CLIENT ALERT: Governor Baker Signs Noncompetition Agreement and Trade Secret Reform into Law – By Jeffrey S. Siegel and Sean P. O'Connor

On August 10, 2018, Governor Charlie Baker signed recently-passed legislation regulating the use and enforcement of noncompetition agreements. In addition to reforming noncompetition agreements, the newly-signed legislation also provides for increased protection for trade secrets under state law. The passage of the law marks the culmination of years of negotiation and reform efforts. The law will go into effect on October 1, 2018.

I. Noncompetition Agreement Reform

The Massachusetts Noncompetition Agreement Act (the "Act") adds Section 24L to chapter 149 of the General Laws. By its terms, the Act "shall apply to employee noncompetition agreements entered into on or after October 1, 2018." The Act limits the ability of employers to enter into "noncompetition agreements" with and enforce those agreements against certain individuals. For those individuals to whom noncompetition agreements may apply, the Act sets out specific limitations and notice requirements for enforcement.

A "noncompetition agreement" is defined under the Act as an agreement under which the employee agrees that the employee "will not engage in certain specified activities competitive with the employee's employer after the employment relationship has ended." Specifically excepted out of the reach of the Act are the following types of agreements (among others):

- covenants not to solicit or hire employees of the employer;
- covenants not to solicit or transact business with customers, clients, or vendors of the employer;
- noncompetition agreements made in connection with the sale of a business entity;
- nondisclosure or confidentiality agreements and invention assignment agreements; and
- noncompetition agreements made in connection with the cessation of or separation from employment if the employee is expressly given seven business days to rescind acceptance.

The Act applies to employees who either live or work in Massachusetts. "Employee" is defined to include both employees and independent contractors.

Categorically, noncompetition agreements are not enforceable against (i) an employee who is classified as nonexempt under the Fair Labor Standards Act; (ii) undergraduate or graduate students that partake in an internship or otherwise enter a short-term employment relationship with an employer, whether paid or unpaid, while enrolled in a full-time or part-time undergraduate or graduate educational institution; (iii) employees that have been terminated without cause or laid off;

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or (iv) employees age 18 or younger.

In order for any noncompetition agreement to be enforceable, it must be in writing, signed by both the employer and the employee, and expressly advise the employee of his/her right to consult with counsel before signing. If the agreement is entered into in connection with the commencement of employment, it must be provided to the employee by the earlier of a formal offer of employment or 10 business days before commencement of the employee's employment. If the agreement is entered into after the commencement of employment, but not in connection with the separation of employment, the employer must provide "fair and reasonable consideration" beyond continued employment and provide at least 10 business days' notice before the agreement is effective.

The Act also governs the terms of the noncompetition agreement. Under the Act,

- the agreement must be no broader than necessary to protect one or more of the following legitimate business interests of the employer: (A) the employer's trade secrets, as that term is defined in section 1 of chapter 93L; (B) the employer's confidential information that otherwise would not qualify as a trade secret; or (C) the employer's goodwill;
- the restricted period may not be more than 12 months from the date of cessation of employment, unless the employee has breached his or her fiduciary duty to the employer or the employee has unlawfully taken, physically or electronically, property belonging to the employer, in which case the duration may not exceed two years from the date of cessation of employment;
- the agreement must be reasonable in geographic reach in relation to the interests protected. A geographic reach that is limited to only the geographic areas in which the employee, during any time within the last two years of employment, provided services or had a material presence or influence is presumptively reasonable;
- the agreement must be reasonable in the scope of proscribed activities in relation to the interests protected. A restriction on activities that protects a legitimate business interest and is limited to only the specific types of services provided by the employee at any time during the last two years of employment is presumptively reasonable;
- the noncompetition agreement shall be supported by a garden leave clause or other mutually-agreed upon consideration between the employer and the employee, provided that such consideration is specified in the noncompetition agreement. To constitute a garden leave clause within the meaning of this section, the agreement must provide for pay to the employee of at least 50% of the employee's highest base salary in the preceding two years before termination and not permit an employer to unilaterally discontinue or otherwise refuse to make the payments (unless the employee breaches); and
- the agreement must be consonant with public policy.

The Act permits courts to "reform or otherwise revise" a noncompetition agreement to the extent necessary to protect the applicable legitimate business interest. This "blue penciling" clause is an option available to the court. If the court elects not to blue-pencil an agreement and declares the noncompetition agreement null and void, the Act permits the court to sever the noncompetition

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agreement and enforce any remaining sections of an overall agreement.

Finally, the Act provides that actions brought under the statute must be brought in the county where the employee resides, or, if mutually agreed upon by the employer and employee, in Suffolk County or the Business Litigation Session. The Act also instructs that any choice of law clause in a noncompete agreement that states the law of another jurisdiction applies is not given any weight if the employee is or has been a resident of or employed in Massachusetts for at least 30 days prior to cessation of employment.

The Act leaves a number of questions unanswered, including:

- What constitutes "fair and reasonable consideration" for a noncompetition agreement? How does a judge determine if an employee received enough in exchange for entering into a noncompetition agreement?
- What constitutes "other mutually agreed upon consideration" to satisfy the garden leave requirement? Can an employer and employee agree that any amount of money – as little as $1 – is enough to meet this threshold?
- What does "without cause" mean with respect to the enforceability of a noncompete against an employee who has been terminated? Does the employer have to notify the employee of the reasons for termination to justify whether a termination is with or without cause?
- Whether the incorporation of a noncompetition agreement entered into before October 1, 2018, into a severance agreement entered into after October 1, 2018 would be analyzed under the Act.

It will take time to flesh out the meaning of the clauses of the Act, as employers first need to enter into post-October 1, 2018 agreements and employees (or future employers) thereafter will need to challenge the enforcement of those documents. Even then, a case would have to make its way up to a Massachusetts appellate court to be binding.

Employers in Massachusetts should be sure that any agreement entered into after October 1, 2018 be consistent with the terms of the Act. For existing noncompetition agreement, while the Act is not applicable, we expect judges may look to the teachings of the Act in determining whether the pre-October 1, 2018 agreements are reasonable.

II. Trade Secret Protections

In addition to the noncompetition reform measures discussed above, the newly-signed legislation provides for Massachusetts to adopt a version of the Uniform Trade Secrets Act ("UTSA"). The new law will replace Sections 42 and 42A of Chapter 93 of the General Laws and further codify and expand upon trade secret protections that were previously available under those Sections as well as under common law. With the law's passing, New York now stands alone as the only remaining state in which some form of the UTSA has not been adopted.

While many of the Massachusetts UTSA's protections will be similar to those previously available under statutory or common law, there will be some notable differences. For example, the Massachusetts UTSA expands upon the traditional definition of trade secrets to include those that

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have “potential” economic value instead of just “actual” economic value. It also provides for fee-shifting provisions whereby attorneys’ fees may be recoverable by prevailing parties if: (i) claims of misappropriation are made or defended in bad faith; (ii) motions for injunctive relief are made or defended in bad faith; or (iii) willful and malicious misappropriation exists. The Massachusetts UTSA also provides for the potential award of exemplary damages in cases of willful and malicious misappropriation.

The Massachusetts UTSA will go into effect on October 1, 2018 and apply to misappropriations of trade secrets occurring on or after that date. Misappropriation claims under the Massachusetts UTSA will need to be brought within three years after the misappropriation is discovered or should have been discovered through the exercise of reasonable diligence.

There will be many questions still to be answered as the law goes into effect and is interpreted through the courts. Regardless, its passing reinforces Massachusetts’ commitment to protecting businesses’ trade secrets. Employers should review their current employment policies and agreements, including their confidentiality and nondisclosure agreements, to ensure that they remain compliant and take advantage of the protections provided for by the new law.

MBJ will continue to monitor these important developments.

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