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WHITE PAPER

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A Growing Trend: Employee Non-Solicitation Provisions Are Under Attack in California and Elsewhere

California courts are known for the skepticism with which they approach post-employment restrictive covenants. Until recently, however, they have generally enforced covenants restricting individuals from soliciting their former employer's employees. This *White Paper* addresses this recent trend, provides an overview of a California Court of Appeals and two federal district court decisions that reflect this trend, and discusses the extent to which California employers can still rely upon such non-solicitation provisions. It also discusses other contexts in which non-solicitation provisions are under attack: from state and federal antitrust regulators and the plaintiffs' bar.

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INTRODUCTION

Non-solicitation provisions and agreements are under attack in various forums from various constituencies. Several state and federal courts in California recently departed from a long-standing willingness to enforce employee non-solicitation provisions. Also, federal and state antitrust authorities and private plaintiffs in antitrust litigation recently launched various attacks against non-solicitation agreements as well. This *White Paper* addresses these trends and offers insight into the extent to which employers in California and elsewhere can rely on their non-solicitation provisions and agreements.

ENFORCEMENT OF EMPLOYEE NON-SOLICITATION PROVISIONS IN CALIFORNIA: *LORAL* AND *EDWARDS*

California is widely known for its broad public policy prohibiting non-competition agreements except in limited situations defined by statute.[1] Codified at California Business & Professions Code § 16600 ("Section 16600"), California law voids "every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind." Based on Section 16600, California courts have found that post-employment employee non-compete,[2] *customer* non-solicitation,[3] and employee *no-hire* provisions[4] are generally void.

Despite the breadth of Section 16600, however, courts have generally enforced *employee* non-solicitation provisions for over 30 years. However, the law in this area may be changing. The California Court of Appeal and two federal district courts recently issued decisions finding that employee non-solicitation provisions are void under Section 16600.

Whether this rule will ultimately be adopted as the law of the land in California remains to be seen. But, given the competitive recruiting market and high importance placed on retaining talented key employees, this is an issue that all companies with California employees should closely monitor. While employers await a final decision on the state of the law in California, employers should continue to ensure their employee non-solicitation provisions are reasonable in term and scope.

Since 1985, *Loral Corp. v. Moyes*[5] has been the seminal authority in California regarding the enforceability of employee non-solicitation provisions. The *Loral* court held that such provisions are enforceable as long as they are reasonable in time and scope.[6] The court also seemed to assume, without deciding, that a similarly limited customer non-solicitation provision was reasonable.[7]

Then, in 2008, in *Edwards v. Arthur Andersen,* the California Supreme Court held that a *customer* non-solicitation provision was unenforceable because it restricted Edwards's practice as an accountant as he could not seek to perform services for Arthur Andersen's customers.[8] The *Edwards* Court also disclaimed the common-law rule-of-reason analysis, finding that if the California legislature had intended to void only *unreasonable* restraints on one's profession, trade, or business, then it could have expressly done so in Section 16600. *Edwards*, however, did not specifically address whether a reasonable employee non-solicitation provision remained enforceable.

THE MOUNTING CHALLENGE TO *LORAL*

Since the latter half of 2018, three California courts have considered whether *Loral* is still good law in light of *Edwards*. All three have held that it is not.

The first case, *AMN Healthcare, Inc. v. Aya Healthcare Services, Inc.*,[9] was arguably a narrow ruling limited to the facts at issue in the case. Plaintiff AMN Healthcare, Inc. and defendant Aya Healthcare Services, Inc. are competing staffing agencies that solicit travel nurses and contract them out to medical care facilities around the country.[10] As a condition of employment, AMN required its travel-nurse recruiters to sign agreements that included a one-year, post-employment employee non-solicitation provision.[11] Despite this restriction, several AMN recruiters left, went to work for Aya, and recruited some travel nurses to leave AMN and provide service for Aya.[12] AMN then filed suit, asserting, among other claims, that the recruiters breached the employee non-solicitation provision.[13]

The California Court of Appeal found that the employee non-solicitation provision was void under Section 16600 because it

limited the defendants' ability to practice their profession (e.g., they could not recruit travel nurses).[14] Notably, the Court also disagreed with AMN's contention that the provision was reasonable—and thus, enforceable—under *Loral*:

> [*Loral*'s] use of a reasonableness standard in analyzing the non-solicitation clause there at issue thus appears to conflict with *Edwards*'s interpretation of Section 16600, which, under the plain language of the statute, prevents a former employer from restraining a former employee from engaging in his or her 'lawful profession, trade, or business *of any kind*. . .'
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> Because the *Edwards* court found Section 16600 'unambiguous,' it noted that 'if the Legislature intended the statute to apply only to restraints that were unreasonable or overbroad, it could have included language to that effect. . .'
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> We thus doubt the continuing viability of [*Loral*] post-*Edwards*.[15]

The second case, *Barker v. Insight Global, LLC*, was a federal district court case that also involved a staffing agency. There, the former employee-plaintiff previously worked for Insight Global as an Account Manager, Sales Manager, and Director of Operations.[16] Insight Global provides staffing services in the information technology, finance, accounting, engineering, and government industries, and as part of his employment, Barker had to agree—during his employment and for one year after separating from Insight Global—not to solicit Insight Global's employees to perform staffing services for a competitor.[17] After Insight Global terminated Barker's employment, he sued for, among other things, declaratory judgment that the employee non-solicitation provision was unenforceable and unfair competition based on the challenged provision.[18]

In response, Insight Global moved to dismiss Barker's declaratory-judgment and unfair-competition claims on multiple grounds. The court initially agreed that the employee non-solicitation provision was reasonable, valid, and enforceable under *Loral* (*Barker I*), and it dismissed the two claims. The court expressly held that *Edwards* did not limit *Loral*'s holding because *Edwards* did not address an employee non-solicitation provision.[19] However, after the *AMN Healthcare* decision issued four months later, Barker moved for reconsideration. Based on *AMN Healthcare*, the court reversed its ruling and held that "California law is properly interpreted post-*Edwards* to invalidate employee non-solicitation provisions."[20]

A California federal district court also issued on the third case at issue, *WeRide Corp. v. Huang*, in April 2019.[21] *WeRide* involves parties (corporate entities and individual defendants) who develop autonomous vehicles for the Chinese market.[22] The individual defendants previously worked for WeRide as its CEO and Director of Hardware before they went to work for a competitor.[23] As part of their employment with WeRide, the individual defendants signed agreements that included an employee non-solicitation provision that continued for one year following separation.[24] After the executives departed and began working for a competing company, WeRide sued them, asserting numerous claims, including breach of the employee non-solicitation provision, and it moved for a preliminary injunction enjoining them from continuing to do so.[25] Based on *AMN Healthcare* and *Barker*, however, the federal court denied this request, finding the provision unenforceable and that WeRide could not show that it was likely to succeed on the merits of this claim.[26]

SO WHAT NOW FOR CALIFORNIA EMPLOYERS?

Although *AMN Healthcare*, *Barker*, and *WeRide* depart from *Loral* and void employee non-solicitation provisions, those cases are not yet dispositive regarding whether all employee non-solicitation provisions are unenforceable under California law. *AMN Healthcare* and *Barker II* are arguably shaped by the facts at issue in those cases and may be limited to instances in which the employee's business, trade, or profession is recruiting, such that the employee non-solicitation provision effectively functions as a non-compete provision. Further, as federal district court cases, *Barker II* and *WeRide* are not binding on California courts, have no precedential value, and are either factually or procedurally unique. Further, with respect to *AMN Healthcare*, California courts outside of the Fourth District remain free to disagree with that court's holding.

Ultimately, in the absence of a decision similar to *AMN Healthcare* in every appellate court district, the California

Supreme Court or the legislature will need to address the issue for there to be certainty in this area. In the meantime, one thing should remain clear for California employers: to be enforceable in any context, an employee non-solicitation provision must be reasonable—that is, it must be limited in term and scope. The term should typically be limited to one or two years, and large employers should consider limiting the scope to employees who the individual worked with and/or became aware of during the individual's employment.

OTHER RECENT ATTACKS ON NON-SOLICITATION PROVISIONS AND AGREEMENTS

Employee non-solicitation agreements between companies are also under attack from federal and state antitrust authorities and private plaintiffs in antitrust litigation. As detailed in our October 2016 *Alert*, the U.S Department of Justice Antitrust Division ("DOJ") and the Federal Trade Commission issued guidance, warning that DOJ intends to prosecute criminally certain wage fixing, no-poach, and non-solicit agreements among employers.

Since that time, DOJ entered into a civil settlement with rail industry companies to resolve an investigation into alleged no-poach agreements, and the FTC settled wage fixing allegations against therapist staffing companies, as detailed in our August 2018 *Alert*. In addition, a group of state attorneys general have filed lawsuits or settled allegations against numerous franchisors in a variety of industries alleging that intra-franchise no-poach clauses are anticompetitive. These state attorneys general cases also have led to follow-up class action litigation.

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ENDNOTES

1 See Cal. Bus. & Prof. Code §§ 16601, 16602, 16602.5.

2 *Dowell v. Biosense Webster, Inc.*, 179 Cal. App. 4th 564, 575 (2009) (finding a noncompete clause void and unenforceable under Section 16600); *D'sa v. Playhut, Inc.*, 85 Cal. App. 4th 927, 935 (2000) (same).

3 *Edwards v. Arthur Andersen*, 44 Cal. 4th 937, 948 (2008) (finding a customer non-solicitation clause void and unenforceable under Section 16600).

4 *See VL Systems, Inc. v. Unisen, Inc.*, 152 Cal. App. 4th 708, 718 (2007) (finding a no-hire provision unenforceable because it was overly broad); *Thomas Weisel Partners LLC v. BNP Paribas*, Case No. C 07-6198 MHP, 2010 WL 546497, at *6 (N.D. Cal. Feb. 10, 2010) (finding a no-hire provision unenforceable because it restricted the mobility of the former employer's employees); *SriCom, Inc. v. EbisLogic, Inc.*, Case No. 12-CV-00904-LHK, 2012 WL 4051222, at *5 (N.D. Cal. Sept. 13, 2012) (same).

5 *Loral Corp. v. Moyes*, 174 Cal. App. 3d 268, 278–79 (1985).

6 *Id.* at 279.

7 *Id.* ("Defendant is restrained from disrupting, damaging, impairing[,] or interfering with his former employer by raiding Conic employees under this termination agreement. This does not appear to be any more of a significant restraint on his engaging in his profession, trade[,] or business than a restraint on solicitation of customers or on disclosure of confidential information.").

8 *Id.* at 948.

9 *AMN Healthcare, Inc. v. Aya Healthcare Servs., Inc.*, 28 Cal. App. 5th 923 (2018).

10 *AMN Healthcare,* 28 Cal. App. 5th at 926.

11 *Id.* at 927.

12 *Id.* at 932.

13 *Id.*

14 *Id.*

15 *Id.* at 938–39 (citing *Edwards*, 44 Cal. 4th 937 throughout) (emphasis in original).

16 *Barker v. Insight Global, LLC*, 2018 WL 3548911, at *1 (N.D. Cal. July 24, 2018) ("Barker I").

17 *Id*.

18 *Id*. at *4.

19 *Id. at* *8 (quoting *Edwards*, 44 Cal. 4th at 946 n.4).

20 *Barker v. Insight Global, LLC*, 2019 WL 176260, at *3 (N.D. Cal. Jan. 11, 2019) ("Barker II").

21 *WeRide Corp. v. Huang*, case no. 5:18-cv-07233-EJD, 2019 WL 1439394 (N.D. Cal. Apr. 1, 2019).

22 *Id.* at *1.

23 *Id.* at *3.

24 *Id.* at *10.

25 *See generally id.*

26 *WeRide*, 2019 WL 1439394, at *10–11.