**Podcast Transcript**

# The Emerging New Era for Noncompetes and Trade Secrets: Future Shock: How To Protect Trade Secrets when Noncompetes Become Truly Disfavored

**Date: February 16, 2022**

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**Run Time:** 31:23

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Rubenking: The restriction and legislation of noncompete agreements is gaining traction around the country. In July, President Biden signed an Executive Order that discussed the regulation of noncompete agreements, which in the past has only been the province of the states. To stay ahead of the game, both employers and executives need to know what changes to expect and how to best prepare for the future. To help bring all this into focus, we've created a six-part series called The Emerging New Era of Noncompetes and Trade Secrets. I'm Randall Rubenking, and you are listening to BakerHosts.

Our sixth and final episode, Future Shock: How to Protect Trade Secrets when Noncompetes Become Truly Disfavored, discusses how companies and

employees have to change their approaches to noncompetes and trade secrets enforcement to adapt to the changing legal landscape. Our guests today are Partners Joyce Ackerbaum Cox and John Siegal, co-chairs of BakerHostetler's Noncompete and Trade Secrets team. Let's listen in.

Siegal: My name is John Siegal. I'm here with Joyce Ackerbaum Cox. We're the co-leaders of the Baker & Hostetler National Noncompete and Trade Secret Practice Group. Here for the noncompetes and trade secrets today is titled Future Shock: How To Protect Trade Secrets when Noncompetes Become Truly Disfavored. Let me just quickly give you a very oversimplified summary of what we've been talking about in the last five sessions in terms of the trends in this area.

What we've been describing and analyzing is a rapid and ongoing change in the world of noncompete and trade secrets law. The basic conclusion and advice is, because of such rapid change we really can't rely on our old knowledge and our old strategies that we and our companies and our clients have done for years. There needs to be a revisiting and a re-strategizing a lot of areas. Five years in, the federal Defend Trade Secrets Act hasn't yet really changed the law materially, although it has very clearly and substantially moved cases involving trade secret claims to the federal courts.

But paradoxically, the DTSA has not met, at least yet, its stated objective of unifying the law nationally. And at the same time on a parallel track, state laws are becoming ever more divergent for reasons we've discussed and will discuss today. There is, it is fair to say, a national movement to restrict and limit the use of noncompete agreements. State statutory prohibitions and regulations on the use of noncompetes for lower-salaried employees are becoming prevalent. Attacks and limitations, both in the courts and statutorily, on the use of noncompetes for purposes of what some call restraints of trade, protecting client and employee relationships are on the defensive.

There is a distinct possibly of federal rulemaking by the Federal Trade Commission as we've discussed. And, in addition the use of noncompetes without notice or without additional consideration is also subject to revisiting and re-evaluation in a lot of jurisdictions. At the same time as we discussed in our fourth session, extraterritoriality and the use of the DTSA to seek to protect trade secrets globally, beyond the borders of the United States, is clearly the next wave that is happening in the federal courts and we all need to follow that closely. And at the same time, as we discussed last month, criminal enforcement against no-poach agreements is here. It is real, and it is something that every company and every client needs to be concerned about. So, with that description of what we've talked about for the last five months, Joyce, where does that leave us all?

Cox: Good question. I think that it leaves us in, with a mixed bag. I think it leaves us with businesses having to be very careful with the noncompetes they choose to use, with businesses being very thoughtful about alternative methods that they can employ to protect their assets and their secrets. And with, what I would say,

a healthy dose of we don't know because the law is just continuously changing. It is going to be unfolding, at both the federal and the state level, as you mentioned, certainly with this administration and with a lot of pending legislation in other states and certainly legislation that has already passed. So, while the kind of the topic of this is how to protect trade secrets when noncompetes become truly disfavored, before we get more specific, I want to talk about just kind of five key takeaways or recommendations when we're talking about noncompetes themselves. Recent kind of studies show that 18% of the current U.S. workforce is subject to a noncompete, and about 38% of workers have at some point been subject to a noncompete. So, it is very prevalent out there, and all of our, many of our clients, many of you on the call today, have used them in the past or currently are using them.

So, I think that, I want to talk about a couple of key takeaways, things that you can think about and consider when leaving here today. And this is from the perspective of if you are the employer drafting the noncompete. Certainly, you know, the reverse holds true as we defend a lot of these cases as well. We, this is one area where you do both sides, employer/employee departing, company hiring, company etc. But this specific advice is really from the drafter's perspective, so I want to make that clear.

I think first and foremost is you've got to give significant thought to who in your workforce needs to be subject to a noncompete and who doesn't. So, long are the days that you give everybody a noncompete as part of onboarding from the CEO down to the janitor or the receptionist. You have to be very mindful of who can harm you and how they can harm you. Is it going to be by confidential information if they leave, they're going to take that with them? Is it going to be by trying to take your customers? Is it going to be because they have some sort of a recipe or a formula, or something like that? Is it going to be because you've spent an extraordinary amount of time putting them through a training program that is particular to your company? So, you've got to be very mindful of what it is you're trying to protect and how. And that is an important kind of starting point when you're thinking about crafting a noncompete.

Also, I think it is really important, and it was mentioned earlier in one of the webinars by our Antitrust Partner Ann O'Brien, that is particularly relevant in the antitrust context. If you have a company, if your company has a culture that is one that never has and never will enforce noncompete, or you work in an industry where you have the type of workforce where it just, doesn't work. And there is a lot of industries like that. If you're not ever going to enforce the noncompete, then, it really shouldn't be in the confidentiality or other employment agreement or it shouldn't be a freestanding agreement, shouldn't have it at all. I think that is really important because that is actually used against companies in a lot of litigation right now that we're seeing in the antitrust field where they have it, and they say, oh, we never, even enforce it. That is actually used against them.

The second kind of takeaway is that, think about other ways that you can seek to protect your company's legitimate business interests other than noncompetes. So, can you rely on a non-solicitation agreement, and of course this is in states

where, non-solicitations are viewed differently than noncompetes. And I believe John talked a little bit about that in his last webinar. But, you know, non-solicitations may very well protect what you're seeking to protect, them going after your customers, or your other employees, and that sort of thing. Think about guard and leave payments. Is it, do you want to keep someone on the payroll and therefore keep them having a duty of loyalty to your company, even though they're not continuing to actively work for you? That is an option. They do that a lot in the U.K., they have for a long time. I think that is something that we're going to maybe start to see more here.

I think another option might be clawback of severance payments. You know, a lot of, certainly for the executives, we pay out, companies pay out severance payments. They do it sometimes in tranches and things like that. There is a violation of an agreement with respect to providing confidential information, or trade secrets, or working for a competitor. Then you can look at clawbacks and those, as well as repayment of training fees. You know, like I said, if there is a particularized program that you put an employee through or something similar, maybe that is kind of a hook to keep people from leaving and going to another company. But of course, there is a lot of state law considerations for each one of those sorts of things. But they're just different options, and so I think that is what we have to do, is think about different options here other than the traditional noncompetes.

So, the third kind of takeaway that I want to mention is, you've got to go in now and review existing employment agreements and agreements that are freestanding noncompete or non-solicitation confidentiality agreements. There is no one-size-fits-all. I think if we, if there is, one major theme that John and I have tried to express throughout this entire, six-month series, is that there is no one-size-fits-all. And we get a lot of frustrated national, multinational, international companies that say, I can't have 50 agreements for each different state. And that is perfectly understandable. But there is a lot of different approaches you can take. So, you can do a regional approach, you can do a national approach, but if you decide that you want to have one on a national basis, you need to understand there are places that it is never going to be enforced, or that you're not even allowed to put them in writing in the first place. So, there is a couple states that you're going to want to have a pullback for employees in those states. And you have to understand that the impact on the business is that if this is a violation that occurs in one of these states, it is not going to get passed. So, it is something that you weigh from a business standpoint if you want to have something on a national level. But, there are other different ways to approach it, somewhere between one agreement and 50-plus different agreements, and we can certainly help you with that. But, that is tough.

When you're actually looking at the noncompete, one of the things that John and I see all the time is, people define their business or their competing business as very, very broad. If you are a parent company or a multinational company, you've got many, many different products and lines of business which very unlikely have anything to do with, or most of which have nothing to do with, perhaps the employee at issue in a noncompete. So, you need to specify what it is that this

employee is touching. What line of business is he involved with, what particular subsidiary, what particular company? You don't want your company to be so broad that you're trying to basically prohibit the individual from working altogether. So, that competing business needs to be as narrowly tailored as possible. And sometimes that can just be the name of the, by addressing the name of the employer that is a party to the agreement. Something to think about.

Also, obviously, defining the geographic scope as narrow as possible. That is really hard these days, given that everything is, like we're doing now, Zoom, and you can reach people nationally, internationally, so easy. But, there are still places where individuals have customers in a particular region within a state or multiple states, or whatnot, and so you want to tailor that as specific as possible to the business that the employee is covering for the employer.

Along these same lines, the choice of law is critical, and I cannot stress this enough. We've mentioned many times about how many new statutes have gone into play. I think John just again mentioned about lower-income employees being, statutes being passed to not pertain to lower-level employees. I think there is probably 10 new statutes, states that have done these. I recently read that it is also not just going to be the blue states, some of the red states are starting to participate, too. So, Iowa and West Virginia have pending legislation in this area.

And I think one thing that is important, when people think of lower-level employees, we're not just talking about fast food employees, or hourly employees. I mean in some states the amount, the threshold level of a lower-level employee could be $100,000. So, you've got to be aware of what your statute says in your particular state and how lower-level is defined. Many times it might be X times the minimum wage or something like that. But it has got a different definition based upon the statute, and you've got to be aware of what that is and pay attention to all the new legislation. And of course, you're always tracking and paying attention to what is going on at the federal level if something is going to come out, in terms of some sort of national, federal legislation.

So, the other thing when you're looking at a choice of law is being mindful of which states blue pencil, or modify, and which ones don't. This is particularly important. For example, Florida will modify and will blue pencil, so if you've got an agreement that is overbroad, they will strike it, rewrite parts of it, so that to make it reasonable. Other states won't. They'll just consider the whole thing unenforceable, or some states will just draw a line through the offending language, and if what is left doesn't make any sense then you, as the business trying to enforce it, are going to be in a bit of a predicament. So, think about how that blue-pencil modification standard is going to come up in the states that are you're looking at.

And I think it is also important to be mindful that a lot of jurisdictions are not going to accept your choice of what provision regardless of what you put in there, if it offends their public policy, or if there are not acceptable ties to the jurisdiction. We see often people say, well, I want to put X state law because I think it is really favorable in my noncompete. I'm like, okay, well what ties does your company

have there? What ties does the employee have there? And if the answer is none and none, or even none on one side or the other, that could be problematic. So, the choice of law, I can't really overstate how important the choice-of-law analysis is when crafting.

When you're reviewing your employment agreements, I think it has become very clear that you've got to remove the no-hire language. I think that that is just on a going-forward basis that is very dangerous to subject any employee to a you-shall-not-hire-our-employees-away-from-our-company. We've seen the danger in this type of no-poach language. In fact, we have, there are states that have on the books no-poach statutes that have never been enforced or don't have any caselaw when you look them up. For example, Florida is one of them. But I think that if this sort of a trend continues, people might start to invoke those, of course not to mention what is going on with the DOJ and all the things that Ann O'Brien spoke about from an antitrust standpoint.

So that is just kind of the, from the employee/employer angle. There is, of course, the whole area of third-party agreements that your company might have with other companies, with staffing firms, with things like that. You also need to review those agreements with a particular eye towards antitrust issues that Ann O'Brien spoke about. Certainly eliminating no-hire language in those, beefing up areas where you're identifying what the interests are so that they're apparent on their face, Those things are very important, because we talked to a lot of clients that continue to just renew the same agreement year after year after year. They've been in place for 10 or 15 years and nobody has actually read the bulk of the agreement except to change kind of the dates of operation and maybe the cost. And that is a problem, got to go back and look at those and now is a good time as any.

And I think the last kind of takeaway, the fifth takeaway, I would say, is really training your employees, particularly the HR staff, your C-Suite employees, and those that are negotiating third-party contracts, on the antitrust issues that we talked about. There is that guidance out there for HR professionals. If you haven't read that, or haven't made sure that your HR folks have read that, we would highly advise that that be provided to all of your HR individuals. But, annual training on these sorts of things is really important because it is a simple email or sometimes a simple comment that companies share one-to-another that might get you in hot water with the Department of Justice. And given their uptick in civils, criminal filings and enforcement under this administration is something to be particularly aware of.

Of course, as John mentioned, as I've said, we've been doing all of this. We have no certainty, no guarantee of enforcement. A lot of times, as I tell my clients, it really depends, the luck of the draw of the judge, because some judges will always hate these, and some will like them, and you never know. But, I think we're getting more to the point where it is going to be more and more problematic, rather than kind of the flip of a coin. So, having said that, John, I'm going to turn it back to you and talk about what impact will all of these kind of

restrictions and scaling back on noncompetes have on trade secrets and the litigation of trade secrets moving forward.

Siegal: Thanks, Joyce. I mean, we don't have a crystal ball and we're not here to see the future. We're just trying to see the issues as they might arise. But I think that clearly based on the skepticism, and legislative and judicial disfavoring of some purposes and rationales for enforcing restrictive covenants, we should all assume the relative importance of the trade secrets rationale to enforce restrictive covenants will greatly increase as skepticism on restraints, on soliciting or converting customer relationships or employee solicitations grows and enforcement is scaled back. So, what do you do?

This certainly increases the importance of not just relying on a noncompete or restrictive covenant, but having adequate and appropriate trade secrets agreements in place with employees. Whether some bundling of confidentiality agreements, nondisclosure agreements, intellectual property agreements, inventions agreements, work-for-hire agreements, all the things that protect a company's trade secrets and confidential proprietary information, so that you're not just relying on the noncompete or an employment-based restrictive covenant as those perhaps become ever more disfavored.

The trade secrets agreements, like what Joyce said about employment-based restrictive covenants, really need to be specifically tailored to the business context and situation, not just in the company, but to the extent possible the employee's role, to identify the technologies involved, identify products involved, processes and employee roles. You know, most of these agreements that most of us see and have written over the years have a broad general definition of trade secret, usually, derived from the restatement perhaps now from the Uniform Trade Secrets Act or the DTSA and that broad general restatement of the law is going to be less effective than trade secrets types agreements that really are tailored to the specifics of the situation when you're trying to enforce them.

Trade secrets audits are highly advisable. They're a great idea and, frankly, most companies never do them. They do them after the fact when the problem arises, right, and it is especially true to proactively review and analyze and make sure you have button downed your measures to maintain secrecy, so that you can demonstrate actual, real implementation of to meet that secrecy requirement in a trade secrets case and not to be trying to cobble it together later, but to be able to show: password protections, protection of vital information on a need-to-know basis, not simply stamping everything confidential and thinking that is going to do it. But, really, in an analytical way going through, reviewing the procedures in place and improving them. It is also very true, with regard to specifying trade secrets. You know, I've seen so many cases, I've been involved in so many cases on both sides, where it is, okay there is a misappropriation of trade secrets, there is a claim, now let's figure it out. How do we specify, how to we detail it, how do we explain it to a court, and the days of being able to do that over the course of the litigation in discovery are numbered under statutes and procedures in a lot of states, specification of trade secrets is required early on. And, if you're scrambling to do it in a litigation context, it is very different and very

less-effective, than if proactively, you're looking at what you're going to need to protect, you're able to define it with some specificity, you're able to identify who has access to materials or processes or information, and how those things are protected.

Having said, we're not here to see the future and don't have a crystal ball, let me make a few predictions, that next year or five years from now, you can call me on, but I think that based on what we've been discussing, these are assumptions that you should use in your business planning and your litigation planning. First, the DTSA will continue the trend of cases migrating to federal courts. The filings in federal courts are way up, and there is every reason to think that will continue. I believe at the same time, though, that federal judges will start to push back on this, and the assumption that because there is the DTSA, and because it is a federal court that it is always the right place to bring a claim is something that you should look at skeptically and think about in any litigated situation. Federal judges will push back. I've seen it happen in cases where judges don't just sit back and let the cases develop, but they apply the stringent standards on a Motion to Dismiss in a federal court, and I think that we should expect some screening process by federal judges, especially in high-volume jurisdictions where they're going to see a lot of these cases, they know that 70-80% of the cases that are being filed in the federal courts are cases that were garden-variety trade secret or noncompete cases filed in the state courts prior to the DTSA. And they will, naturally, look for ways to limit access to their docket. So, I think you've got to push back against the idea that because there is a DTSA and subject matter jurisdiction, you always bring these cases in federal courts. I think there'll be a blowback on that.

U.S. courts, U.S. federal courts are and will increasingly attract extraterritorial claims in trade secrets cases, it is an available forum. We all need to watch how the caselaw develops on this, but if the caselaw continues to permit such filings, it is going to be a very attractive forum, and there'll be more and more cases. And, something that is not really in the nature of prediction, but in the nature of something to think about, is that if these trends towards more stingy, if you will, enforcement of restrictive covenants continues and perhaps a tighter screen on trade secrets cases that go all the way into discovery and towards trial, I really urge people to consider whether and when arbitration is a relatively more attractive place for plaintiffs bringing these claims. It depends on the industry, depends on what arbitrable forum. I certainly can say from experience in the financial services world that FINRA remains a very available form with not only injunctive relief but perhaps a greater acceptance of damages claims in trade secrets and restrictive covenants cases than in a lot of courts. And, so I would urge people who are thinking about where to bring claims, and how to bring them, prospectively in drafting agreements, to think about arbitration and where does it make sense, and where might there be industry or other arbitrable forums that are more attractive venues.

I've seen this for 25-plus years practicing in this field, as many others on the call no doubt have, but whatever happens, I have no doubt it will continue to be the case, that nearly every company believes that nearly everything it has and

everything it does is a trade secret, or at least proprietary confidential information that is protectable through agreements, and at the same time that nearly every departing employee believes or claims they believe that nearly everything their company does is not a trade secret. And we all know the truth and the facts lie in-between those two polarities, and that is why there is so much trade secrets litigation and will continue to be. And, no matter how these statutory regimes evolve, and no matter how the caselaw evolves, because of those competing tensions, we're going to continue to see a lot of activity in this area, with a lot of us, a lot for all of us to do and learn. And, so we look forward to keeping in touch with you all and talking about it. And. Joyce, let me kick it back to you to close out, and thank you all for listening.

Cox: Thanks, John. I, it would be nice if we had crystal ball in this area for sure, but there is going to be a lot for us to keep our eye on in the coming years.

This brings us to the conclusion of our six-month, six-part series that we have conducted for you over the last several months. We thank everyone for joining us. Please let us know if there is anything that we can do to help you. We've got, obviously, a national team of people sitting in a variety of states and we've covered this from the drafting, all the way through the litigation stage, and can help you in any way that we can. We'd also be happy to hear from you, if there are particular subjects that you'd like to hear about from us with respect to future webinars, whether it is a one-off or we opt to do kind of another series. Maybe it will be on what the FTC and what the Biden Administration do. Certainly if that comes out, you'll be hearing from us. We, again, appreciate your attendance and please reach out and let us know if you have any feedback or we can help you in any way. Thank you so much. Have a great day.

Rubenking: Thank you, Joyce and John. If you have any questions for them, their contact information is in the show notes. As always, thanks for listening to BakerHosts. Comments heard on BakerHosts are for informational purposes, and should not be construed as legal advice regarding any specific facts or circumstances. Listeners should not act upon the information provided on BakerHosts without first consulting with a lawyer directly. The opinions expressed on BakerHosts are those of participants appearing on the program and do not necessarily reflect those of the firm. For more information about our practices and experience, please visit bakerlaw.com.