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Alert | Emerging Technology/Labor & Employment

February 2019

Impact of New Massachusetts Noncompete Law on Emerging Tech Companies

The Massachusetts Noncompetition Agreement Act, M.G.L. c. 149, § 24L, has been the law of the Commonwealth for almost four months. The statute only applies to agreements entered into between employers and certain employees and independent contractors on or after Oct. 1, 2018, so the law's ramifications are still largely yet to be determined. Nevertheless, even in the short time the law has been operative, its implications for emerging technology and start-up companies have been significant.

The Push for Change Leads to Legislative Compromise

Many employees and even some employers had been clamoring for changes to the Massachusetts non-competition laws for some time. Critics of non-competition agreements have argued that the state of the law impeded innovation and did not adequately protect the interest of employees. Many from the start-up and venture capital community pushed for non-competition law reform, contending that employee mobility is critical to the freedom to innovate.

On the other hand, many employers and industry groups supported maintaining the status quo of non-competition law, or even favored stricter non-competition laws, citing their importance in guarding against the theft of intellectual property and confidential, proprietary information, also critical to incentivizing innovation.

In the end, the legislature reached a compromise providing both sides some, but not all, of what they wanted.

What Emerging Tech Companies Need to Know

Requirements for Entering Into a Valid Non-Competition Agreement

If entered into before employment, a valid non-competition agreement must now:

1. be in writing;
2. be signed by the employer and the employee;
3. expressly state that the employee has the right to consult with counsel prior to signing; and
4. be provided to the employee by the earlier of a formal offer of employment or 10 business days before the start of the employment.

If entered into *during* employment, a valid non-competition agreement must:

1. be in writing;
2. be signed by the employer and employee;
3. expressly state that the employee has the right to consult with counsel prior to signing;
4. notice must be provided to the employee at least 10 business days prior to its effective date;
5. be supported by fair and reasonable consideration independent from continued employment.

Scope, Duration, and Enforceability

The duration of the non-compete cannot exceed 12 months from the date employment ended. As was previously the case, a non-compete restriction can only protect a legitimate business interest (such as trade secrets, confidential information, goodwill).

The new law also makes a non-compete "presumptively reasonable" where the geographic scope is limited to the geographic areas in which the employee provided services or had a material presence during the last two years of employment, and the scope of proscribed activities is limited to the specific types of services provided by the employee during the last two years of employment.

The statute expressly states the law shall apply to all employees who have been (for at least 30 days immediately preceding his or her cessation of employment) a resident of or employed in Massachusetts at the time of termination, and that no choice of law provision to the contrary shall be enforceable.

Garden Leave or Other Mutually-Agreed Upon Consideration

One of the most significant changes is the requirement that the employer provide consideration to the employee during the restricted period. Specifically, the law states that the employer must provide "garden leave," defined as at least 50 percent of the employee's highest annualized base salary paid by the employer within two years preceding termination, or "other mutually agreed upon consideration," which is not defined.

Implications for Emerging Tech Companies

Given that the law is so new, there are still many questions regarding how it will be interpreted, such as how courts will define "other mutually agreed upon consideration." That said, the law's enactment has already significantly affected how many companies, including start-up and emerging technology companies, are recruiting and hiring and approaching corporate deal-making.

For example, because the law contains fairly stringent technical requirements, some start-ups are taking the view that the law's mandates are simply too onerous. Even complying with the law's 10-day notice requirements can be challenging in the fast-paced start-up world where companies often need to make hires "on the spot."

Further, many start-ups have expressed considerable reluctance to enter into non-competes requiring a potential payout of "garden leave" years down the road when the company may not be able to forecast its financial condition beyond the next few months. While this hesitation is reasonable, such companies should keep in mind that the law allows for an employer to choose not to enforce the non-competition agreement and therefore pay no garden leave, if the agreement is so structured.

Other employers, including those within the emerging technology space, are finding that they can achieve their goals (i.e., protecting confidential and proprietary information and relationships with clients, customers, or employees), without entering into non-competition agreements. The new law applies only to non-competition agreements, and expressly does not cover non-solicitation or nondisclosure agreements, which can often be used by employers, particularly within the technology industry, to protect intellectual property and client and employee relationships. In other cases, sometimes in the life-science sphere, companies simply do not believe that such agreements will adequately protect the disclosure of their intellectual property should one of their employees choose to jump to a competitor. In such instances, companies are proceeding with ensuring that valid non-compete agreements under the new law are in place.

Of course, within certain technology sectors, non-compete agreements had fallen out of favor years ago, particularly because many tech-related deals involved California companies where non-competition agreements have long been prohibited. These companies are having less difficulty adjusting to the new law. In other cases, however, investors are still insisting on having in place non-competition agreements "to the extent permitted by law" or, "to the *maximum* extent permitted by law." Such clauses pose particular challenges given that, without a more developed body of case law interpreting the new law, it is challenging to agree on exactly what the law allows at this point.

Key Takeaways for Emerging Tech Companies

Because parties cannot contract out of the new law by way of a choice of law provision, and particularly as it applies to employees and independent contractors alike, the law has broad-reaching implications for every company doing business in Massachusetts. Following are considerations for start-up and emerging technology companies:

- Think strategically about how, if at all, to utilize and enforce non-competes with respect to employees, including considering whether the business interests the company seeks to protect may be adequately guarded by alternative means (i.e., a non-solicitation or nondisclosure agreement);
- Update standard employment agreements, offer letters, and other HR documents to be compliant with the new law;

- Consider carefully whether prospective employees are subject to valid non-competes, as hiring or soliciting an employee subject to such an agreement could lead to having to rescind employment offers or, worse yet, expensive and time-consuming litigation.

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