

Employee Mobility and Trade Secrets: How to Hold on to Confidential Information and Your Employees

PANEL 2



Today's Presenters



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Employee Mobility Is a Strong Public Policy of California

Non-compete Agreements

- Noncompetition agreements are generally unenforceable in California
- *Cal Bus. & Prof. Code Section 16600*: “Except as provided in this chapter, every contract by which anyone is restrained from engaging in a lawful profession, trade or business of any kind is to that extent void”
- **Edwards v. Arthur Andersen LLP** (2008) 44 Cal. 4th 937
 - No “narrow limitation” exception
- **Practitioner’s Note**: can’t require employees to sign unenforceable non-competes
 - California case law – basis for wrongful termination claim
 - Labor Code Section 432.5

Other Restrictive Covenants

- Three common types:
 - Customer non-solicitation – Generally unenforceable California
 - No-Hire provisions – Unenforceable in California
 - Employee non-solicitation – no longer enforceable in CA?
- **Majority rule outside CA? Restrictions must be:**
 - Reasonable in scope (geography, time, subject matter)
 - Narrowly tailored to protect a legitimate business interest

Section 16600 Exceptions

- Section 16600 prohibition on noncompetition agreements contains specific exceptions:
- Person selling a business or substantially all of ownership interest in business (including goodwill) may agree with the buyer to refrain from:
 - carrying on a like business;
 - within a specified geographic area in which the business sold has been carried on;
 - provided the buyer, or any person deriving title to the goodwill or ownership interest from the buyer, carries on a like business therein
- Also applies to dissolution of a partnership or a member leaving a limited liability company

Strategies to Get Around California's Rule

- “Garden leave” = Provisions authorizing salary and benefits during a non-solicitation or noncompetition period
- *Garden leave provisions have not been tested in California courts*
- Such provisions may be of marginal utility:
 - The employee can always leave
 - The employer's option is to cut off payments
- “Employee choice” doctrine
 - Restrictive covenant not subject to the usual reasonableness standard when it is contingent upon an employee's choice between receiving and retaining a benefit - and competing.

A stack of three dark-colored books is shown, secured with a heavy metal chain. The chain is wrapped around the books and fastened with a padlock, symbolizing the protection of trade secrets. The books are stacked on a light-colored surface. A semi-transparent dark green rectangular box with a thin light green border is overlaid on the books, containing the text.

What About An Employer's Trade Secrets?

Trade Secrets Exception?

- A trade secrets exception is not expressly stated in Section 16600
- **Edwards v. Arthur Andersen:** The California Supreme Court avoided answering the question
- **Asset Marketing Sys. v. Gagnon** (9th Cir. 2008) 542 F.3d 748: Ninth Circuit interpreted *Edwards* as not applying to restrictive covenants designed to protect employer's trade secrets
- Courts have held that courts may enjoin tortious conduct under the Uniform Trade Secrets Act and Unfair Competition Law by banning the use of a former employer's trade secrets to identify, solicit or otherwise unfairly compete with the former employer's clients

Cal. Uniform Trade Secrets Act

- Cal. Civil Code section 3426 et seq.
- What's a trade secret?
 - Information that derives economic value from not being generally known to the public or competitors; AND
 - Reasonable steps must be taken to protect the secrecy of the trade secret information

Defend Trade Secrets Act

- Effective May 2016 - created federal cause of action for trade secret misappropriation, but does not preempt state laws
- Similar to UTSA - definition of “trade secret” and “misappropriation“, remedies, statute of limitations
- **AUA Private Equity Partners v. Soto** (S.D.N.Y. April 5, 2018) 2018 WL 1684339: Fact that defendant took documents was sufficient for DTSA claim; fact that she didn’t use them was irrelevant, as the DTSA does not require “use” or “disclosure”
- New whistleblower protection:
 - Immunity from liability for disclosure of trade secret if made in confidence to officials solely for purpose of reporting or investigating suspected violation of law
 - If disclosed in complaint or other document filed in lawsuit or other proceeding if made under seal

Defend Trade Secrets Act - Notice

- Requires employers to provide notice of immunity to employees and contractors, for contracts entered into or updated after May 11, 2016
- Specific language, or cross-reference to policy document
 - Nondisclosure agreements
 - Assignment of inventions agreements
 - Whistleblower policy
 - Handbooks
 - Contractor agreements
- Failure to provide notice? Employer cannot recover attorneys fees or exemplary damages

Tread Carefully

- California Civil Code section 3426.4: “If a claim of misappropriation is made in bad faith, a motion to terminate an injunction is made or resisted in bad faith, or willful and malicious misappropriation exists, the court may award reasonable attorney’s fees and costs to the prevailing party.”
- **FLIR Systems, Inc. v. Parrish** (2009) 174 Cal.App.4th 1270: Court found that company brought misappropriation claim in bad faith to stifle competition; former employees awarded \$1.6 million in attorneys’ fees and costs
- **SASCO v. Rosendin Electric, Inc.** (2012) 207 Cal.App.4th 837: Court affirmed a trial court’s order awarding the defendants almost \$485,000 in attorneys’ fees and costs pursuant to section 3426.4

A hand is shown in the bottom right corner, holding a piece of white chalk and drawing a large arrow on a dark brown chalkboard. The chalkboard is covered with numerous smaller, hand-drawn white arrows of various sizes and orientations. A semi-transparent white rectangular box with a thin black border is positioned in the center of the image, containing the text "The Trends".

The Trends

Trends

- States are becoming less tolerant of restrictive covenants
- Increase in trade secret litigation
- Remote workforces may be more difficult to monitor for possible trade secret theft
- Jurisdictional issues relating to enforceability of restrictive covenants against remote workforce
- DOJ prosecution of “no-hire” agreements
- Risk of litigation based on presentation of unenforceable restrictive covenants



Hiring & Onboarding

RESUME

POSITION	COMPANY	DATE
SENIOR DESIGNER	ABC COMPANY	2010 - 2012
ASSISTANT DESIGNER	DEF COMPANY	2008 - 2010
BACHELOR OF ART	GHI UNIVERSITY	2005 - 2008
COOL DESIGN TRAINING	JKL TRAINING	2003 - 2005

AWARDS

- Best Designer of 2010
- Winner of Euro Design 2009
- Best Creative Designer 2008
- Winner - National Design Competition
- Winner Adobe...

Precautions in the Hiring Process

- Ascertain whether candidate has knowledge of prior employer's trade secrets
- Remind applicants not to share trade secrets, in writing if of particular concern
- Do not copy or upload/download any files/documents for use at company
- Do not permit new hires to perform work until after departure from prior employer
- Do not move customers/orders over – traffic must come from customers to you
- Should employers review agreements before/after hire? Or, avoid reviewing them altogether?

Written Agreements for New Hires

- Offer letter
- Employment agreements
- Handbook provisions
 - Add provisions affirming that prior employments pose no conflicts
 - Specifically inform them NOT to bring/upload information from prior employer

Nondisclosure Agreements

- Have new employee sign a confidentiality and nondisclosure agreement:
- Prior Employment:
 - Has not retained or taken the files/documents/information of the prior company
 - Will not use files/documents/information from the prior company
 - Will not use the trade secrets or confidential and proprietary information of the prior company
- Current Employment:
 - Put an employee on notice regarding the confidential nature of information.
 - Obligation not to use or disclose the information for impermissible purposes.
 - Avoid vague or overly broad language (may not be enforceable).
 - Reasonably identify trade secrets.

Assignment of Inventions

- Assignment of inventions agreements provide that the employer owns any invention created during the course of employment by an employee who is employed to invent
- Provisions to include:
 - Employee discloses prior inventions.
 - Assigns inventions under certain circumstances, even post-termination.
 - Agrees that all original works of authorship are “works made for hire”
 - Agrees that employer has the choice to commercialize or market inventions
 - Agrees to assist with securing intellectual property rights

Assignment of Inventions

- “Work Made For Hire”
- Converts freelancers into employees:
 - Workers’ compensation
 - Unemployment insurance
 - All other purposes?
- California Labor Code §2870
- Limits assignment of inventions
 - Created during non-working time
 - Not using company’s equipment
 - Unrelated to company’s business

Hiring from Other States

- Most states other than California allow non-competition agreements if they are reasonable in scope, and sometimes, if they are designed to protect against illegal or unfair conduct
- If individual is moving from a non-California company or worked outside of California, the former employer may try to enforce the non-compete in a non-California court
- Enforceability of venue selection clauses
- Enforceability of choice of law provisions

Labor Code Section 925

- Effective Jan. 1, 2017 - enacted in response to agreements containing restrictive covenants and foreign choice of law and forum provisions
- Cannot require California employee to agree to employment provision, as a condition of employment, that contains non-California forum or choice of law
 - Exception: If employee represented by counsel for purposes of negotiating the agreement, including the forum and choice of law provisions – not clear if use of exception gets around B&P 16600
- **Mechanix Wear, Inc. v. Performance Fabrics, Inc.** (C.D. Cal. Jan. 31, 2017) 2017 WL 417193: Interpreting section 925 as inapplicable because former employee did not “agree to” forum selection clause while a resident of California

A sepia-toned photograph of a person's hands working on a wooden surface. One hand is placing a puzzle piece into a larger assembly, while the other hand uses a piece of chalk to draw a curved arrow pointing upwards and to the right. The puzzle pieces are light-colored and contrast with the darker wood. A semi-transparent rectangular box with a thin yellow border is centered over the image, containing the title text.

Steps to Protect Trade Secrets During Employment

Protecting Trade Secrets

Identify trade secrets and document how they were created/obtained

Notify employees regarding what the company considers a trade secret

Mark trade secrets as confidential

Periodically perform “trade secrets audit” – identify what information may be protected as a trade secret and put security measures in place

Use firewalls, secure systems, and password-protected files

Use double encryption on databases containing trade secrets

Protecting Trade Secrets

Limit access to trade secrets to those employees who are required to use the information for work purposes

Use carefully drafted non-disclosure agreements

Deploy a “banner” setting forth conditions under which an employee may access the company’s computer system, containing specific language limiting access to information necessary for their job

Monitor employee computer use for trade secrets and confidentiality breaches

Confidentiality reminders and regular training on policies and practices

Email and data security policies

Passwords

A person in a dark suit and striped tie is holding a large, open cardboard box. Inside the box, several black folders and papers are visible. The person's hands are positioned to support the box from underneath. The background is a plain, light-colored wall. The entire image has a warm, sepia-toned filter.

Managing Departing Employees

Protecting Trade Secrets - Duty of Loyalty

- Duty of loyalty prevents departing employee from starting work for new employer until termination of employment
- Employees starting their own business:
 - Can incorporate new businesses while employed, can look for office space, purchase or lease space, and furnish new office
 - Can even hire others and make preparations
 - Cannot start operating the new business until termination
 - **Aerovironment v. Torres** (Cal. Superior Court No. 56-2015-00465460, 2018): Court enforced confidentiality agreements against employees who started competing business before departing current employer; awarded employer \$2.4 million in damages for breach of contract

Policies & Procedures

- Develop process to determine whether employee:
 - had access to trade secret/confidential information; and
 - is likely to take such information or use it at new job
- Develop process to capture relevant information on computers or in emails – preserve the evidence!
 - Metadata
 - Chain of custody
 - Tampering
- Develop process to ensure restriction of access to company systems immediately upon termination
 - Email access
 - Access to company social media
 - Voicemail access

Exit Interviews

- Remind departing employee of obligation to keep information confidential (in accordance with policy, confidentiality or non-disclosure agreements)
- Ask for return of all company property
- Ensure that employee has taken all company data off of personal devices (iPad, cell phone) and social media accounts/cloud server
- Provide directions or assistance regarding how to dispose of confidential information on personal computers

Termination Certificate

- Certify that all company property has been returned
- Confirm that no copies of documents or other items have been provided to third parties
- Acknowledge obligation to keep information confidential
- Signed by the departing employee

Post-Departure Announcements

- Assuming a solicitation can be prohibited (e.g., because it is based on the use of trade secrets), when does a former employee's post-departure announcement to customers or former co-workers amount to a solicitation?
- Generally, simple announcement of new employment is not a solicitation
- Social media
 - Not Solicitation - Invite to connect on LinkedIn
 - Breach of Solicitation Clause – Invitation to request a quote on LinkedIn.

Departing Employees

If theft is suspected or employee is departing...

Disable access

Preserve data destruction/overwrite protocol

Conduct exit interviews

Letter with reminder of NDA obligations

Take swift action against disclosure or misappropriation



Best practice

Best Practices

Best Practices

Agreements

- Be cautious about restrictive covenants
- Use non-disclosure agreements
- Use assignment of inventions agreements
- Beware “work for hire” language for freelancers

Trade Secrets

- Identify & designate trade secrets
- Limit access
- Take steps to keep confidential

Employment Life Cycle

- Upon hire
 - Protect against using others’ trade secrets
- During employment
 - Take steps to establish and protect trade secrets
- Termination of Employment
 - Remind employees of their obligations

Thank You
