THE FUTURE OF "NO POACH" CLAUSES: PRACTICAL ADVICE AND VIEWPOINTS FROM THE EMPLOYMENT AND ANTITRUST PERSPECTIVES

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JO: Bill [Sailer], you are working inside a major tech company. Have you seen a significant change in corporate awareness or attitudes about no-poach clauses since government and private litigation around these clauses has increased in recent months?

WS: Absolutely! What for many years was a common practice for companies who were wary of exposing their employees to potential suitors is now something that carries significant risk and has to be evaluated carefully. The challenge for a company is that it intuitively seems appropriate to engage in these agreements in certain circumstances; thus, individual managers may not understand the risks of these arrangements and may fail to seek out legal advice before taking any steps in that regard. It can get frustrating to have a business relationship with another company, only to have them lure your employees to work for them, after learning who are the strong performers. Nonetheless, besides presenting legal risk, a simple "no-poach" approach is probably not the most effective way to retain the at-risk employees in any event.

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JO: That is a good point, Bill. Setting aside the legal risks of these agreements, they are not likely to garner goodwill with employees, and instead might send a message of distrust. It is key for outside and inside counsel to work with their clients on how to simultaneously protect intellectual property vigorously, which is obviously key for companies like Qualcomm, while avoiding undue and risky restraints on employee mobility. Dina and Rod, does your experience comport with Bill's?

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> Bill Sailer

DH: To some extent, yes. Larger U.S. companies interacting more regularly with antitrust counsel are aware of these developments, but many smaller companies and companies not based in the U.S. are less aware of what has been happening in the no-poach arena. In my experience, all companies have been eager to better understand these developments once they become aware of them, so I always make sure to raise these issues with new clients, even when they're coming to me on completely unrelated topics.

RS: There is no question that the increased scrutiny of no-poach agreements in recent years has caused companies to be aware of the issue. This increased awareness began after the DOJ's lawsuit against the high-tech companies and has continued as a result of the issuance of the October 2016 DOJ & FTC Guidelines for HR Professionals. In the past, HR departments were not seen as a likely source of antitrust conspiracies, so they were not the focus of antitrust compliance training. That has changed and companies appear very aware of the potential issues in this area and are taking steps to address them.

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In the wake of the issuance of the guidelines in 2016, there have been many class actions filed claiming companies entered into unlawful no-poach agreements. All of this activity has put the potential issues related to no-poach agreements on the radar for companies. In that sense, the goal of the DOJ and FTC in issuing the guidelines has been satisfied – companies are now focused on these types of agreements in a way they were not before. But by asserting that "naked" no-poach agreements are per se unlawful, the guidelines may have emboldened the plaintiffs' bar more than intended.

In fact, in March of this year, the DOJ filed a statement of interest in three related class actions involving alleged no-poach clauses in franchisor-franchisee agreements. The DOJ tried to clarify that no-poach agreements between a franchising parent company and its franchisees are vertical agreements that may have pro-competitive benefits rendering per se treatment inappropriate. We will have to see if this clarification from the DOJ slows the tide of no-poach class actions alleging these types of agreements to be per se unlawful. Obviously, such cases would be much more difficult if a rule of reason showing were required.

JO: Thanks Rod, I am sure you are not surprised to hear that the plaintiffs' bar has been watching those cases closely. But as you point out, the potential rule of reason treatment, applies only to vertical arrangements for example franchisor to franchisee, and not agreements between horizontal competitors like we saw in the high-tech industry a few years ago. And, as you also correctly stated, the so-called "rule of reason" standard does not bar a finding of illegality; it only requires a more detailed showing of unreasonableness, whereas a "per se" treatment makes the clause illegal on its face with no further inquiry.

Jim, as an employment lawyer perhaps you have a different perspective than the antitrust or in-house lawyers on this panel. Have you had a similar experience regarding your clients' awareness of this issue?

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>
> Dina Hoffer

JM: Yes, I have seen significant changes in both corporate awareness and attitudes in recent months and years. The big wake-up call on this came in 2016 when the Department of Justice announced that it would proceed criminally against naked no-poach agreements. That announcement got a lot of people's attention, and as Rod noted, the attention continued when the Department of Justice and Federal Trade Commission issued its "Antitrust Guidance for Human Resource Professionals." Over the last 12 months, state attorneys general continued to shine the spotlight on this issue by pursuing enforcement actions against companies based on their use of no-poach clauses, mostly in franchise agreements. In addition to the significant government action in this space, the plaintiff's bar has been very aggressive in bringing lawsuits challenging no-poach agreements across the country. As a result of this attention, companies have become increasingly aware of the risks of using no-poach clauses and have become more careful in their use of no-poach clauses.

JO: And Bill [Whelan], you are also on the employment side, and as I understand it you recently prevailed in a case that provided significant clarity about the legality of no-poach clauses in California. Can you tell us about what you learned there?

WW: That's right, Jennifer. Companies are, of course, still entitled to protect their trade secrets and proprietary information through reasonably drafted confidentiality or non-disclosure agreements. However, in California at least, the names of employees, their contact information, and their pay rarely qualify as legitimate trade secrets.

In general, it is a mistake for California employers to try to bar former employees from recruiting or soliciting their former co-workers. Prior to 2008, no-poach agreements were defensible based on case law. Starting in 2008, however, the California courts issued a series of rulings that called the enforceability of no-poach agreements in California into question. In our case, AMN Healthcare v. Aya Healthcare Services, the court's decision made it clear that no-poach agreements are unlawful, void, and unenforceable restraints of trade under California statutory and common law. Simply having these provisions in their contracts exposes employers to liability under California's Unfair Competition Law.

JO: So then, how, if at all, have you changed your advice to clients in the wake of the Aya case?

WW: While I would tell clients such as employment agencies that they should not have no-poach agreements with their employees, in order to protect themselves, they can have provisions in their contracts with their clients to obligate the client to reimburse them for the costs of recruitment and training if the client hires away employees within specified time frames. Those types of provisions are not no-poach agreements but are more akin to placement or finder's fees.

California courts have upheld reasonably drafted provisions along these lines because the provisions do not restrain trade or interfere with the free mobility of employees. Rather, they are simply contractual

recognitions of the expenses incurred by temp agencies, which the client agrees to reimburse if the client hires away an employee. With limitations, staffing agencies can also protect their customer and applicant lists as trade secrets under relevant trade secret statutes.

JO: That's quite interesting, Bill. One must wonder, however, whether an arrangement to reimburse recruitment and training costs in an agreement between two directly-competing employers would be upheld. While it may not necessarily prohibit an employee from changing firms, it does allow a competitor to increase its rivals' recruitment costs and increase the likelihood that employees will "stay put," which in turn serves to suppress wages. Dina and Rod, given recent trends, do you or would you counsel your clients to continue to use no-poach clauses in their agreements under certain circumstances, for example to protect trade secrets known by a narrow set of executives or high level engineers, or is it simply too risky to use them at all?

RS: Depending on a company's tolerance for risk and on the particular circumstances, it may make sense to use a no-poach clause in an agreement. As has been mentioned, the guidelines state that the DOJ and FTC will treat "naked" no-poach agreements among competing employers as per se unlawful, although they make exception for any such agreements that are reasonably necessary to a legitimate collaboration among employers. There are circumstances where a no-poach agreement should be viewed as pro-competitive and necessary even where there is not a formal joint venture. For example, the guidelines specifically reference joint ventures as the type of legitimate collaboration in which no-poach agreements should not be viewed as per se unlawful. Another example might be where a company hires a vendor to come onto one of its sites to perform a service. A no-poach clause in the contract preventing the company from poaching the vendor's employees who visit the site to perform that work would seem to be legitimate if it were drafted in such a way as to be narrowly tailored to cover only the employees who visit the site. But, again, while there would be a good argument for a no-poach clause being reasonable in that type of circumstance, it would be up to the company whether to assume the risk that such a provision would be deemed per se unlawful if challenged in court. Even in situations where no-poach agreements are appropriate, it is important to make sure that they are not any broader than necessary to accomplish their legitimate purpose.

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> Jim McQuade

DH: I generally agree with Rod. I do believe that clients can still safely employ no-poach agreements that are ancillary to legitimate business collaborations with competitors when they are very carefully drafted and narrowly tailored. However, given the current climate surrounding no-poach agreements, companies should consider using agreements between the employer and employee rather than between two employers if possible. Non-solicitation provisions entered into with employees are generally enforceable if they serve a legitimate business purpose and are not overly broad or burdensome. For example, companies could incorporate employee non-solicitation clauses into severance agreements or offer signing bonuses conditioned on a certain period of employment. These types of transparent limitations that are agreed to by higher level employees and tied to some sort of additional compensation do not raise the same antitrust concerns that no-poach agreements between two employers raise.

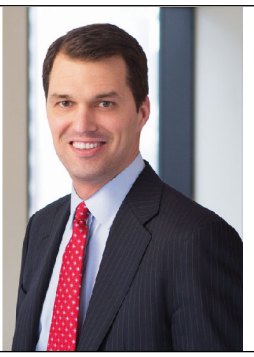
JO: Thanks Dina, the severance and signing bonus suggestions are thought-provoking in that they could replace a potentially anticompetitive agreement with rivals with an incentive agreement with the employee herself. I would note that, at least in California, where non-competes are not enforceable unless tied to equity transfer, those methods would not likely survive a challenge under the unfair competition law. Jim, do employment attorneys share that perspective?

JM: I would continue to counsel clients to use no-poach clauses under appropriate circumstances. I often see no-poach clauses proposed as one term of a settlement agreement in an employee raiding case or in a case involving breaches of employee non-solicitation provisions. In these types of cases, the employer may continue to properly use no-poach provisions, given the appropriate circumstances and provided the provisions are properly drafted. I do not think that the use of these provisions in this context is so risky that they should not be used at all.

JO: This appears to be a delicate balance. No poach clauses are risky, but most of you would not necessarily counsel a client that they can never use them. So Bill and Bill, how would you articulate the real business advantages and perils of these types of clauses when presenting a risk/benefit analysis to a hypothetical Board member or C-Suite executive of your company or of one of your clients?

WS: Given the guidance from the California Supreme Court, the Department of Justice, and the Federal Trade Commission, the risks are relatively plain, and sophisticated business leaders understand that attempting to enforce unenforceable obligations can boomerang into a bigger problem for the company.

orrick



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To the extent that the Company is concerned about losing key employees or allowing important information or intellectual property to walk out the door, then I would advise to focus on other, more enforceable methods to protect the company's interests. This ranges from IT monitoring and security strategies, to treating employees with dignity and respect, even when leaving for a competitor.

Finally, educating employees about their obligations as a departing employee of the company – to protect the company's confidential information and to respect their confidentiality agreements, goes a great way towards ensuring that there are no unintentional leaks.

WW: The value of no-poach agreements has always been limited in the real world. The usual argument in favor of them was that they deter some employees from recruiting their former colleagues, even if the company never intended to try to enforce them. The argument was that many employees would not consult competent counsel and would therefore assume that the provision was enforceable. In practice, that only seemed to be true in situations which did not truly matter to the company.

No poach agreements are often ignored by employees who correctly predicted that they were unlikely to be sued. Furthermore, it was simple to manufacture evidence and get around the no-poach agreement by simply documenting that it was the departing employee who initiated the contact with the new company, rather than the other way around. Even the early decisions did not enforce "no hire" agreements, only recruitment initiated by the former employee towards former co-workers was barred.

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Bill Whelan

Recent cases and Department of Justice guidance illustrate the risks of continuing to use no-poach agreements. The company is exposed to antitrust and state unfair competition law lawsuits, which can end with the company having to pay for both sides' attorneys' fees. As Bill noted, employers have always had, and continue to have, valid and enforceable ways to protect legitimate interests such as trade secrets and confidential information. Companies can also compete the old-fashioned way for employees, by ensuring that their valued employees are happy with their pay, working conditions, opportunities for professional growth and advancement, benefits, and so on. That is a much more effective and economical way to compete for talent than through litigation based on no-poach agreements.

JO: Bill [Sailer], you work for Qualcomm, where I think it is safe to assume that protecting IP is at the top of the C-Suite's list of priorities. Do you agree that no-poach agreements are appropriate in certain circumstances, especially where IP is involved?

WS: As with all good legal questions, the answer to this one is, "it depends." One important question to ask is whether or not no-poach agreements truly protect IP. While they may make it more difficult to identify strong performers at a company in order to lure them to a new company, IP protection largely rests upon a company having strong processes in place to protect their confidential information, as well as a strong culture of integrity. Also, to the extent that no poach agreements drive the recruitment and hiring process "underground," it may make it more difficult to protect IP than with situations where employees feel free to be more transparent about potential moves to other companies.

JO: That makes perfect sense Bill, look to the root of the problem, so to speak. Many defend the use of these clauses to protect IP, but in reality, that may not be effective and in fact may be mere pretext. That is, sometimes these agreements are entered into with the intent to suppress wages, rather than protect any valuable company property.

Plaintiffs alleged just that in In Re Animation Workers Antitrust Litigation, which Rod litigated. There, plaintiffs alleged that the competitor defendants agreed to adhere to set salary ranges in order to suppress the wages of a limited and highly skilled set of employees. Rod, in the wake of that case, would you advise your clients never to exchange salary information with competitors? Or do you limit that prohibition to an explicit agreement to adhere to a certain salary or range? Does the industry/labor pool at issue need to be considered?

RS: Companies should make every effort to comply with the safe harbor provision of the DOJ healthcare guidelines on the exchange of information, which generally require data to be historical and sufficiently aggregated so that any particular company's information cannot be discerned. Sharing salary information, just like sharing pricing information, directly among competitors should be avoided, as it could lead to an inference of an agreement to set salaries. This would apply regardless of the industry involved. Companies can rely on publicly available information or on industry surveys that meet the criteria set forth in the DOJ healthcare guidelines.

JO: Thanks Rod. Changing gears a bit, I want to discuss the interplay of no-poach and M&A. I recently worked on a matter where a

purchaser in a merger transaction came across potentially illegal no-poach agreements in the diligence process, and it ultimately cratered the deal. The seller had entered these agreements at his competitors' request as part of a potential joint venture and was not even aware there was any legal issue surrounding them. Unfortunately, the clauses were much too broad, and it ultimately cost him the acquisition of his company. In your experience, do counsel in an M&A deal look for no-poach clauses in due diligence when identifying issues and risks, and should they?

> "One has to wonder, however, whether an arrangement to reimburse recruitment and training costs in an agreement between two directly-competing employers would be upheld. While it may not necessarily prohibit an employee from changing firms, it does allow a competitor to increase its rivals' recruitment costs and increase the likelihood that employees will "stay put," which in turn serves to suppress wages."
>
> Jennifer Oliver

RS: Given the increase in litigation over these kinds of agreements, some of which has led to large settlements, it would be prudent to review for no-poach clauses when reviewing contracts as part of due diligence.

DH: This is certainly an issue that deserves consideration in the merger context. It's important to note that the DOJ's 2016 guidance makes clear that only "naked" no-poach agreements would be considered criminal and per se illegal. "Naked" no-poach agreements are those that are not considered reasonably necessary to legitimate business collaborations. No-poach agreements that are considered reasonably necessary to legitimate business collaborations, which can include mergers, are analyzed under the rule of reason and may very well be upheld by a court. That said, even when reasonably necessary to a legitimate business collaboration, no-poach agreements should be very carefully drafted and narrowly tailored such that they are in clear furtherance of the collaboration at issue and limited in scope and duration.

JO: Dina, in sum, isn't the elimination of no-poach clauses important in maintaining employee mobility and free competition?

DH: I don't think it's fair to say that eliminating no-poach clauses is necessary to maintain employee mobility and free competition across the board. There are situations in which these types of agreements provide pro-competitive benefits and efficiencies to the market that can justify their continued existence. For example, in situations where a joint venture or settlement agreement would not exist without a no-poach clause, the market can benefit from these types of agreements.

JO: Well, it seems the consensus among the group is that employer-employee agreements may have some traction, whereas competitor to competitor agreements do not. But, from an employment law perspective, even employer-employee agreements that restrict employee mobility have risks, particularly in California if they do not comply with the letter and spirit of Code 16600. And in any event, it also sounds like many on this panel believe that these clauses have limited value. I agree and would argue that they are detrimental to employee mobility and hamper wage competition, allowing companies to keep wages low and avoid paying a fair market price for talent, especially where there is a limited talent pool in a specialized industry. We'll be watching business practices, agency policies, and litigation trends in this area carefully for sure.

Thank you all, this has been a fascinating conversation!

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