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California Broadens Restrictions on Employee Non-Competes

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Starting January 1, 2024, California will be broadening its already expansive prohibitions on employee non-compete agreements. Senate Bill (SB) 699, signed into law on September 1, 2023, added Section 16600.5 to the Business & Professions Code, which expands California's existing restrictions on non-competes to agreements created out-of-state and creates new enforcement rights for employees to challenge non-compete clauses.

California's Business and Professions Code section 16600 currently voids contracts that restrain an employee from engaging in a lawful profession, trade, or business of any kind. State courts have historically applied Section 16600 to bar agreements made in California restricting post-employment competition, with limited exceptions.[1]

Section 16600.5 will prohibit enforcement of any contract previously forbidden under Section 16600 "regardless of where and when the contract was signed." Plaintiffs may capitalize on this broad phrasing to argue that the new law should apply retroactively to *any* contract with non-compete provisions, and courts will likely have to clarify whether California's presumption against retroactivity applies.[2] The new law will further bar "an employer or former employer from attempting to enforce a contract that is void regardless of whether the contract was signed and the employment was maintained outside of California."[3] Employers that enter into a contract that is void or attempt to enforce a contract forbidden by Section 16600 will have committed a civil violation. The expanded restrictions are intended to (i) respond to an increasingly remote talent market, in which "California employers increasingly face the challenge of employers outside of California attempting to prevent the hiring of former employees"; and (ii) to preserve the state's "competitive business interests" by "protecting the freedom of movement of persons whom California-based employers wish to employ to provide services in California, regardless of the person's state of residence."[4]

It remains to be seen how broadly Section 16600.5 will apply in practice, and whether jurisdictional challenges may limit its effect within and outside California. For example, employees who recently moved to California may cite Section 16600.5 in California courts to try to invalidate non-competes that they previously agreed to, even if such clauses were legally negotiated out-of-state with a non-California employer. Alternatively, remote workers employed in other states by California employers may try to invoke the provision in their local jurisdictions to invalidate non-competes formed outside of California, even if the employee never set foot in California. Of course, this raises the question of whether a non-California court will find Section 16600.5 to apply to an employee outside California. Section 16600.5 also raises the question of whether a California court has the authority to rule a non-compete is unenforceable even if the agreement complies with the law of the state in which it was made or has already been held enforceable by a non-California court. Employers should monitor whether and to what extent courts apply judicial principles of comity and extraterritoriality in adjudicating these types of cases.[5]

Employers should also be aware that the law authorizes employees, former employees, and prospective employees to seek injunctive relief, actual damages, or both, and entitles a prevailing plaintiff to recover reasonable attorneys' fees and costs. But employers who

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prevail in litigation over restrictive covenants are not entitled under the new law to recover their fees against the losing individuals. Employers with ties to California are encouraged to review their employee agreements in light of this new law.

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[1] Statutory exceptions to Section 16600 include restrictive covenants in the sale or dissolution of corporations, partnerships, and limited liability corporations. *See* Cal. Bus. & Prof. Code §§ 16601, 16602, 16602.5.

[2] Cal. Civ. Code, § 3; *Evangelatos v. Super. Ct.*, 44 Cal. 3d 1188, 1208 (1988) (holding that a statute will not be applied retroactively unless it contains "an express retroactivity provision" or it is "very clear from extrinsic sources that the Legislature . . . must have intended a retroactive application").

[3] 2023 Cal. S.B. No. 699 (2023-2024 Regular Session).

[4] *Id.* §§ 1 (d) & (f).

[5] *See, e.g.*, *Advanced Bionics Corp. v. Medtronic, Inc.*, 29 Cal. 4th 697, 706–07 (2002), *as modified* (Mar. 5, 2003) (applying the comity principle to reason that while "California has a strong interest in protecting its employees from noncompetition agreements" under section 16600, "[a] parallel action in a different state presents sovereignty concerns that compel California courts to use judicial restraint when determining whether they may properly issue a TRO against parties pursuing an action in a foreign jurisdiction."); *Ward v. United Airlines, Inc.*, 986 F.3d 1234, 1240 (9th Cir. 2021) (discussing the breadth of the extraterritoriality principle).

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