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New California Statutes Expected to Have National Impact on Post-Employment Restrictive Covenants

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On January 1, 2024, two new California statutes that could have a national impact on employee restrictive covenants, such as noncompete and non-solicitation agreements, will become effective. California's Business and Professional Code (BPC) already contains stringent provisions essentially prohibiting noncompetes and non-solicits with employees in California. The two new bills, Senate Bill 699 (SB 699) and Assembly Bill 1076 (AB 1076), broaden those prohibitions.

Both bills will force employers—in California and across the country, and with employees in California and elsewhere—to ensure that no employees or former employees have restrictive covenants covered by the sweep of the new statutes. In the wake of these laws, many employers will need to implement protocols to ensure that they are not subject to enforcement litigation in California that could lead to costly liability and civil penalties. Given their breadth, it is likely that the new statutory provisions will be challenged and that there will be substantial litigation over their scope and application.

SB 699

SB 699 starts with a policy statement claiming that California has benefited from its law voiding post-employment restrictions. But the bill notes that even so, the policy against such contract provisions has been thwarted by California employers continuing to use them in employment contracts. The bill also asserts that, as the market for talent has become national and remote work has become more common, employers outside of California are trying to prevent employers in California from hiring employees through the use of restrictive covenants. The policy statement then asserts that "California's public policy against restraint of trade law trumps other state laws when an employee seeks employment in California, even if the employee had signed the contractual restraint while living outside of California and working for a non-California employer."

Against this background, SB 699 adds a new section 16600.5 to the BPC that essentially voids restrictive covenants that would have been enforceable when signed if the employee subsequently moves to California. First, the statute provides that a restrictive covenant that is unenforceable under the BPC is void "regardless of where and when the contract was signed." Second, employers are prohibited from trying to enforce a contract that is void under the BPC even if the contract was signed and the employment occurred outside of California. Third, employers are prohibited from entering into an agreement with an employee or prospective employee that is void under the BPC. Finally, the statute allows employees to sue employers for violating the statute. Employees can seek damages and injunctive relief, and a prevailing employee is entitled to recover reasonable attorney's fees and costs.

Significantly, under SB 699 if an employee or former employee moves to California, then it does not matter where the employer-employee relationship was formed, where the employee worked, what law the contract chooses, or where the contract was executed. Thus, a New York employer hiring an employee who lives in New York to work in New York may fall under the scope of SB 699 if that employee subsequently moves to California. In an environment in which remote work is simpler than ever before and employees are increasingly mobile, this could

open employers up to potential liability that they might not be able to foresee at the time they enter into restrictive covenants with new hires. Conversely, an open question under SB 699 is whether California-based employers might be prohibited from entering into or enforcing noncompete agreements with employees working in states where those agreements are enforceable. Out-of-state employees may challenge such agreements by litigating against their California-based employers in California courts.

SB 699 may cause employers to more aggressively commence litigation in courts outside of California so that agreements that were lawful when or where signed can be enforced before a California court can invalidate them. Non-California based employers may be incentivized by this statute to try to obtain relief from courts in their home jurisdictions to enforce a restrictive covenant after an employee's departure, particularly if the employee is planning to or has moved to California to work for a competitor. That same strategy might work for California-based employers seeking relief in their employee's jurisdiction.[1]

In any event, keeping track of where current and former employees live and work will be an important factor in complying with the new provisions in SB 699.

AB 1076

AB 1076 amends BPC section 16600 and adds new section 16600.1. The amended statute makes it unlawful to include a noncompete clause in an employment contract or to require an employee to enter into a noncompete agreement unless one of the existing exceptions in the BPC applies. The new statute creates an affirmative obligation for employers, by February 14, 2024, to notify their current and former employees that they were, but no longer are, subject to a restrictive covenant in their employment contracts.

The amended section provides that the existing statutory language voiding any contract that restrains an individual from engaging in a lawful profession, trade, or business of any kind "shall be read broadly . . . to void the application of any noncompete agreement in an employment context, or any noncompete clause in an employment contract, no matter how narrowly tailored, that does not satisfy an exception in this [statute]." While the statute refers to a "noncompete", it does not define this term. The statute, however, recites that it codifies existing law, particularly as pronounced by the California Supreme Court in *Edwards v. Arthur Andersen LLP*, 44 Cal.4th 937 (2008), where the Court invalidated both a noncompete and a non-solicitation agreement because each "restricted [the employee's] ability to practice his . . . profession." *Id.* at 948. California courts may seize on the Legislature's citation to *Edwards*, along with pronouncements that the section be read "broadly" to apply to "any noncompete," to interpret the new statute to cover non-solicitation and other restrictive covenants in addition to noncompetes.

Finally, the amended section states that it "shall not be limited to contracts where the person being restrained . . . is a party to the contract." This further broadens the scope of the law to include entities and persons whose business is affected by a noncompete agreement.[2]

Significantly, AB 1076 creates a new notice requirement that must be complied with by February 14, 2024. It requires employers to notify current employees (as well as former employees who were employed after January 1, 2022) of any noncompete agreements they signed which are now void. The notice must be (1) individualized, (2) in writing, and (3) sent to the last known address and email address of each covered employee. Noncompliance with the notice requirement "constitutes an act of unfair competition within the meaning of Chapter 5," sections 17200-17210 of the BPC, and thus subjects an employer to civil penalties.[3]

It will be critical for employers to review their records for contracts with employees that violate the new statutory scheme and to track down current and former employees with such contracts to give them the required notice that these provisions are void. This applies to current and former employees who are in California, including those who work remotely from within California (even if the employer is out-of-state), and former employees who moved to California. Some employers may choose, in an abundance of caution, to send notices to all employees with noncompete provisions in their contracts to inform them that these agreements are unenforceable in California.

Conclusion

SB 699 and AB 1076 reaffirm and strengthen California law rendering most post-employment restrictions with employees void and unenforceable. The scope of the new statutes is broad, as they purport to apply to all such provisions regardless of where they were initially executed or where the employee worked as long as the employee eventually is located in California—and potentially even more broadly depending on how courts interpret the new statute's reach.

Until questions about the constitutionality, scope, and enforceability of these new statutes are answered, employers should consider:

- Reviewing their employment records and identifying employees (and former employees who were employed after January 1, 2022) who are subject to restrictive covenants.
- Identifying current employees (and former employees who were employed after January 1, 2022) with such agreements who are located in California, regardless of whether they were California residents when they signed the agreement.
- Preparing notices that comply with AB 1076's notice requirement and sending those notices by mail and email.
- Putting in place a notice retention policy to ensure there are records of compliance with the notice provision.
- Updating hiring practices, particularly if employees will be based in California. That should include a review of template employment agreements and offer letters to assess whether post-employment restrictions should continue to be included and ensuring that departing employees are provided with the required notice if they are or will be in California.

As employers begin to tackle these issues in the new year, Carter Ledyard & Milburn LLP's knowledgeable and skilled employment attorneys can help navigate this developing new legal landscape.

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[1] California's Labor Code also allows for enforcement of a post-employment restriction if a California employee entered into an agreement governed by another state's law and was represented by counsel in negotiating the choice of law provision. CA Labor Code § 925(e). The impact of the new law on this provision is unclear.

[2] This section does not have direct applicability to the employment context, but more broadly demonstrates the new law's strengthening of California law disfavoring contractual agreements that restrain free trade in the market. The California Supreme Court addressed circumstances that raised this question without settling it in *Ixchel Pharma, LLC v. Biogen, Inc.*, 9 Cal.5th 1130 (2020). The Court held that BPC section 16600 could invalidate a settlement agreement that had the effect of restraining trade, even where the party impacted by the agreement was not a party to it, as a predicate for tortious interference with an existing contract. *Id.* at 1162.

[3] The California Unfair Competition Law, codified in Chapter 5 of the BPC, provides for civil penalties of up to $2,500 for *each* violation. BPC § 17206(a).

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