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Legislature Passes Sweeping Non-Compete Reform; Bill Awaits Governor's Signature

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On July 31, 2018, the Massachusetts Legislature passed long-debated legislation aimed at reforming the law surrounding non-competition agreements. Non-competition agreements are commonly used to restrict competition following the ending of the employment relationship. If signed by the Governor in its present form, the law would go into effect October 1, 2018 and significantly alter the landscape related to non-compete agreements for employers and employees in Massachusetts.

Overview of the Legislation

This law would provide sweeping reform to the way employers would be required to structure non-competition agreements. Below is a brief summary of some of the Bill's most significant provisions.

Coverage

The law covers both employees *and* independent contractors who work *or* live in Massachusetts. Multi-state employers are not exempt from this law as it relates to their employees who live or work in Massachusetts.

The law would go into effect on October 1, 2018 and would apply to non-competition agreements entered into on or after this date. Importantly, the law does not regulate non-solicitation agreements (for example, prohibitions on soliciting employees or customers), non-disclosure agreements, or certain other commonly used restraints designed to protect an employer's business interests. The law also does not generally apply to non-competition agreements made in connection with the cessation or separation of employment if the employee is expressly given 7 business days to rescind acceptance. Another notable exception is that the law would also not apply to agreements made in connection to the sale of a business entity where the owner of said business is restricted from competition in exchange for "significant" consideration.

Restrictions on Enforceability

The Bill provides that non-competition agreements cannot be enforced against:

- Employees classified as nonexempt (*i.e.*, eligible for overtime) under the FLSA;
- Undergraduate or graduate students partaking in an internship or other short-term employment relationship with an employer;
- Employees who are 18 years old or younger.

Under this Bill, non-competition would also not be enforceable against any employee who is terminated from employment "without cause or laid-off."

For non-compete agreements entered into at the commencement of employment, the agreement must:

- Be in writing, signed by both the employer and employee;
- Expressly state that the employee "has the right to consult with counsel prior to signing"; and
- Be provided to the employee *before* a formal offer of employment is made or 10 business days before commencement of the employee's employment, whichever comes first.

For non-compete agreements entered into after the commencement of employment, the agreement must:

- Be in writing, signed by both the employer and employee;
- Be supported by "fair and reasonable" consideration, independent from the mere continuation of employment;
- Expressly state that the employee "has the right to consult with counsel prior to signing"; and
- Include notice of not less than 10 business days before the effective date of the agreement.

Additional Requirements for Non-Competition Agreements

Largely incorporating existing common law (case law) protections, the Bill specifically provides that non-compete agreements 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 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

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employer's goodwill." Agreements must also be "reasonable in scope of proscribed activities in relation to the interests protected", and must be "reasonable in geographic reach in relation to the interests protected." Although case law already requires non-compete agreements to be reasonable in temporal scope, the Bill specifically limits the restrictive period to no more than 12 months (with a limited exception where there was a breach of fiduciary duty or theft of employer property the agreement may allow for a 2 year restrictive period).

Of particular note, the Bill adds a new requirement that agreements must include a "garden leave clause, or other mutually-agreed upon consideration between the employer and the employee." More common internationally than domestically, "garden leave" clauses provide for continued payment during the restrictive period. This Bill provides that a garden leave clause shall:

- provide for the payment, consistent with the requirements for the payment of wages under section 148 of chapter 149, on a pro-rata basis during the entirety of the restricted period of at least 50 percent of the employee's highest annualized base salary paid by the employer within the 2 years preceding the employee's termination; and
- except in the event of a breach by the employee, not permit an employer to unilaterally discontinue the payments.

Should this Bill be signed into law, it is yet to be seen how this additional financial burden may affect employers' use of non-competition agreements. Similarly uncertain is the meaning of the phrase "other mutually-agreed upon consideration" which appears to open the door for alternative financial arrangements – left uncertain (and perhaps for litigation) is the amount necessary to satisfy the alternative consideration requirements of this section.

Next Steps

This Bill, if signed into law, would significantly change the rules related to non-competition agreements, and for some may require a reconsideration of strategy and approach to protecting business interests. While non-competition agreements would still be lawful and enforceable under this Bill (assuming the requirements are met), the additional requirements and costs are likely to alter the legal landscape and incentivize different approaches. Industries that rely on non-exempt labor or have high lay-off rates will be particularly affected. Among other potential considerations is the use of revamped non-solicitation and confidentiality covenants, which fall

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outside the specific provisions of this Bill. These provisions can be used separately from or in conjunction with non-competition provisions. Stay tuned for additional updates.

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If you have any questions about this issue, please contact Kier Wachterhauser or the attorney responsible for your account, or call (617) 479-5000.

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