June 11, 2019

LAW BUSINESS TECHNOLOGY
BUSINESS TECHNOLOGY LAW
TECHNOLOGY LAW BUSINESS
THE RECORDER
daily at www.therecorder.com
An ALM Publication

Employee Nonsolicitation Clauses Are Not Enforceable in California

By Cheryl Cauley

Recognizing that noncompete provisions are invalid under California law, employers in California have long used employee nonsolicitation provisions in their employment agreements as an alternative strategy to limit competition for employees. Now, courts are making clear that this work-around is unacceptable, and that employee nonsolicitation clauses are impermissible in California.

Under California Business & Professions Code Section 16600, "every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void." "Section 16600 expresses California's strong public policy of protecting the right of its citizens to pursue any lawful employment and enterprise of their choice," see *Dowell v. Biosense Webster*, 179 Cal. App. 4th 564, 575 (2009). California courts have consistently confirmed that Section 16600 "evinces a settled legislative policy in favor of open competition and employee mobility," as in *Edwards v. Arthur* Andersen, 44 Cal. 4th 937, 946 (2008).

With that strong public policy as a guide, California courts have explicitly held that noncompetition provisions, which prohibit former employees from working at a competitor for some period of time, violate Section 16600 because they impede employee mobility. As a result, California employers no longer include noncompetes in their employment contracts. Instead, many include an employee nonsolicitation clause, which prohibits former employees from reaching out to former coworkers to try to hire them at their new workplace.

The Chilling Effects of Employee Nonsolicitation Agreements

While not as obviously an impediment to employee mobility as noncompetes, nonsolicitation provisions limit employees' job opportunities due to the actual and perceived risk of enforcement and litigation. For example, consider Employee A who leaves Company 1—bound by a nonsolicitation agreement—to work at Company 2. Other Company 1 employees might worry about contacting Company 2 for a job because they don't want Employee A to be accused of violating his nonsolicitation agreement (a risk even if Employee A is not involved in the recruiting process). Company 2 might also hesitate to recruit or hire other employees from Company 1 because it does not want to have to defend threats or lawsuits from Company 1 relating to Employee A's nonsolicitation agreement. As a result, employees at both

Cheryl A. Cauley, partner with Taylor & Patchen.

Company 1 and Company 2 are hindered in their ability to practice their chosen profession, trade or business by losing the opportunity to freely choose their jobs and their colleagues. And, aware of the chilling effects, employers often enforce or threaten enforcement of nonsolicitation provisions to prevent competitors from hiring their employees, even when a former employee did not affirmatively recruit those employees.

Until recently, employers have felt they may lawfully require employee nonsolicitation agreements from their employees because of the decades-old holding in *Loral v. Moyes*, 174 Cal. App. 3d 268 (1985). There, the California

Court of Appeal for the Sixth District held that a provision prohibiting the employee-defendant from "raiding" the plaintiffs' employees was a "reasonable" restraint and thus permissible under Section 16600. In 2008, however, *Edwards* made clear that there is no "rule of reasonableness" under Section 16600; instead, subject to limited statutory exception, a restraint of any kind is improper. But because *Edwards* did not explicitly overrule *Loral*, and because the holding did not specifically address employee nonsolicitation provisions, employers continued to use such provisions without any check from the courts. That has now changed.

The Far-Reaching Implications of the AMN Decision

In November 2018, the California Court of Appeal for the Fourth District held that an employee nonsolicitation clause was invalid under *Edwards* and Section 16600. *AMN Healthcare v. Aya Healthcare Services*, 28 Cal. App. 5th 923, 936–39 (2018). In so holding, the court explained that *Edwards*' rejection of a "reasonableness" exception demonstrates that *Loral's* holding is likely no longer viable. To avoid that conclusion, some employers will likely point out that the nonsolicit in *AMN* applied to professional recruiters—on whom such clauses have a more obvious, direct impact—and will argue the holding should be limited to employees in that type of position. But, while the court mentions the employees' position as one basis for invalidity, its legal analysis under *Edwards* makes clear the decision extends to all employee nonsolicitation agreements. Two courts in the Northern District of California have since agreed, see *Barker v. Insight Global*, No. 16-cv-07186-BLF, 2019 WL 176260, at *2–*3 (N.D. Cal. Jan. 11, 2019); *WeRide v. Huang*, No. 18-cv-07233-EJD, 2019 WL 1439394, at *10–*11 (N.D. Cal. Apr. 1, 2019).

These decisions are likely to have far-reaching implications that will be felt immediately by employers and employees alike. The *AMN* court not only held that the nonsolicitation clause at issue was unenforceable, it also permanently enjoined the plaintiff-company from enforcing the clause against all other former employees. In addition, the court awarded attorney fees to the defendants because, by successfully showing the non-solicitation clause was unenforceable, they "conferred a significant benefit on the public." Those holdings are likely to encourage additional lawsuits—perhaps on a class-wide basis—for declaratory relief on this issue. The increase of such lawsuits is especially likely because contracts that violate Section 16600 are, by definition, a violation of California's Unfair Competition Law, which allows for restitution, and may justify an award of attorney fees under Code of Civil Procedure Section 1021.5. See Cal. Bus. & Prof. Code Section 17200; *Application Group v. Hunter Group*, 61 Cal. App. 4th 881, 906–08 (1998) (finding a non-compete "in violation of Section 16600 to be a violation of Section 17200 as well").

The Post-AMN Benefits to Employees

Employers are unlikely to be able to continue to use existing nonsolicitation clauses as a tool to prevent other companies from competing for their employees or to discourage current employees from leaving. This should have positive implications for employees, who will no longer feel hindered from following a former colleague to a new job, or recruiting former colleagues to a new venture. Further, if employers want to prevent such departures, they will need to convince employees to stay through incentives—such as increased pay or benefits, or improved work experience—rather than through threats and restraints. Although it took a decade after *Edwards*, courts have finally reached the logical conclusion compelled by California's strong public policy in favor of employee mobility: employee nonsolicitation agreements may no longer be enforced.

Cheryl Cauley *is a partner with Taylor & Patchen in San Francisco who focuses her practice on complex commercial litigation and intellectual property disputes, representing clients in fields such as internet search and advertising, wireless communications and biotechnology.*