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CALIFORNIA COURT OF APPEAL DECISION CREATES UNCERTAINTY REGARDING THE CONTINUED ENFORCEABILITY OF EMPLOYEE NON-SOLICITATION PROVISIONS

A new ruling from a California Court of Appeal calls into question the common wisdom in California that, while non-competes are generally barred, reasonable employee non-solicitation provisions are enforceable.

To Our Clients and Friends:

Earlier this month, in *AMN Healthcare, Inc. v. Aya Healthcare Servs., Inc.*, a California Court of Appeal ruled that an employer could not enforce its employee non-solicit against former company recruiters, after finding that the clause would keep the recruiters from performing their jobs in violation of California Business and Professions Code §16600.[1] For the last 30 years, employers have cited *Loral Corp. v. Moyes* (1985) 174 Cal. App. 3d 268, 279-80, in support of their employee non-solicits under California law—but in *AMN Healthcare*, the Court of Appeal expressed doubt regarding *Loral*'s continued viability. The *AMN Healthcare* Court stopped short of overruling *Loral*, and instead expressly distinguished it, providing employers with the ability to argue that *Loral* may still remain good law. Nonetheless, going forward, employers should carefully consider whether to include employee non-solicits in their employment contracts with California employees.

Employee Non-Solicits Long Viewed as Enforceable in California

Under California law, all employees owe their employer a fiduciary duty of loyalty during their employment. Once the employment relationship ends, however, such duties end automatically and only legally enforceable, contractually-negotiated duties remain. As a result, employers have historically sought to exercise some measure of control over the mobility of former employees by employing three types of post-employment restrictive covenants: (1) non-competes (i.e., clauses preventing former employees from working in the same field or in the same geographic region in which the former employer operates); (2) customer non-solicits (i.e., clauses preventing former employees from soliciting their former employer's customers for their own business purposes); and (3) employee non-solicits (i.e., clauses preventing former employees from soliciting their former employer's current employees for employment opportunities elsewhere).[2]

Subject only to three narrow statutory exceptions,[3] California courts have long held that both non-competes and customer non-solicits are void and unenforceable as against public policy under California Business and Professions Code §16600, which provides "every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void."[4] Likewise,

broad "no-hire" covenants entered into between two business entities (i.e., contractual arrangements between a vendor and a client, etc., to the effect that neither entity will hire individuals employed by the other entity) have also been found to be unenforceable, on similar grounds.[5] In contrast, however, narrowly drawn employee non-solicits *have* historically been viewed as enforceable, ever since *Loral Corp. v. Moyes* (1985) 174 Cal. App. 3d 268, where a California Court of Appeal concluded that employee non-solicits only "slightly" affect employment opportunities, and thus do not constitute unreasonable restraints on trade that run afoul of Section 16600. For more than 30 years now, employers have cited *Loral* as the touchstone decision in support of the proposition that reasonable employee non-solicits remain enforceable.

Indeed, despite several potential challenges under Section 16600 over the years, *Loral* and the employee non-solicit have survived. For example, in *Edwards v. Arthur Andersen LLP* (2008) 44 Cal. 4th 937, the Supreme Court stated that Section 16600 establishes a bright-line "per se" rule, which invalidates any post-employment covenant that has the practical effect of restraining a former employee's ability to work in his or her chosen profession (subject only to the narrow statutory carve-outs noted above).[6] And yet, despite its bright line rule, the Supreme Court did not overrule *Loral*—in fact, the *Edwards* decision actually cites *Loral* approvingly (albeit for an unrelated legal proposition).[7] Likewise, one post-*Edwards* Court of Appeal decision (*Fillpoint, LLC v. Maas (2012) 208 Cal. App. 4th 1170*) reveals similar tension with *Loral*'s reasoning, specifically by striking down a customer non-solicit—but *Fillpoint* did not directly address *Loral* or even the employee non-solicit found in the *Fillpoint* contract. Up until *AMN Healthcare*, no further appellate decisions have addressed the continuing viability of *Loral*; as a result, parties have continued to cite *Loral* as support for the enforceability of employee non-solicits.

***AMN Healthcare* Calls the Employee Non-Solicit into Question**

On November 1, 2018, however, a California Court of Appeal, in *AMN Healthcare, Inc. v. Aya Healthcare Servs., Inc.*, finally issued a published decision that directly addresses *Loral*—finding it factually distinguishable, but also expressing skepticism about its continued viability. The employer in question, AMN Healthcare, Inc. ("AMN"), is a recruiter and provider of temporary healthcare professionals, specifically travel nurses, to health-care facilities. The defendants, several former AMN recruiters, were all required to sign Confidentiality and Non-Disclosure Agreements ("CNDAs") which prevented them from soliciting any other AMN employees for a period of one year following their terminations from AMN. In addition, the CNDAs also required defendants not to disclose confidential information (including information related to customers, marketing and development, and financial information) to third parties. After defendants left AMN to work for competitor Aya Healthcare Services ("Aya"), they solicited AMN travel nurses to join Aya—relying on information that they allegedly learned while working at AMN. AMN brought suit against both the former employees and Aya, claiming violations of the CNDA (including the employee non-solicit) and related torts. The trial court granted Aya's motion for summary judgment after finding that the employee non-solicit within the CNDA was void as against public policy under Section 16600. AMN appealed.

The Court of Appeal affirmed the trial court's decision, holding that the employee non-solicit unlawfully restricted the former AMN recruiters from practicing their chosen profession—i.e., recruiting travel nurses—in violation of Section 16600.

The Court of Appeal stressed that in *Edwards*, the California Supreme Court expressly rejected the Ninth Circuit's "narrow restraint exception" to Section 16600, making illegal only those restraints which *completely* preclude one from engaging in their chosen profession.[8] The *Edwards* Court found that this clearly contradicted both the "unambiguous" language of Section 16600 and California's fundamental public policy in favor of promoting employee mobility.[9] While declining to reject *Loral* outright, the Court of Appeal in *AMN Healthcare* thus noted that *Edwards*, which held that Section 16600 was unambiguous and applied to even narrowly tailored post-employment covenants, cast "doubt [on] the continuing viability of [*Loral*] post-*Edwards*."[10]

Nevertheless, the Court of Appeal expressly recognized that *Loral* is factually distinguishable from *AMN Healthcare*. Unlike a former executive officer's ability to solicit employees (which was at issue in *Loral*), a recruiter's job *necessarily* involves the solicitation of employees. In this way, the non-solicit in *AMN Healthcare* works like a traditional non-compete, by preventing the recruiters from doing their job. The same may not be true (at least to the same degree) with respect to most other types of employees, making AMN Healthcare very unique.[11] And the Court of Appeal also observed that the employee non-solicit period in question in *AMN Healthcare* extended for a full year, even though temporary nursing assignments typically last only 13 weeks. Under the facts of the case, this was held as an unreasonable time restriction—another way in which the *AMN Healthcare* decision may be factually distinguishable from *Loral* (where the restrictive covenant in question was found to be reasonable in both scope and duration).[12]

How Do Employers Make Sense of *AMN Healthcare*?

By distinguishing *Loral* rather than outright overruling it, the *AMN Healthcare* Court left uncertain the ongoing viability of employee non-solicits under California law. This uncertainty is unlikely to be resolved unless and until the Supreme Court of California—which has already had ample opportunity to overturn *Loral*, and which previously declined to do so in *Edwards*—definitively decides the matter.[13] In light of this uncertainty, prudent employers may now wish to reconsider the potential risks and rewards of continuing to include employee non-solicits in future contracts with California employees. For example, although the employer would have strong arguments that the law is, at best, unsettled, plaintiff's counsel might seek to impose liability for the use of an allegedly unlawful post-employment covenant under the California Labor Code, California's Unfair Competition law, or California common law.

On the other hand, employee non-solicits can be an incredibly valuable tool to employers seeking to protect their business from being raided by former employees. Indeed, in emerging technology sectors, among others, qualified, knowledgeable workers may be the employer's most valuable asset. And enforceable non-solicits create a certain level of stability for a company, helping to reduce the risk that the departure of a key employee does not result in a mass exodus of other valuable employees.

[1] *AMN Healthcare, Inc. v. Aya Healthcare Servs., Inc.* (2018) No. D071924, 2018 WL 5669154, at *8.

[2] Employees working in technical fields are also often required to execute invention assignment agreements (i.e., contracts under which the employee is required to disclose and assign to the employer any contributions and inventions relating to the employer's business that were conceived or created during the employment period), and such provisions are generally enforceable under California law. California courts also routinely enforce both post-employment confidentiality and non-disclosure clauses, and California business owners additionally enjoy robust trade secret protection under the California Uniform Trade Secret Act, codified at California Civil Code § 3462, *et seq*.

[3] The three narrow statutory exceptions are carved out under sections 16601-16602.5, which collectively provide that non-compete and employee non-solicitation agreements may be enforceable—if reasonable in scope and duration—against an individual who sells a business; a former business partner; and/or a former member of an LLC.

[4] See, e.g., *Edwards v. Arthur Andersen LLP* (2008) 44 Cal.4th 937, 948-950; *Dowell v. Biosense Webster, Inc.* (2009) 179 Cal. App. 4th 564, 574.

[5] See, e.g., *VL Systems, Inc. v. Unisen, Inc.* (2007) 152 Cal. App. 4th 708.

[6] *Edwards, supra*, 44 Cal. 4th at p. 948.

[7] *Id.* at p. 954.

[8] *AMN, supra*, 2018 WL 5669154, at p.*8.

[9] *Ibid.*

[10] *Id.* at p. *9.

[11] *Id.* at p. *8.

[12] *Loral, supra*, 174 Cal. App. 3d at p. 279.

[13] *Edwards, supra*, 44 Cal. 4th at p. 954.

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Gibson Dunn lawyers are available to assist in addressing any questions you may have about the AMN Healthcare decision, and in evaluating the risks and benefits of inserting non-solicits in future employment contracts with California employees. Please contact the Gibson Dunn lawyer with whom you usually work or the following Labor and Employment practice group leaders and members:

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