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Recent Developments in Trade Secrets and Employee Mobility in the Workforce Webinar

Thursday, March 22, 2018

Presented by

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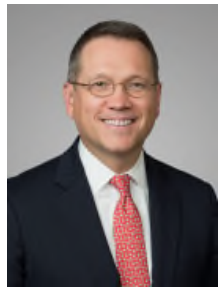

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Agenda

1. New and Proposed State and Federal Non-Compete Statutes
2. Significant New Non-Compete Cases
3. Using “Garden Leave” Clauses in Lieu of Non-Competes
4. Significant Recent Trade Secret Cases
5. Practical Impact of Federal Defend Trade Secrets Act (DTSA)
6. Practice Points and Case Developments Under the DTSA
7. Changes in Regulatory and Statutory Restrictions on Confidentiality Agreements

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New and Proposed State and Federal Non-Compete Statutes

New and Proposed State Non-Compete Statutes

Nevada A.B. No. 276, N.R.S. Ch. 613, as amended (effective June 3, 2017)

Nevada Law Requires Nevada Judges to "Blue Pencil" Non-Competes

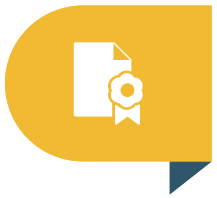
- **Statute provides**: Non-compete agreements are unenforceable unless the non-compete:
  - Is supported by "valuable consideration" (not defined);
  - does not impose any restraint that is greater than is required for the employer's protection;
  - does not impose any undue hardship on the employee; and
  - imposes restrictions that are appropriate relative to the valuable consideration.
- **Most importantly**: Requires judges to "blue pencil" overbroad non-competes to the extent necessary to render agreement enforceable.
- **Also note**: In RIFs, reorganizations, or restructurings, non-competes are only enforceable while the employer is paying the employee's salary, benefits, or equivalent (including severance).

New and Proposed State Non-Compete Statutes

Washington State H.B. 1967 (pending)

Washington State Proposes New Terms for Non-Compete Agreements

- **Legislation would require that:**



All terms of non-compete agreement be disclosed to prospective employees in writing no later than acceptance of employment offer

Employers provide independent consideration when non-compete agreement is extended after commencement of employment.

If an employer requires an employee to sign non-competes that it knows contains unenforceable provisions, the employee can recover actual damages, statutory damages of $5,000, and attorneys' fees.

New and Proposed State Non-Compete Statutes

Prohibition of Contracts in Restraint of Trade Act (proposed amendment to the Illinois Freedom to Work Act)

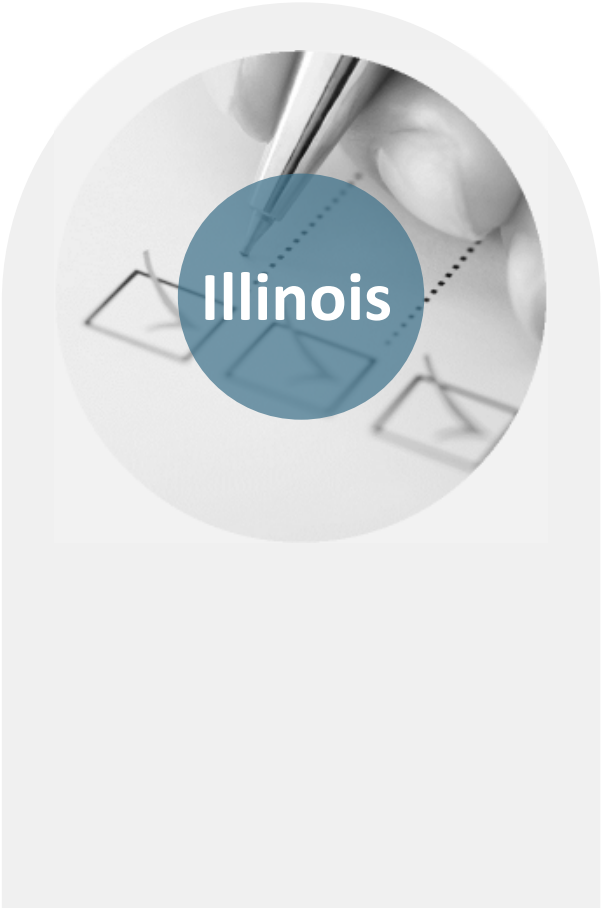
Illinois Governor Proposes to Abolish Non-Competes

Proposed legislation (supported by Republican Governor) would:

Void "any contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind."

Cover non-compete agreements signed by all employees that earn less than $1,000,000.

Provide an exception for sale of business.



Is Illinois the next California of non-competes?

Maybe.

(Hint: Does Illinois want to be Amazon's second HQ?)

More Proposals Banning Non-Competes for Low-Wage Workers and More

Legislation also has been proposed in:

- **Maryland** (H.B. 506): Voids non-competes with employees who make less than $15/hour or $31,200/year
- **New York**: Ban if under NYS salary threshold
- **New York City**: Ban for "low wage workers"

Two federal bills have been introduced:

- LADDER Act (H.R. 2873)
- MOVE Act (S. 1504)

And Massachusetts is still at it:

- Several bill versions introduced

Stay tuned!

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Significant New Non-Compete Cases

White v. Mederi Caretenders Visiting Servs. of Se. Fla., LLC

226 So.3d 774 (Fla. Sept. 14, 2017)

Facts: *Marketing reps in home health industry, whose primary roles were to cultivate relationships with referral sources, went to direct competitor in violation of non-competes.*

Issue: *Were their referral sources a protected legitimate business interest under Florida statute governing non-compete agreements, even though "referral sources" are not one of the five "business interests" listed in the statute?*

Florida S. Ct: *Yes*.

- The statutory list is non-exhaustive; courts must focus on the purpose of the statute:
  - "preventing unfair competition by protecting crucial business interests."
- But, the "determination of whether an activity qualifies . . . is inherently a factual inquiry, which is heavily industry- and context-specific."

NOTE: Result may be different in common law states:

- Under Mass. law, court found:
  - no legitimate interest in remembered information about identities and needs of clients; or
  - no protection for ordinary competition.
  - (*ABM Indus. Grps., LLC v. Palmarozzo*, 2017 WL 2292744 (Mass. Super. Mar. 30, 2017))

In re Document Technologies Litigation

2017 WL 2895945 (S.D.N.Y. July 5, 2017)

Indemnification ≠ Tortious Interference *(Preliminary Injunction Denied)*

- Four senior sales executives of plaintiff employer collectively left to join a competitor.
- New Employer agreed to indemnify them from claims of improper conduct and gave them significant signing bonuses to make up for lost compensation.
- ***Issue:*** Did employees and new employer cross any forbidden lines?
- ***Judge Rakoff:*** No, conduct **was not**:
  - **Unfair competition**: Employees marketing themselves as "package deal" is not unfair competition, since each had individually resolved to leave in advance of coming together.
  - **Breach of contract**: Accepting employment and engaging in preparatory meetings are permissible acts that do not violate the underlying non-compete agreement.
  - **Tortious interference**: Merely indemnifying new hires and providing signing bonuses is not tortious interference.

E.T. Products, LLC v. D.E. Miller Holdings, Inc.

872 F.3d 464 (7th Cir. 2017)

Broader Restrictions Allowed in Sale of Business Context

- Sellers of business signed non-compete agreements with buyers.
  - 5-year duration
  - All of North America as geographic scope
- ***Threshold issue:*** Were these overly broad and therefore unenforceable under Indiana law?
- ***7th Circuit:*** No, not in the sale-of-business context.
  - Relatively equal bargaining power
  - Necessary to protect purchased goodwill
  - Buyer had plans to expand throughout North America at time of purchase
- ***Ultimate issue:*** Is a manufacturer's distributor the manufacturer's competitor, and did the sellers therefore violate their non-compete?
- ***7th Circuit:*** No. The distributor is not in the same business as manufacturer under the terms of the non-compete.

Acclaim Sys., Inc. v. Infosys, Ltd.

679 F. App'x. 207 (3rd Cir. 2017)

No Tortious Interference Based on Common Industry Practice

Defendant contracted to work with four IT consultants, who each stated that they had no pre-existing non-competes.

Issue: Under PA law, can a defendant without actual knowledge of a non-compete have the necessary specific intent for a tortious interference claim?

Third Circuit: No.

- Although restrictive covenants are "common policy" in the IT consulting industry, they are not so universal that defendant can be presumed to have knowledge.
- No "willful blindness" here.

Ag Spectrum Co. v. Elder

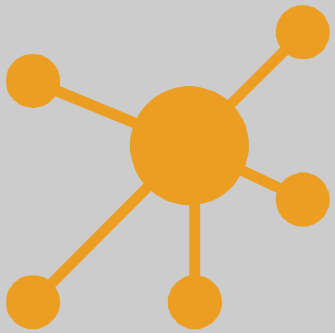
865 F.3d 1088 (8th Cir. 2017)

Non-Competes with Independent Contractors May Be OK

- Independent contractor agreement barred competition for three years following termination of agreement.
- ***Issue:*** Under Iowa law, was the agreement enforceable?
- ***Eighth Circuit:*** **No.**
  - Non-competes binding independent contractors are not per se unenforceable.
  - But here the non-compete agreement was unreasonable because:
    - not necessary to protect plaintiff's business;
    - defendant provided his own professional contacts as an independent contractor; and
    - provision burdened defendant disproportionately to the plaintiff's benefit.
  - Court held that Defendant's "business activity fosters fair competition in the marketplace, not unjust enrichment."
- ***The moral of the story:*** Never lose sight of judicial distaste for non-competes!

Bankers Life & Cas. Co. v. Am. Senior Benefits LLC

83 N.E.3d 1085 (Ill. App. 2017)



- Employee who was contractually barred from soliciting former co-workers sent three former co-workers generic requests to become "connections" on LinkedIn.
- ***Issue:*** Did this cross the line from mere passive social media activity (generally okay) to an unlawful solicitation?
- ***Ill. Ct. of Appeals:*** **No.**
  - This was not a direct or active effort to recruit former co-workers.
  - Why not? No mention of new employer, no suggestion that they view his new job description, and no encouragement to leave.
  - Court evaluated the content of the activity, not the medium by which the employee participated in the activity.
- ***Takeaway:*** Close call. Active social media activity that is more focused and deliberate can violate non-solicitation agreements.

Manitowoc Co. v. Lanning

2018 Wisc. LEXIS 12

- Circuit Court, after bench trial, awarded over $100,000 against former employee who violated non-solicitation of employees provision in employment agreement.
  - Court of Appeals reversed on grounds that non-solicitation of employees provision is unenforceable under Wisconsin statute (Wisc. Stat. §103.465) prohibiting "covenants not to compete" that constitute a restraint of trade.
- ***Issue:*** Does Wisc. Stat. § 103.465 apply to non-solicitation of employees provisions and, if so, does it render such provisions unenforceable?
- ***Wisc. Supreme Court:*** Yes and Yes
  - The application of the statute does not rely on how the provision is framed or labeled, but depends on whether its effect is an unreasonable restraint on employees and competition.
  - The non-solicitation of employees provision restricts the ability of the employee and his new employer to compete fully in the labor pool, as the employees from the former employer (Manitowoc) would be off-limits.
- ***Takeaway:*** Wisconsin's statute prohibiting non-competes that restrain competition should be interpreted broadly, beyond its effect on the immediate employee.

Choice of Law and Forum Selection Clauses Matter – *Sometimes*!

Consol. Infrastructure Grp., Inc. v. USIC, LLC, 2017 WL 2222917 (D. Neb. May 18, 2017)

- Indiana employer
- Non-competes with six employees (three lived or worked in Nebraska)
- Nebraska hostile to non-competes

- Indiana choice of law and forum
- Employees sought declaratory judgment in Nebraska federal court
- Employer sued in Indiana and moved to transfer Nebraska case to Indiana.

Result?? Nebraska federal court honored forum selection and granted transfer motion

Oxford Global Resources, LLC v. Hernandez, 2017 WL 2623137 (Mass. Super. June 9, 2017)

- Massachusetts employer
- Former employee lived and worked in California
- California law is hostile to non-competes

- Massachusetts choice of law and forum
- Employer sued in Massachusetts

***Result??* Massachusetts state court found that choice of law was adhesory**

- **Forum selection violated California public policy**

Cautionary Tales From Other Recent Non-Compete Cases

SpaceAge Consulting Corp. v. Vizconde
2017 WL 4183281
(N.J. Super. Sept. 22, 2017)

Non-compete unenforceable

- Employer violated wage and hour laws by failing to pay employee properly during training period
- Agreement void and unenforceable

Mid-America Bus. Sys. v. Sanderson
2017 WL 4480107
(D. Minn. Oct. 6, 2017)

Court denies TRO request

- Agreement signed after commencement of employment lacked adequate consideration
- Need more than continued employment

Lifebrite Labs, LLC v. Cooksey
2016 WL 7840217
(N.D. Ga. Dec. 9, 2016)

Court defines blue pencil limits under Georgia statute

- Ability to "modify" overbroad provisions is limited to striking offending provisions
- Court cannot rewrite contracts by supplying new terms

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Using "Garden Leave" Clauses in Lieu of Non-Competes

Using “Garden Leave” as an Alternative to Traditional Non-Competes

- Law not well-developed, but garden leave generally faces less judicial hostility
- Typically 30-90 days – most crucial period for most employers
- Most commonly used in financial services industry
- **Bottom Line:**
  - Garden leave clauses are far more likely to be respected than non-competes because of shorter duration and seen as less punitive

Advantages and Drawbacks of Garden Leave Provisions

PROS

- Anticipated greater receptivity by courts
- Added protections for the employer during the garden leave period
- Orderly transition of client relationships and work responsibility
- Decreased likelihood of overuse when not necessary to protect legitimate interests
- Flexibility

CONS

- Higher cost to employer
- Short duration of garden leave (30-90 days) compared to non-compete agreements (12-18 months)
- Lack of case law and judicial guidance
- Logistical issues regarding electronic access during garden leave if employee is needed during that time

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Significant New Trade Secret Cases

Sentinel Ins. Co. v. Yorktown Indus.

2017 WL 446044 (N.D. Ill. Feb. 2, 2017)

Insurance Coverage for Trade Secret Theft?

- Sentinel Insurance Co. issued Yorktown Industries a policy covering "personal and advertising injury."
- "Advertising injury" defined as "copying in your 'advertisement' or on 'your web site,' a person's or organization's 'advertising idea' or style of 'advertisement.'"
- Yorktown was sued for trade secret theft.
- Yorktown sought coverage under the policy, arguing that the trade secrets claim counted as "stealing someone's advertising idea."
- Sentinel filed a declaratory judgment action and won:
  - Court ruled that the alleged trade secret misappropriation was not an "advertising injury" covered under the policy.
- ***Takeaway:***
  - Review insurance policies and notify carriers for potential coverage of any adverse claim.
  - Depending on the allegations and policy language, insurance coverage may exist.

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Defend Trade Secrets Act (DTSA)

Practice Points and Case Developments

The Federal Defend Trade Secrets Act (DTSA)

Practical Impact

Grants
Federal court jurisdiction for all trade secret misappropriation cases

Requires
Modification of employee agreements governing "confidentiality"

Impacts
New York and Massachusetts most substantively

Lacks
Penalty for violations of notice of immunity requirement

The Federal Defend Trade Secrets Act (DTSA)

Practice Points and Case Developments

Pleading Requirements

- Under the now well-known *Twombly/ Iqbal* standard, applicable on motions to dismiss under Fed. R. Civ. P. 12(b)(6), DTSA plaintiffs must adequately allege, among other requirements, improper acquisition and/or improper disclosure or use of a trade secret, and must do so through more than conclusory allegations or labels.

Prominence Advisors, Inc. v. Dalton

2017 U.S. Dist. LEXIS 207617 (N.D. Ill. Dec. 18, 2017): (dismissing the DTSA count because the Complaint did not, among other things, "include any facts to support [Plaintiff's] bald allegation that [Defendant] disclosed the Confidential Information without authorization or consent.").

The Federal Defend Trade Secrets Act (DTSA)

Practice Points and Case Developments

Pleading Requirements

- DTSA plaintiffs must also adequately allege that they took reasonable steps to maintain the secrecy of protected information.

Compare

Raben Tire Co. v. Dennis McFarland
2017 WL 741569 (W.D. Ky. Feb 24, 2017):

- Rule 12(b)(6) motion granted *with prejudice.*
- Plaintiff failed to allege that employees were required to sign confidentiality agreements or any other indicia of reasonable steps to maintain secrecy.

Aggreko, LLC v. Barreto,
2017 WL 963170 (D. N. Dak. Mar. 13, 2017):

- Rule 12(b)(6) motion denied.
- Plaintiff alleged that it required employees to sign confidentiality agreement and that information was not disseminated outside the workplace.

The Federal Defend Trade Secrets Act (DTSA)

Practice Points and Case Developments

Ex Parte Seizure Orders

Seizure orders are only appropriate in extreme circumstances.

- ***OOO Brunswick Rail Mgmt. v. Sultanov***, 2017 WL 67119 (N.D. Cal. Jan. 6, 2017): "A court may issue a seizure order only if, among other requirements, an order under Fed. R. Civ. P. 65 or another form of equitable relief would be inadequate."

Traditional Rule 65 TROs are still the preferred means of ordering seizure of property in DTSA cases.

- ***Magnesita Refractories Co. v. Mishra***, 2017 WL 655860 (N.D. Ind. Jan. 25, 2017): "Obviously, in this case, Rule 65 did the trick."

The Federal Defend Trade Secrets Act (DTSA)

Practice Points and Case Developments

Timing Defense

- Defendants may have a "timing defense" when the alleged misappropriation occurred before the DTSA's enactment (May 11, 2016), or there is no indication as to when the alleged misappropriation occurred.
  - ***Cave Consulting Grp., Inc. v. Truven Health Analytics Inc.*** 2017 WL 1436044 (N.D. Cal. Apr. 24, 2017):

    "Without facts about when post-enactment use occurred and whether the information disclosed was new or somehow different from the prior misappropriation, plaintiff has failed to state a claim under the DTSA."

- No timing defense when plaintiff can show that misappropriation continued to (or indefinitely will) occur after the statute's enactment.
  - ***Brand Energy & Infrastructure Serv. v. Irex Contracting Grp.*** 2017 WL 1105648 (E.D. Pa. Mar. 23, 2017):
    - Plaintiff allowed to pursue DTSA claim because amended complaint alleged multiple uses of trade secrets that occurred after the DTSA was enacted.

Regulatory and Statutory Restrictions on Confidentiality Agreements

- ✓ SEC
- ✓ FINRA
- ✓ OSHA
- ✓ NLRB
- ✓ EEOC
- ✓ DTSA

Required whistleblower carve-outs

Sharing of compensation information

Required DTSA notice of immunity disclosure

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Questions?

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