Top Five Non-Compete and Trade Secret Issues to Watch for in 2011

Insights
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1. Texas Supreme Court Decision: Can Money Serve as Consideration for a Non-Compete?

In April of 2010, the Texas Supreme Court agreed to review an appellate court decision that will require the Court to answer the following question: Can money serve as consideration for a non-compete? In Marsh USA v. Cook, a high level employee received stock options in exchange for a signing a non-compete. After the employee left, the employer attempted to enforce his restrictive covenants and failed. Why? In simple terms, Texas has a statute governing non-compete agreements. The statute says restrictive covenants must be ancillary to an otherwise enforceable agreement at the time the agreement is made, and the otherwise enforceable agreement must give rise to the need for protection. What does that mean? It seems a lot of courts and lawyers in Texas have been asking the same question. For example, suppose an employer promises to provide an employee with confidential customer information, but requires the employee to agree not to solicit clients. Various Texas cases find this to satisfy statutory requirements. The employer has made "an otherwise enforceable agreement" – an agreement in which it obligates itself to provide the employee with confidential information – and at the time the agreement is made, the employee executes a restrictive covenant that is ancillary to the "otherwise enforceable agreement" which gives rise to the need for protection. In Marsh USA, the employee argued that providing stock options did not give rise to a need for a restrictive covenant. In response, Marsh argued that such a holding is hostile to economic development and that employers should be able to protect goodwill that exists in the form of customers relationships. The Texas Supreme Court accepted the case in early April 2010. Perhaps a decision will be issued in 2011.

2. California Clarity on Trade Secrets Exception

In 2008, the California Supreme Court addressed the 'narrow restraint' exception to enforcement of non-competes in California. Specifically, in Edwards v. Arthur Andersen LLP, the California Supreme Court rejected the argument that California's statutory proscription on non-competes only applies to restraints that totally prohibit an employee from engaging in his or her profession. Prior to Edwards, some courts held that a restrictive covenant was permitted if it contained a mere limitation on an employee's ability to compete. The Court expressly stopped short of addressing the validity of what it termed the "so-called trade secret exception" in which California courts permit contractual

restrictions that are "necessary to protect an employers' trade secrets." Look for California appellate courts to address this ongoing issue in 2011.

3. Computer Fraud & Abuse Act: A Split Among the Circuits

In recent years, there has been an ongoing debate within the judiciary over whether the federal Computer Fraud & Abuse Act applies in the context of a faithless employee. Namely, some federal courts question whether the CFAA applies to a faithless employee's misappropriation of his or her employer's confidential information or trade secrets by means of the employer's computer, to which the employee had authorized access as a result of his or her employment. On this legal issue, there is a continuum of interpretations of the CFAA within the federal judiciary. Some district and appellate courts hold that the CFAA gives employers a federal cause of action against their disloyal departing employees, in what has been perceived as a pro-employer interpretation. On the other end of this continuum are what would appear to be employee-favorable opinions holding that the CFAA does not create such a right in employers. As the federal circuits line up on each side of this issue, it is reasonable to assume the issue will be pressed on appeal at some point. 2011 seems as good of a time as any to do so.

4. Non-Compete Legislation to Resurface in Massachusetts

Much was written about the non-compete bill working its way through the Massachusetts legislature in 2010. In March of 2010, the bill was favorably reported out of committee and, on May 25, 2010, it was submitted to the Judiciary Committee for its consideration. Later in the year, it was attached to an economic development bill, and then removed. Look for the bill to be reintroduced in 2011.

5. Social Media Issues Gain Traction

In a sobering reminder that online social media is changing the way many companies do business in unforeseen ways, a federal court shot down an employer's trade secret claim in 2010 based largely upon the availability of information via the internet. In Sasqua Group, Inc. v. Courtney, a magistrate judge for the United States District Court for the Eastern District of New York held that although an employer's customer list may have been a trade secret years ago, "the exponential proliferation of information made available through full-blown use of the Internet [presents] a different story." The district court subsequently adopted and approved the magistrate's lengthy and detailed opinion. Others have debated the extent to which non-solicitation agreements and other restrictive covenants apply to conduct undertaken by employees through online social media, such as post-employment communications with clients through sites such as LinkedIn. As online social media spreads in popularity and usage, look for more and more courts (and commentators) to address this interesting issue.

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