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Employee Benefit Plan Review

# California Appeals Court Provides Much Needed Clarification on Enforceability of Employee Non-Solicit Provisions Post-*Edwards*

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The California Court of Appeal for the Fourth Appellate District has decided *AMN Healthcare, Inc. v. Aya Healthcare Servs., Inc.*,[1] affirming the trial court's holding that an employer's non-solicitation agreement – restricting former employees from recruiting the employer's existing employees – violated Cal. Bus. & Prof. Code Section 16600, which voids restraints on the ability of a person to engage in a trade, business, or profession. This decision is significant because it squarely addresses the impact of the 2008 *Edwards v. Arthur Andersen LLP* decision on employee non-solicitation agreements – an issue courts have previously avoided addressing directly.

## *Loral Corp.* and the Judicially-Created Non-Solicit Exception to Section 16600

In *Loral Corp. v. Moyes*,[2] more than 20 years before the *Edwards* decision, the California Court of Appeal held that a termination agreement between a corporation against its former chief executive officer, which restrained the defendant from disrupting, damaging, impairing, or interfering with the plaintiff's business by "raiding" its employees, was not void on its face under Section 16600.

In reaching this conclusion, the *Loral* court cited three Georgia state court opinions to support its holding that the potential impact on trade must be considered before invaliding a non-solicitation covenant, and that "enforceability depends upon [the covenant's] reasonableness, evaluated in terms of the employer, the employee, and the public."[3] The *Loral* court further determined that the restraint at issue only slightly affected the plaintiffs' employees as it did not completely prevent plaintiff's employees from working with a former employee at a different company. Instead, it only prohibited the prior employee from soliciting present employees.[4]

After the ruling in *Loral*, a common perception was that provisions prohibiting an employee from soliciting other employees for a certain amount of time post-employment were enforceable under California law.

## *Edwards* Changed Everything, or Did It?

In 2008, the California Supreme Court provided a bright line rule for how covenants that restrain trade should be treated under California law. The court held that any restraint on trade – even if narrowly tailored – is void under Business & Professions Code Section 16600, which codifies California's strong public policy against restraints on trade, unless the restraint

fell within one of three statutory exceptions.

In *Edwards v. Arthur Andersen LLP*,[5] Raymond Edwards II challenged the validity of a non-compete agreement he signed with Arthur Andersen which, among other things, (1) prohibited Edwards, for an 18-month period, from performing professional services of the type he had provided while at Andersen, for any client on whose account he had worked during 18 months prior to his termination; and (2) prohibited Edwards, for a year after termination, from performing professional services of the type he performed while at Anderson, for any client of Andersen's Los Angeles office.[6] In finding that the challenged non-compete agreement was invalid under California Business and Professions Code § 16600, the court held that, under § 16600's plain meaning, an employer cannot by contract restrain a former employee from engaging in his or her profession, trade, or business unless the agreement falls within one of the exceptions to the rule. The court expressly rejected Andersen's argument that the term "restrain" under Section 16600 should be interpreted to mean "prohibit," so that only contracts which prohibit an employee from engaging in his or her profession, trade, or business are illegal.[7]

Andersen also requested that the court adopt the "limited or narrow-restraint" exception adopted by the U.S. Court of Appeals for the Ninth Circuit in *Campbell v. Trustees of Leland Stanford Jr. Univ.*,[8] which excepted application of § 16600 where an employee was barred from pursuing "only a small or limited part of the business, trade or profession." The court again rejected this argument and instead held that "Section 16600 is unambiguous, and if the Legislature intended the statute to apply only to restraints that were unreasonable or overbroad, it could have included language to that effect."[9]

Because *Edwards* did not squarely address the validity of employee non-solicitation agreements, courts have been split on whether such provisions are still enforceable if they do not fall within one of the enumerated exceptions to § 16600. Some cases followed the reasoning in *Loral*:

- *Sunbelt Rentals, Inc. v. Victor*,[10] relying on *Loral* in finding that a non-solicitation provision restricting former employees from soliciting current Sunbelt employees for employment was not invalid;
- *Arthur J. Gallagher & Co. v. Lang*,[11] citing *Loral* for the proposition that "California courts recognize that an employer may not prohibit its former employees from hiring the employer's current employees, but an employer may lawfully prohibit its former employees from actively recruiting or soliciting its current employees."

While other cases rejected *Loral*'s reasoning as inconsistent with § 16600:

- *SriCom, Inc. v. EbisLogic, Inc.*,[12] holding non-solicitation clause was unenforceable under Section 16600 and the reasoning in *Edwards*;
- *Fields v. QSP, Inc.*,[13] holding restriction prohibiting former employee from soliciting former employer's customers and employees was "per se unlawful under California law regardless of the reasonableness of the covenant because 'an employer cannot by contract restrain a former employee from engaging in his or her profession.'"

Yet, despite the fact that these courts examined the validity of employee non-solicitation agreements post-*Edwards*, the California Supreme Court has not taken up the issue and the Court of Appeal decisions have not directly addressed the impact of *Edwards* on employee non-solicitation agreements – until now.

### *AMN Healthcare* Appears to Resolve the Dispute and Finds Employee Non-Solicits are Void in Light of *Edwards*

AMN and Aya are competitors in the business of providing temporary healthcare professionals, in particular "travel nurses," to medical care facilities throughout the country. After certain AMN travel nurse recruiters left AMN and joined Aya, AMN sued Aya and the departing employees alleging various causes of action including breach of contract and misappropriation of trade secrets under the California Uniform Trade Secrets Act (CUTSA).[14] Aya and the departing employees filed a cross-complaint for declaratory relief and unfair competition. Aya and the departing employees also challenged, under § 16600, the validity of an employee non-solicit provision, which prohibited the AMN departing employees from directly or indirectly soliciting or inducing, or causing others to solicit or induce, any employee to leave the service of AMN. Relying primarily on *Loral*, AMN argued that the employee non-solicitation provision was valid and enforceable because it merely prohibited the departing employees from soliciting current AMN employees.[15]

**Based on these factors, the *AMN* court expressed doubt about the continuing viability of *Loral* post-*Edwards*.**

In its analysis, the court initially determined that the employee non-solicitation provision at issue

"clearly restrained the [departing employees] from practicing their chosen profession of recruiting nurses on 13-week assignments with AMN."[16] The court then expressly rejected AMN's contention that the employee non-solicitation provision is valid because it "merely applie[d] to prevent nonsolicitation of [AMN's] employees."[17] In rejecting AMN's argument, the court examined the continuing viability of *Loral* post-*Edwards* and held that, even though *Edwards* did not address the validity of employee non-solicit agreements, *Edwards* rejected the argument that the Legislature meant the word "restrain" in Section 16600 to mean "prohibit" – which would conflict with *Loral*'s use of a reasonableness standard in analyzing the employee non-solicitation provision at issue in that case.[18] The court also highlighted the fact that the *Edwards* court refused to adopt the *Campbell* "limited" or "narrow-restraint" exception to Section 16600.[19] Based on these factors, the *AMN* court expressed doubt about the continuing viability of *Loral* post-*Edwards*. The court also held that even if *Loral*'s use of the reasonableness standard survived post-*Edwards*, the *Loral* case was factually distinguishable from the *AMN* case, where the departing employees were in the business of recruiting and placing nurses in medical facilities throughout the country.[20]

## Non-Solicitation Clauses Post-*AMN Healthcare*

In California, Court of Appeal decisions must be certified for publication by the California Supreme Court, which strongly supports the argument that employee non-solicitation provisions – even if narrowly drafted – are not enforceable in California. Going forward, California employers should place little weight on employee non-solicitation provisions. Indeed, in light of this decision, the risk of including employee non-solicitation provisions in employee agreements likely outweighs the possible benefit from a court possibly enforcing it, because knowingly including an unenforceable provision in an employee agreement may expose a company to liability under California's unfair competition law. Tread carefully.

## Notes

1. 239 Cal.Rptr.3d 577 (2018).
2. 174 Cal. App. 3d 268, 280 (1985).
3. *Loral*, 174 Cal. App. 3d at 278-279 (citing Orkin Exterminating Co., Inc. v. Martin Co., 240 Ga. 662 (1978)); Harrison v. Sarah Coventry, Inc., 228 Ga. 169 (1971); and Lane Co. v. Taylor, 174 Ga. App. 356 (1985).
4. *Loral*, 174 Cal. App. 3d at 279.
5. 44 Cal. 4th 937 (2008).
6. Although the non-compete agreement at issue in *Edwards v. Anderson* also contained a provision prohibiting the solicitation of other Anderson employees for eighteen months post-employment, Edwards did not challenge the validity of the employee non-solicit provision.
7. *Edwards*, 44 Cal. 4th at 947.
8. 817 F.2d 499 (9th Cir.1987).
9. *Id*. at 950.
10. No. C 13-4240 SBA, 2014 WL 492364, *9 (N.D. Cal. Feb. 5, 2014).
11. No. C 14-0909 CW, 2014 WL 2195062, *4 (N.D. Cal. May 23, 2014).
12. No. 12-CV-00904-LHK, 2012 WL 4051222, at *4-5 (N.D. Cal. Sept. 13, 2012).
13. No. CV 12-1238 CAS PJWX, 2012 WL 2049528, at *9 (C.D. Cal. June 4, 2012).
14. Civil Code Sections 3426 *et seq*.
15. AMN Healthcare, Inc. v. Aya Healthcare Servs., Inc., 239 Cal. Rptr. 3d 577, 588 (Ct. App. 2018).
16. *Id*. at 588.
17. *Id*. at 586.
18. *Id*. at 589.
19. *Id*.
20. *Id*. 590.

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