of employment must be signed by both the employer and employee, and expressly state that the employee has a right to consult counsel before signing the agreement. Additionally, the agreement must be provided with the formal offer letter, or at least 10 business days prior to the employee's first day, whichever is earlier.

Requirements for agreements entered into *after* the commencement of employment

In a significant change to current Massachusetts common law, continued employment will no longer be sufficient consideration for agreements entered into after an employee starts work. Instead, "fair and reasonable" consideration, independent of continued employment, must be provided by the employer. What will constitute "fair and reasonable" consideration will no doubt be influenced by case law from other jurisdictions where continued employment is not sufficient consideration, as well as those cases at the Superior Court level which have addressed this issue in the context of determining whether enforcement is equitable under the circumstances. Like agreements entered into prior to commencement of employment, employees must receive at least 10 business days' notice before the non-compete is effective, and the agreement must be in writing, signed by employer and employee, and expressly set forth the employee's right to consult with counsel.

Garden leave (or not)

Those readers who have been following the tortured path of non-compete reform will recall that the concept of garden leave was a major topic of discussion in past efforts to pass a non-compete bill, and was the major reason why legislation was not passed last year. This bill offers a somewhat watered down version of this concept by requiring the employer to pay 50% of the employee's annualized base salary during the restricted period, or some other "mutually agreed upon consideration," which must be specified in the agreement. Where employers opt to give garden leave, such payments may not be unilaterally discontinued by the employer, except where the employee has breached the agreement. However, this could raise difficult questions regarding when an employee is deemed to have breached, and we foresee many potential lawsuits or counterclaims for breach of contract by employees claiming that the termination of such payments was inappropriate.

Non-competes unenforceable against certain employees, including those laid off or terminated without cause and low-wage workers

In a nod to the furor over non-competes governing low-wage workers and certain other groups, this bill prohibits the use of such agreements for: (1) nonexempt employees under the Fair Labor Standards Act (see our analysis here of how this provision could be difficult to interpret, given that the FLSA's overtime exemptions are not always a model of clarity and can be a moving target); (2) undergrads and grad students working part-time; (3) employees 18 and younger; and (4) employees terminated without cause or laid off.

"Springing" non-competes

Notably, this bill allows a court to impose a non-compete as a penalty for an employee's breach of other enforceable restrictive covenants (such as non-solicit agreements) or statutory or common law duties. We view this as a fairly extraordinary remedy, and suspect that only very egregious conduct from employees will cause a court to consider it.

Choice of law

The bill prohibits employers from applying another state's law to an employee's non-compete agreement, provided the employee lived in Massachusetts for the last 30 days before cessation of his or her employment. This could be complicated for multi-jurisdictional employers who enter into non-compete agreements with non-Massachusetts residents if those employees subsequently move to Massachusetts following execution. It would seem that such employers would need to ensure that within 30 days of such a move, the employee's agreement is reviewed and/or renewed to ensure compliance with Massachusetts law.

Venue

All actions to enforce non-compete agreements must be initiated in the employee's home county or in Suffolk County (and if in Suffolk County, only in the Superior Court's Business Litigation Session). Notably absent from the bill is any mention of actions brought in federal court with pendant state law claims, or the ability to remove cases to federal court located in the employee's county.

Other requirements consistent with common law

As already contemplated in common law decisions, regardless of when the agreement was entered into, the bill requires that the agreement must be no broader than necessary to protect the employer's legitimate business interests (trade secrets, confidential information, or goodwill), and must be consonant with public policy.

Likewise, the agreement must be reasonable in temporal and geographic scope and the scope of activities prohibited. The bill provides that a geographic scope that is limited to the locations in which the employee provided services or had a material presence or influence in the last two years of his or her employment will be deemed presumptively valid, as will a provision limiting the scope of prohibited activities to those services provided by the employee during the last two years of employment.

Reformation

Similarly, consistent with existing law, the bill provides that courts may reform "or otherwise revise" overbroad or otherwise unenforceable non-compete agreements. Note that while some commenters have reported that the bill would allow courts to "blue pencil" an overbroad agreement, the passed bill does not reference "blue penciling," a doctrine that allows the court to revise an agreement only by excising grammatically severable language (i.e., under the "blue pencil" doctrine, courts could not add language to limit an agreement). While certainly a court can, by reforming the agreement, excise certain words and decline to add new language, references to the "blue pencil" doctrine are nonetheless somewhat misleading, because they imply that the court cannot add language to render an overbroad agreement enforceable.

UTSA adoption

Finally, with this bill, Massachusetts will become the 49th state in the Union (with only New York lagging) to adopt a version of the Uniform Trade Secret Act ("UTSA").

What now?

Businesses with employees in Massachusetts (or who move to Massachusetts) will need to carefully review their agreements with such employees to ensure compliance with this new bill (assuming of course that it is signed by Governor Baker). While

the bill is ***not*** retroactive, any agreements entered into on or after October 1, 2018, must comply with the new requirements. Even though agreements entered into before October 1, 2018, will not be subject to this bill, the prudent practice would be to review existing agreements for compliance with this law, and consider making changes to bring them into compliance.

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