RISKY BUSINESS

NO-POACH, NON-COMPETES, AND OTHER ANTICOMPETITIVE EMPLOYMENT PRACTICES ARE "OLD-TIME" ROCK AND ROLL

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"Don't steal anything. If I come back here and anything's missing I am going straight to the police."

Tom Cruise as Joel Goodson in Risky Business

No one wants their most valuable assets taken. For businesses, those assets often include employees, customers, and trade secrets. But employers who try to protect these assets are on notice: anticompetitive agreements related to employment are subject to scrutiny and may result in fines or even criminal charges.

In October 2016, the DOJ and FTC took the extraordinary step of issuing guidelines putting HR professionals on notice that certain practices – including no-poaching agreements – could expose employers to both civil liability and criminal penalties (the "2016 Guidelines").[1] Similar legislative agendas are popping up. After one recent study reported that 58% of major fast food franchise agreements include restrictions on the recruitment and hiring of workers currently employed by other units affiliated with the franchisor,[2] a group of U.S. Senators penned a letter to 89 franchise CEOs requesting they discontinue allegedly collusive no-poaching agreements that prohibit franchisees from hiring workers employed by an-

"58% of major fast food franchise agreements include restrictions on the recruitment and hiring of workers currently employed by other units affiliated with the franchisor."

[1] DOJ: Antitrust Division and FTC, Antitrust Guidance for Human Resource Professionals (Oct. 20, 2016) [hereinafter 2016 Guidelines] (available at https://www.ftc.gov/system/files/documents/public_statements/992623/ftc-doj_hr_guidance_final_10-20-16.pdf) (last visited April 12, 2019).

[2] Filippo Balestrieri, Federico G. Mantovanelli & Shannon Seitz, The Department of Justice and Federal Trade Commission Guidance for Human Resources Professionals and Recent Comments by Enforcement Officials Related to No-Poaching Agreements, Analysis Group Inc. (Feb. 1, 2018) (available at http://www.analysisgroup.com/uploadedfiles/content/insights/publishing/no-poaching-agreements-guidance_aba_spring_18.pdf) (last visited April 12, 2019).

other franchisee.[3] Fast food no-poach agreements were in the spotlight again this month when the DOJ and Washington State Attorney General ("Washington AG") submitted amicus briefs in three class actions challenging the provisions.[4] While the DOJ has advocated for a rule of reason analysis of no-poach provisions in franchise agreements, the Washington AG is more skeptical, arguing that no-poach provisions in Washington franchise agreements may merit a per se approach.

There has been only one publicly-announced enforcement action since the 2016 Guidelines were released (a civil action discussed below), but antitrust agencies have warned that enforcement will escalate to include criminal charges in the future. Other forms of government enforcement against similar clauses, such as non-competes and non-disclosure agreements, may very well follow.

October 2016 Guidelines:

Criminal & Civil Enforcement for Employment Agreements

The October 2016 guidelines focus on no-poaching and wage fixing agreements, cautioning that "[a]n individual likely is breaking the antitrust laws if he or she [1] agrees with individual(s) at another company about employee salary or other terms of compensation, either at a specific level or within a range (so-called wage-fixing agreements), or [2] agrees with individual(s) at another company to refuse to solicit or hire that other company's employees (so-called 'no poaching' agreements)."[5] Illegal no-poaching agreements have resulted in consent decrees, and

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[3] Sheila Raftery Wiggins, No-Poach Agreements Are Targeted by Government, Employees and Legislators, N.J. L. J. (Aug. 16, 2018) (available at https://www.law.com/njlawjournal/2018/08/16/no-poach-agreements-are-targeted-by-government-employees-and-legislators/) (last visited April 12, 2019).

[4] Jon Jacobs & Thomas Boeder, Debating DOJ And Wash. Attorney General No-Poach Briefs, Law360 (March 15, 2019) (available at https://www.law360.com/classaction/articles/1139537/debating-doj-and-wash-attorney-general-no-poach-briefs) (last visited April 12, 2019). As Deputy Assistant Attorney General Michael Murray has commented, the DOJ is "making an active amicus program a priority." Michael Murray, Antitrust Enforcement in Labor Markets: The Department of Justice's Efforts, Prepared Remarks at Santa Clara University School of Law (March 1, 2019) (available at https://www.justice.gov/opa/speech/file/1142111/download) (last visited April 12, 2019).

[5] 2016 Guidelines, supra, at 3. (at 3).

going forward, so-called "naked" no-poaching and wage fixing agreements may result in criminal proceedings including prison time and fines.[6]

While some have called the "decision to treat no-poach and wage-fixing agreements as 'hardcore' criminal cartel conduct" a "remarkable … deviation from an exhibited reticence to expand the per se category beyond practices condemned by legal precedent as inherently anti-competitive," the DOJ has not wavered.[7] Assistant Attorney General Makan Delrahim has warned that criminal charges, including against parties to civil settlements with the Antitrust Division that have failed to honor the terms, are a real possibility.[8] And in addition to treble damages for civil violations, criminal penalties are heavy: up to a decade behind bars and fines of up to $100 million for corporations and $1 million for individuals, plus double the gross loss or gain caused by the poaching or wage-fixing.[9]

"Antitrust enforcers have confirmed that 'naked' wage-fixing and no-poaching agreements are per se illegal, precluding any further inquiry into competitive effects."

The No-Poach Analysis: Per Se or Rule of Reason?

Antitrust enforcers have confirmed that "naked" wage-fixing and no-poaching agreements are per se illegal, precluding any further inquiry into competitive effects.[10] "Naked" agreements are "among employers, whether entered into directly or through a third-party intermediary, [which are] separate from or not reasonably necessary to a larger legitimate collaboration be-

[6] 2016 Guidelines, supra, at 4.

[7] Dina Hoffer & Elizabeth Prewitt, To hire or not to hire: U.S. cartel enforcement targeting employment practices, Concurrences No. 3-2018, 79 (2018).

[8] Juan Arteaga, *Prepare For DOJ's Criminal No-Poach Prosecutions*, Law360 (Feb. 5, 2018) (*available at* https://www.law360.com/articles/1009025/prepare-for-doj-s-criminal-no-poach-prosecutions) (last visited April 12, 2019).

[9] *Id.*

[10] 2016 Guidelines, supra, at 3. (3)

tween the employers…."[11] This development marks a shift: "the same level of antitrust protection" is now extended "to individuals and employees as to products… ."[12]

No-poaching or wage-fixing agreements are not per se illegal, on the other hand, if they are separate from, or reasonably necessary to, a larger legitimate collaboration between the employers. "Legitimate joint ventures (including, for example, appropriate shared use of facilities) are not considered per se illegal under the antitrust laws."[13] Rather, these non-naked agreements will be subject to "rule of reason" analysis weighing pro-competitive against anticompetitive effects, rather than per se treatment. For example, pre-Guidelines, the court in *Eichorn v. AT&T Corp,* 248 F.3d 131, 146, (3d Cir. 2001) held that agreements between competitors were not an unreasonable restraint of trade in violation of antitrust laws if they were "reasonable in duration and geographical limitation," were entered into in conjunction with a legitimate collaboration, such as a "termination of employment or sale of a business," and went no further than necessary to effectuate that legitimate collaboration (i.e. "to ensure successful transition of ownership").

This begs a question: what activities can be considered "legitimate"? A limited-scope joint venture between companies with a restricted pool of employees may be a legitimate collaboration pursuant to which sufficiently narrow no-poaching or non-solicitation agreements could be lawful under the federal antitrust laws (but see below re state laws). On the other hand, an employer seeking to prevent an employee from moving to a competitor soon after hire is likely not a legitimate justification to enter a reciprocal no-hire agreement with competitors. Likewise, a no-poach provision of a Letter of Intent ("LOI") to enter into a merger or acquisition may be intended to protect a company from losing valued employees if the merger falls through, yet not considered a legitimate collaboration under antitrust law. Employers should be cautioned that-

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[11] *Id.*

[12] Jaimie Chen, "No-Poach" Agreements as Sherman Act § 1 Violations: How We Got Here and Where We're Going, 28:1 J. OF ANTITRUST, UNFAIR COMPETITION, AND PRIVACY L. SECTION OF THE CAL. LAW. ASS'N 82, 93 (2018).

[13] 2016 Guidelines, *supra*, at 3.

LOIs produced in a Hart-Scott-Rodino Act merger approval filing may alert the federal agencies to civil or criminal issues.[14]

The High-Tech case

In *High-Tech Emp. Antitrust Litig.,* 856 F.Supp.2d at 1123, a case cited by the October 2016 guidelines and which culminated in a consent decree, the Ninth Circuit found "[p]laintiffs have alleged 'an example of the type of injury the antitrust laws are meant to protect'" based upon allegations "that their salary and mobility were suppressed by Defendants' agreements not to cold call." Among other things, the court in *High-Tech* took issue with the fact that each list of employees to not be called was "not limited by geography, job function, product group, or time period; and was not related to a collaboration between that pair of Defendants." *Id*. at 1111. But even no-poach agreements that do contain those limitations may be subject to antitrust scrutiny. To wit, California Business & Professions Code section 16600 "provides that, other than certain statutory exceptions… 'every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void.'" *Gatan, Inc. v. Nion Co.,* 2016 U.S.Dist. LEXIS 42764, at *6 (N.D. Cal. Mar. 30, 2016). Similarly, the Northern District of California has adopted the holding of *AMN Healthcare, Inc. v. Aya Healthcare Servs., Inc.,* 28 Cal. App. 5th 923 (2018) to find that section 16600 invalidated a non-solicit provision. *Barker v. Insight Glob., LLC,* 2019 U.S. Dist. LEXIS 6523, at *8-9 (N.D. Cal. Jan. 11, 2019).

The Air Brakes case

On April 3, 2018 the Antitrust Division brought its first post-2016 Guidelines case. DOJ maintained that alleged naked no-poaching agreements by Knorr-Bremse AG and Westinghouse Air Brake Technologies Corp. constituted per se violations of Section 1 of the Sherman Act. [15]

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[14] Locke Lord Publications, *Locke Lord Quick Study: No-Poach, No-Solicit Provisions of Corporate Agreements Now Face Criminal Prosecution* (May 1, 2018) (*available at* https://www.lockelord.com/newsandevents/publications/2018/05/corporate-agreements-face-criminal-prosecution) (last visited April 12, 2019).

[15] Division Update Spring 2018, DOJ, *No More No-Poach: The Antitrust Division Continues to Investigate and Prosecute "No-Poach" and Wage-Fixing Agreements* (April 10, 2018) (*available at* https://www.justice.gov/atr/division-operations/division-update-spring-2018/antitrust-division-continues-investigate-and-prosecute-no-poach-and-wage-fixing-agreements) (last visited April 12, 2019).

According to the Competitive Impact Statement, the parties "entered into a series of agreements not to solicit, recruit, hire without prior approval, or otherwise compete for employees ... [which] were not reasonably necessary to any separate, legitimate business transaction or collaboration between the companies." *U.S. v. Knorr-Bremse AG and Westinghouse Air Brake Tech. Corp.*, No. 1:18-cv-00747 (D.D.C. April 3, 2018) (Competitive Impact Statement, Dkt. No. 3, pp. 1-2). That case is still pending.

Private Class Cases

Private class cases have predictably attracted the DOJ's interest as well; the DOJ has filed Statements of Interest in a suit involving an agreement between Duke and UNC to not poach each other's medical school professors, as well as in the civil follow-on counterpart to its investigation of the Knorr-Bremse AG and Westinghouse Air Brake Technologies Corp. railway industry no-poach agreements.[16] [17]

Non-Compete Clauses: State Law Leading the Way

The October 2016 Guidelines do "not address the legality of specific terms contained in contracts between an employer and an employee, including non-compete clauses." Non-compete clauses ("non-competes") generally require employees to refrain from engaging in a similar business, often during a specified time frame and/or within the same specified geographic area as the employer. But if the FTC and DOJ take their cues from the states, federal enforcement of restrictive employment practices could expand beyond no-poach to other types of arrangements like non-competes.

One example is California code section 16600. In *Golden v. Cal. Emergency Physicians Med. Grp.,* 782 F.3d 1083, 1085 (9th Cir. 2015) a doctor settling with his former staffing consor-

[16] Boris Bershteyn, Karen Hoffman Lent, Tara Reinhart & Zachary Siegler, *DOJ Is Trying To Rein In Franchise No-Poach Suits*, Law360 (Feb. 5, 2018) (*available at* https://www.law360.com/foodbeverage/articles/1130056/doj-is-trying-to-rein-in-franchise-no-poach-suits) (last visited April 12, 2019).

[17] Chen, *supra*, at 96-97. Though the government has not yet become involved, it is worthwhile to note that another recent private class case involving a no-poach agreement between Samsung and LG, *Frost v. LG Elecs. Inc.*, No. 16-cv-05206-BLF, 2018 U.S. Dist. LEXIS 204502 (N.D. Cal. June 22, 2018), was dismissed and is on appeal before the Ninth Circuit.

tium agreed "to waive any and all rights to employment with [the staffing consortium] or at any facility that [the staffing consortium] may own or with which it may contract in the future." The district court order enforcing the settlement was appealed, and the Ninth Circuit found that section 16600 "does not specifically target covenants not to compete between employees and their employers." Rather, it voids "'*every* contract' that 'restrain[s]' someone 'from engaging in a lawful profession, trade, or business'." *Id*. at 1090 (citation omitted). The Ninth Circuit's analysis suggests that other forms of anticompetitive employment agreements, such as no-poaching and non-solicit agreements, could also fall within section 16600's ambit. *Id*. at 1090.

In Nevada, Nev. Rev. Stat. 613.195, codified in 2017, states that "[a] noncompetition covenant is void and unenforceable unless the noncompetition covenant:

(a) Is supported by valuable consideration;

(b) Does not impose any restraint that is greater than is required for the protection of the employer for whose benefit the restraint is imposed;

(c) Does not impose any undue hardship on the employee; and

(d) Imposes restrictions that are appropriate in relation to the valuable consideration supporting the noncompetition covenant."

In contrast to California's section 16600, Nevada's requirements explicitly allow noncompetes to limit the former employee's practice in terms of "time, geographical area and scope of activity," unless the termination of the employment is due to "a reduction of force, reorganization or similar restructuring of the employer," in which case the noncompete "is only enforceable during the period in which the employer is paying the employee's salary, benefits or equivalent compensation, including, without limitation, severance pay." Nev. Rev. Stat. Ann. § 613.195. The new law allows a court to greenlight a noncompete that may otherwise be found unreasonable in its "limitations as to time, geographical area or scope of activity." *Id*.

In Arizona, the Supreme Court rejected a Court of Appeal's attempt to rescue a non-compete, deciding that while courts may "[ignore] severable portions of a covenant to make it more

reasonable, [the Arizona Supreme Court] will not permit courts to add terms or rewrite provisions." *Valley Med. Specialists v. Farber*, 194 Ariz. 363, 372 (1999). This seminal case was a departure from the usual judicial reasoning on non-competes, in which the hardship imposed upon the departing employee would weigh against upholding the clause. *Id*. at 368. Here, the court shifted its focus to public policy concerns instead, noting "[b]alancing these competing interests [e.g. the right to work, right to contract, and public's right to competition] is no easy task and no exact formula can be used." *Id*. at 369. The Arizona standard reflects broadened scrutiny of non-competes and dovetails with antitrust concerns about injury to competition: "The burden is on the party wishing to enforce the covenant to demonstrate that the restraint is no greater than necessary to protect the employer's legitimate interest, and that such interest is not outweighed by the hardship to the employee and the likely injury to the public." *Id*. at 372.

In Washington, on the other hand, non-competes remain enforceable after the State Legislature failed to enact two bills earlier this year: House Bill 2903 would have prohibited non-competes for certain jobs, while Senate Bill 6526 "would have largely imitated California's extremely restrictive non-compete laws."[18] Non-competes are generally found reasonable and enforceable in Washington so long as three questions are asked and satisfactorily answered: "(1) whether restraint is necessary for the protection of the business or goodwill of the employer, (2) whether it imposes upon the employee any greater restraint than is reasonably necessary to secure the employer's business or goodwill, and (3) whether the degree of injury to the public is such loss of the service and skill of the employee as to warrant nonenforcement of the covenant." *Knight v. McDaniel*, 37 Wash. App. 366, 369, 680 P.2d 448, 452 (1984). Note, however, that even if these conditions are met, a non-compete may still be found unenforceable for lack of consideration. *See Labriola v. Pollard Grp., Inc.,* 152 Wash. 2d 828, 838 (2004) (invalidating a non-compete where employee who signed the non-compete "was already employed for five

[18] Dawn Mertineit & Dallin Wilson, *Washington State's Legislature Rains on Non-Compete Critics' Parade Yet Again*, Seyfarth Shaw LLP (Feb. 22, 2018) (*available at* https://www.tradesecretslaw.com/2018/02/articles/noncompete-enforceability/washington-states-legislature-rains-on-non-compete-critics-parade-yet-again/) (last visited April 12, 2019).

years and received no additional benefits than what he was entitled to under" the initial employment agreement).

Even in the strictest states, some derivative forms of non-competes can be upheld. For example, courts recognize that employee mobility can threaten fair competition among employers if a departing employee takes protected information to a former employer's competitor.[19]

The California Uniform Trade Secrets Act defines a trade secret as "information, including a formula, pattern, compilation, program, device, method, technique, or process, that:

"Courts recognize that employee mobility can threaten fair competition among employers if a departed employee takes protected information to a former employer's competitor."

(1) Derives independent economic value, actual or potential, from not being generally known to the public or to other persons who can obtain economic value from its disclosure or use; and

(2) Is the subject of efforts that are reasonable under the circumstances to maintain its secrecy." Cal. Civ. Code § 3426.1(d).

While California has codified exceptions to section 16000 under narrow circumstances, such as the sale or dissolution of certain businesses,[20] courts recognize the additional "'trade secret exception' to Section 16600, pursuant to which a non-compete or non-solicitation clause may be valid under Section 16600 if it is necessary to protect a trade secret." *Richmond Techs., Inc. v. Aumtech Bus. Sols.*, No. 11-CV-02460-LHK, 2011 U.S. Dist. LEXIS 71269, at *59-60 (N.D. Cal. July 1, 2011).

But relying on trade secret clauses to rescue an otherwise invalid non-compete is aggressive. In *Gatan* (*supra*) the Plaintiff manufacturer's contract with the defendant included a clause prohibiting resale. Discussing the trade secret exception to the California statute, the Ninth Cir-

[19] See, e.g., *Jones Printing, LLC v. Adams Litho. Co.*, 2017 U.S. Dist. LEXIS 99754, at *5 (E.D. Tenn. June 28, 2017) (citing trade secrets as type of information filed under seal, in matter involving trade secret information allegedly conveyed by former employees to new employer-competitor).

[20] Cal. Bus. & Prof. Code § 16601.

cuit reasoned that "'[u]nder California law, non-competition agreements are unenforceable unless necessary to protect an employer's trade secret,' and a court in this district has further observed that, because section 16600 has not been limited to the employer/employee context, there is no reason to similarly limit the trade secret exception." *Id*. at *6 (citations omitted). Ultimately, the Court found the non-compete provision was void under 16600 because it was unnecessary to protect Gatan's trade secrets. *Id*. at *9. With so many states narrowing the scope of acceptable non-competes, increased federal scrutiny seems inevitable, particularly in the wake of the October 2016 Guidelines.F.[21]

A less risky approach is to use trade secret statutes in *lieu* of non-compete arrangements to enjoin a former employee's efforts with a competitor on trade secret grounds. The federal Defense of Trade Secrets Act (18 U.S.C. § 1831, *et seq*.) states that "a court may grant an injunction to prevent any actual or threatened misappropriation" of a trade secret related to a product or service used in, or intended for, interstate or foreign commerce, as long as the injunction does not "prevent a person from entering into an employment relationship, and that conditions placed on such employment shall be based on evidence of threatened misappropriation and not merely on the information the person knows; or otherwise conflict with an applicable State law prohibiting restraints on the practice of a lawful profession, trade, or business." 18 U.S.C. § 1836(b)(3)(A)(i)(I).

Non-disclosure agreements ("NDAs") and other provisions prohibiting the dissemination of trade secrets and other confidential or proprietary information by an employee are another alternative to non-competes. *See Richmond Techs., Inc. v. Aumtech Bus. Sols.*, No. 11-CV-02460-LHK, 2011 U.S. Dist. LEXIS 71269. But, as always, take care in California: employers claiming inevitable disclosure by the former employee face an uphill battle there, given that "under California, law, the theory of inevitable disclosure does not supply the proof needed to establish a

[21] In 2017, the FTC formed the Economic Liberty Task Force ("ELTF"), which has examined occupational license portability and complements the policies embodied by the in the October 2016 guidelines. Policy Perspectives Options to Enhance Occupational License Portability, FTC (Sept. 2018) (*available at* https://www.ftc.gov/system/files/documents/reports/options-enhance-occupational-license-portability/license_portability_policy_paper.pdf) (last visited April 12, 2019). While non-competes have not been explicitly targeted by the ELTF, broad concerns about worker mobility may predict future FTC enforcement against non-competes on antitrust grounds.

probability of success on the merits." *Bayer Corp. v. Roche Molecular Sys.,* 72 F. Supp. 2d 1111, 1112 (N.D. Cal. 1999).

Conclusion

Enhanced scrutiny of potentially anticompetitive employment practices — and the diminished likelihood that traditional exceptions to anticompetitive employment agreements will rescue employers — means that employers must diligently monitor the language of all employment agreements and competitor communications about the labor force. Internal auditing may reveal opportunities for an employer to seek training and/or outside counsel to avoid pitfalls.

Likewise, outside counsel should include employment agreements in the suite of dangers addressed by antitrust compliance programs and seek the advice of antitrust specialists when in doubt.

Anything less is risky business.

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