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WHITE PAPER

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Massachusetts Noncompete and Trade Secret Reform Will Have Far-Reaching Impact

Businesses across the country are feeling the effects of a pair of laws recently enacted in Massachusetts.

The “garden leave” clause in Massachusetts’ new noncompete law dictates that during the period in which a departed employee is prohibited from working for a competitor, the previous employer must compensate the departed employee by paying at least 50 percent of his or her salary. However, compromise language added to the final version of the law permits “mutually-agreed upon consideration” to be substituted for the garden leave compensation.

Massachusetts’ Trade Secrets Act replaces a six-part test for trade secrets with a statutory definition similar to that of the Uniform Trade Secrets Act (“UTSA”). Notably, under the Massachusetts act, a trade secret must provide actual or potential economic advantage to its owner, in contrast to the UTSA, which in most states requires actual economic advantage.

This Jones Day *White Paper* describes the probable impact of both laws.

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On October 1, 2018, two new laws went into effect in Massachusetts that are already significantly impacting businesses across the country. These new provisions governing noncompete agreements and trade secrets signaled a compromise between the Massachusetts emerging high-tech culture and more established industries, which have been battling over legislative reform for years.

NEW NONCOMPETE PROVISIONS

The new law on noncompetes, Massachusetts Gen. Laws ch. 149, § 24L, replaces a set of standards that were developed over the past few decades in Massachusetts courts. It imposes significant new requirements on noncompetes in employment agreements¹ and no doubt will have an impact on employment practices beyond the Massachusetts border.

Under the law, noncompete obligations entered into after October 1, 2018, must be in writing and must be provided to new employees on the earlier of the formal offer of employment or 10 business days before the employee starts work. A noncompete that is entered into after the commencement of employment but not in connection with a separation from the company must be provided at least 10 business days before it becomes effective. And in a significant departure from existing Massachusetts law,² it must be supported by “fair and reasonable consideration” separate and apart from continued employment.

In circumstances where the noncompete is merely being extended into a new contract year, it is not evident that additional consideration will be required. Moreover, the law does not provide any guidance on what may be considered fair and reasonable when new noncompete obligations are imposed on employees, but it is possible that nonmonetary consideration, like additional vacation days or accelerated vesting of other benefits, may be enough.

The most heralded change in the new law is a requirement that noncompetes include a “garden leave” clause, under which employers agree to pay departed employees at least half of their highest annualized base salary (exclusive of any bonuses or commissions) over the preceding two years.³ A last-minute compromise in the law added an exception for the provision of garden leave if the employee and employer agree to specific alternative consideration, which must be specified in the

noncompete agreement. The statute does not provide any guidance on the magnitude or scope of the alternative consideration. For example, it may be that nominal consideration of \$10, if accepted by both the employer and the employee, may be an enforceable alternative to garden leave.⁴ Another alternative may be that the employer and employee agree in advance to a formula for calculating a lump-sum severance payment in lieu of garden leave.

Under the new law, noncompetes are presumptively valid when the employer’s interests cannot be protected by a nonsolicitation agreement or a nondisclosure agreement, and they generally must protect at least one of the following: employer trade secrets, employer confidential information that does not qualify as a trade secret, or the employer’s goodwill. These provisions mirror existing case law in Massachusetts,⁵ and Massachusetts businesses already have some guideposts interpreting what they mean. For example, protection of an employer’s goodwill is more likely to arise in circumstances where the competing company to which an employee would go is in the same market (i.e., sells the same products or services) as the employer. A Massachusetts federal court recently held that when a salesperson left one company to work for another that had overlapping customers, the first employer’s goodwill was at risk and merited enforcement of a noncompete.⁶ Likewise, it is accepted that confidential information that does not qualify as a trade secret has to be something more than general skill or knowledge acquired during the course of employment.⁷

Noncompetes in Massachusetts are now limited to no more than one year, though they can be extended to as long as two years in the case of theft or breach of fiduciary duty, and can extend geographically only to areas where the employee provided services or had a material presence or influence in her last two years of employment.⁸ Yet even if a noncompete is extended beyond one year, the garden leave requirement is limited to one year.

Under the new law, employers cannot enforce noncompetes if employees are terminated without cause or are laid off.⁹ In addition, employees who are classified as nonexempt under the Fair Labor Standards Act, 29 U.S.C. §§ 201–219, cannot be held to noncompetes. Because noncompetes entered into in connection with a separation are excluded from the law, employers can continue to impose noncompete obligations

in exchange for severance, provided the employees are given seven days to rescind the agreement.

Finally, notwithstanding anything to the contrary in the employment agreement, actions to enforce an agreement against an employee who lived in Massachusetts for at least 30 days before termination must be brought in the Massachusetts county where the employee resides, although the parties can expressly agree in advance to venue in the Superior Court in Boston. Employers in other states whose employees may relocate to Massachusetts during their tenure should take care to ensure that their noncompetes comply with the law, which expressly overrides any choice-of-law provision for employees who live in Massachusetts for at least a month before their employment ends.

NEW TRADE SECRET LAW

Massachusetts' first Trade Secrets Act became effective on October 1, 2018, as well, leaving only New York without such a statute. The statute rejects a decades-old six-part test for trade secrets, borrowed from the 1939 Restatement of Torts,¹⁰ and replaces it with a statutory definition that is similar to the definition in the Uniform Trade Secrets Act ("UTSA").¹¹

Under the Massachusetts act, a trade secret must provide actual or *potential* economic advantage to its owner, in contrast to the UTSA, which in most states requires actual economic advantage. This change may signal the end of the "continuing use" doctrine, under which Massachusetts courts have recognized only continually used processes or ideas as susceptible of protection.¹²

Under this formulation, negative trade secrets were often not protected. For example, while a successful manufacturing process was clearly protected, knowledge about what steps or mechanisms should be avoided was less clearly protected because, by definition, they were not in use. Likewise, innovations made but not immediately commercialized might not have previously been protected, but they are more clearly protected under the new statute.

Another important feature of the new trade secret law is the potential adoption of the "inevitable disclosure" doctrine. Until now, Massachusetts courts have not recognized the doctrine,

citing its potential for curtailing employment opportunities even without a noncompete. The new law not only protects against actual trade secret misappropriation, but also protects against threatened misappropriation, a feature that may signal a recognition that there are circumstances where an employee cannot work at a competitor without—even unknowingly—disclosing trade secrets, and that such circumstances merit protection for the employer.

At least one court has held that the requirement of "actual or threatened" misappropriation is distinct from the inevitable disclosure doctrine, because the former requires actual proof while the latter is based on an inference that disclosure cannot be avoided.¹³ Still, businesses that hire employees who may have had access to trade secrets at their former employers should try to ensure that new hires are not put in a position where they might inadvertently disclose something confidential.

Until now, trade secret misappropriation claims were virtually always accompanied by claims (and counterclaims) under the Massachusetts Consumer Protection Act, chapter 93A, which also covers unfair business practices between two businesses. Under the new law, such actions are unnecessary and are probably preempted. Instead, the Massachusetts act allows for double damages for "willful and malicious misappropriation" and provides that in cases of bad faith, the prevailing party may recover its attorney's fees. No other statute in Massachusetts contains such a fee-shifting feature,¹⁴ and its inclusion in this statute likely signals a desire to avoid curtailing consumer protection claims, which are often regarded by judges as being brought simply as a matter of course.¹⁵

Like most state trade secrets acts, the Massachusetts act requires that a plaintiff must "state with reasonable particularity" the circumstances of the misappropriation, including the nature of the trade secret and the basis for its protection. In addition, before a plaintiff can even begin discovery, it must identify the trade secret with "sufficient particularity ... to allow the court to determine the appropriate parameters of discovery" and to enable the opponent to prepare a defense. The statute appears to have been modeled on a California provision, Cal. Civ. Code § 2019.210, which likewise requires identification of a trade secret with reasonable particularity before discovery commences. But unlike its California counterpart, which has spawned a significant body of case law when the parties disagree about whether a trade secret is sufficiently

defined, the Massachusetts version suggests that in actions brought under it, the court must be actively engaged with the plaintiff before it is permitted even to serve discovery. Such a process would be unique to Massachusetts and might result in fewer published decisions to serve as guideposts.

Together, these two features of the Massachusetts economic development bill will have a significant impact on companies in Massachusetts. While the noncompete law arguably enhances employee mobility, especially for employees who are not terminated for cause, the Trade Secrets Act's new, more explicit protections should provide employers with some assurance that employees will not be free to assist competitors unfairly.

LAWYER CONTACTS

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ENDNOTES

- 1 The law does not apply to noncompete agreements unless they are made in connection with an employment agreement. Agreements not to solicit customers or employees, agreements made in connection with the purchase or sale of a business, and noncompetes entered into in connection with cessation of employment (provided an employee is given a seven-day rescission right) are not covered by the requirements of the new statute.
- 2 *Economy Grocery Stores Corp. v. McMenemy*, 290 Mass. 549, 552, 195 N.E. 747 (1935) (covenant not to compete signed 18 months after defendant began working for plaintiff as at-will employee "was not void for lack of consideration" because "it implied ... a promise on the part of the plaintiff to employ the defendant" thereafter); *ABM Indus. Grps., LLC v. Palmarozzo*, 34 Mass. L. Rptr. 217 (Super. Ct. 2017) ("Continued at-will employment is sufficient consideration to support a noncompete agreement in Massachusetts, just as it is sufficient consideration to support other contractual terms.").
- 3 Even if a noncompete extends longer than a year because of theft or breach of fiduciary duty, the garden leave requirement terminates after a year.
- 4 Bob Salsberg, Associated Press, "'Garden' Clause in New Law Requires Pay During Noncompete," Sept. 30, 2018.
- 5 *Boulanger v. Dunkin' Donuts Inc.*, 442 Mass. 635, 641, 815 N.E.2d 572 (2004).
- 6 *New England Controls, Inc. v. Pilsbury*, 2018 WL 3150223, at *8 (D. Mass. June 27, 2018) (granting temporary restraining order).
- 7 *Dynamics Research Corp. v. Analytic Sciences Corp.*, 9 Mass. App. Ct. 254, 267, 400 N.E.2d 1274 (1980).
- 8 The law leaves some room for other reasonable geographic considerations but notes that limitations consistent with these are "presumptively reasonable."
- 9 Noncompetes are also unenforceable against minors or full-time students who are employed as interns or in other short-term engagements.
- 10 *Jet Spray Cooler, Inc. v. Crampton*, 361 Mass. 835, 840, 282 N.E.2d 921 (1972).
- 11 The term "trade secret" as used in the statute now "means and includes anything tangible or intangible or electronically kept or stored, which constitutes, represents, evidences or records a secret scientific, technical, merchandising, production or management information, design, process, procedure, formula, invention or improvement." Mass. Gen. Laws ch. 266, § 30(4).
- 12 *J.T. Healy & Son, Inc. v. James A. Murphy & Son, Inc.*, 357 Mass. 728, 736 (1970) ("A trade secret is a process or device for continuous use in the operation of the business.").
- 13 *Whyte v. Schlage Lock Co.*, 125 Cal. Rptr. 2d 277, 291 (Ct. App. 2002).
- 14 The Consumer Protection Act, Mass. Gen. Laws ch. 93A, § 11, permits recovery of fees by a successful plaintiff, but not by a successful defendant. Mass. Gen. Laws ch. 231, § 6F, allows a party to obtain an award of fees and costs upon a finding that its opponent's arguments "were wholly insubstantial, frivolous and not advanced in good faith," but this statute is rarely applied.
- 15 E.g., *Instrument Industries Trust v. Danaher Corp.*, 2005 WL 3670416, *7 (Mass. Super. Ct. Nov. 28, 2005) ("Count IV is the ubiquitous c. 93A claim that appears so frequently in complaints before this Court.").

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