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# Leaky Covenants-Not-to-Compete as the Legal Infrastructure for Innovation

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# Leaky Covenants-Not-to-Compete as the Legal Infrastructure for Innovation

Robert W. Gomulkiewicz\*

*The flow of information that naturally occurs when employees change firms plays a vital role in spurring innovation. Numerous law review articles have explored how covenants-not-to-compete (“non-competes”) can impede this important information flow. In 1999 Professor Ronald Gilson published an influential article concluding that California’s ban on non-competes led to the rise of California’s Silicon Valley and the comparative decline of Massachusetts’ high technology corridor known as Route 128. Despite the scholarly praise for California’s approach, most states enforce non-competes that are reasonable. That may change, however, because many states are re-evaluating their non-compete laws to avoid Gilson’s cautionary tale about the fate of Route 128. But do states really need to ban non-competes in order to provide an inviting platform for innovation? This Article provides an answer to that important and intriguing question by examining, for the first time, whether technology firms actually enforce non-competes. Evidence from Washington State indicates that technology firms rarely enforce non-competes. In other words, non-competes are very leaky — knowledge workers move freely*

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\* Copyright © 2015 Robert W. Gomulkiewicz. UW Law Foundation Professor of Law; Faculty Director, Intellectual Property Law & Policy Graduate Program, University of Washington School of Law. For useful comments, I thank: Steve Calandrillo, Vince Chiappetta, Maggie Chon, Timothy Chou, Jonathan Franklin, Mallory Gitt, Jack Kirkwood, Anita Krug, Vijay Kumar, Anna Laakman, Andrea Lairson, Ida Lairson, Lydia Loren, Sean O’Connor, Kate O’Neill, Xuan-Thao Nguyen, Graham Reynolds, Karen Sandrick, Toshiko Takenaka, Kathryn Watts, and participants at the Pacific Intellectual Property Scholars Conference and Lewis & Clark Law School’s Business Law Forum. For excellent research assistance I thank Peter Montine, Ashleigh Rhodes, and the extraordinary librarians at the Gallagher Law Library of the University of Washington School of Law. I dedicate this article to Karl Quackenbush who asked me to work on a non-compete case when I was new associate, which led to my enduring fascination with the subject.

from one technology business to another in Washington just as they do in California. The Washington case study has crucial implications for all states. It suggests that states do not need to ban non-competes in order to foster innovation as many scholars contend. It also shows that leaky non-competes provide better protection for trade secrets than a complete ban provides. States can offer a fertile legal infrastructure for innovation without banning non-competes by taking steps to assure that non-compete enforcement is leaky, including measures to address the potential chilling effect of non-competes. California, for its part, should embrace the so-called “trade secret exception” to its ban on non-competes to improve California’s legal infrastructure for start-ups and established firms that rely on robust trade secret protection.

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INTRODUCTION

We live in an information economy where information technology firms covet their knowledge workers. A firm's success depends on recruiting smart researchers, skillful product developers, and clever business strategists,<sup>1</sup> so firms compete aggressively for the most talented workers. Talented workers move as they see fit, sometimes for more money but often in search of the most interesting work. However, a departing employee's covenant-not-to-compete (often called a "non-compete") can impede the flow of talent.

Numerous law review articles have explored the use of non-competes.<sup>2</sup> On the positive side, scholars point out that non-competes provide an incentive for firms to invest in employee training, encourage employees to share secrets within the firm, and safeguard against the disclosure of confidential information to a competitor.<sup>3</sup> On the negative side, scholars emphasize that non-competes stymie an individual's fundamental right to earn a living.<sup>4</sup> This seems particularly unjust when an employee has limited bargaining power and receives no separate consideration for the covenant.<sup>5</sup> Non-

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<sup>1</sup> See Matt Day, *Microsoft Employees — Past and Present — Look Back over the Years*, SEATTLE TIMES, May 24, 2015, at D6 (asking Microsoft Senior Vice President Yusuf Mehdi about where Microsoft will be in another 40 years and quoting him as saying that success hinges on making Microsoft an appealing stop for technology's most talented minds: "It isn't the technology. It isn't the products or services. They all come and go. What won't change is we'll still get the best and brightest. If we keep that, this place is going to be around for a long, long time").

<sup>2</sup> A Westlaw search on April 23, 2014 performed by the reference librarians of the Gallagher Law Library at the University of Washington School of Law found several hundred law journal articles discussing various aspects of non-competes. A representative sampling of those articles can be found in the footnotes *infra* Introduction–Part IV.

<sup>3</sup> See Harlan M. Blake, *Employee Agreements Not to Compete*, 73 HARV. L. REV. 625, 650-53 (1960).

<sup>4</sup> See Charles T. Graves, *Analyzing the Non-Competition Covenant as a Category of Intellectual Property Regulation*, 3 HASTINGS SCI. & TECH. L.J. 69, 71-72 (2011) (criticizing the enforcement of non-competes on several grounds).

<sup>5</sup> See, e.g., Rachel Arnow-Richman, *Cubewrap Contracts and Worker Mobility: The Dilution of Employee Bargaining Power via Standard Form Noncompetes*, 2006 MICH. ST. L. REV. 963 [hereinafter *Cubewrap Contracts*] (arguing that courts do not properly

competes also interfere with the flow of information that naturally results when employees change firms. Scholars argue that these “information spillovers” play a critical role in spurring innovation in technology industries.<sup>6</sup>

Discussion by legal scholars about the link between non-competes and information spillovers<sup>7</sup> began in earnest in 1999 when Professor Ronald Gilson published an influential article comparing innovation in California to that in Massachusetts.<sup>8</sup> He concluded that California’s law against enforcing non-competes provided a superior legal infrastructure for innovation, which explained the rise of Silicon Valley as an industrial district and the comparative decline of Massachusetts’ high technology corridor known as Route 128.<sup>9</sup> Many scholars agree with Gilson, arguing that California’s ban on non-competes is not only fair to workers, but provides the best approach for nurturing technology businesses (especially startups) and stimulating innovation in general.<sup>10</sup>

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consider the bargaining power of employees); Kate O’Neill, *Should I Stay or Should I Go?* — *Covenants Not to Compete in a Down Economy: A Proposal for Better Advocacy and Better Judicial Opinions*, 6 HASTINGS BUS. L.J. 83 (2010) (analyzing non-compete agreements from a theoretical and practical standpoint).

<sup>6</sup> See ORLY LOBEL, TALENT WANTS TO BE FREE 118-19 (2013); On Amir & Orly Lobel, *Driving Performance: A Growth Theory of Noncompete Law*, 16 STAN. TECH. L. REV. 833, 856-61 (2013); T. Leigh Anenson, *The Role of Equity in Employment Noncompetition Cases*, 42 AM. BUS. L.J. 1, 54 (2005). *But see* Grant R. Garber, Comment, *Noncompete Clauses: Employee Mobility, Innovation Ecosystems, and Multinational R&D Offshoring*, 28 BERKELEY TECH. L.J. 1079, 1082 (2013) (arguing that non-enforcement of non-competes “may be detrimental to the development of innovation ecosystems in emerging markets”).

<sup>7</sup> This article focuses on the relationship between non-competes and innovation in the software and information technology sector rather than the general fairness of non-competes or their role in other contexts such as professional services or sales. *See* Norman D. Bishara, *Covenants Not to Compete in a Knowledge Economy: Balancing Innovation from Employee Mobility Against Legal Protection for Human Capital*, 27 BERKELEY J. EMP. & LAB. L. 287, 315-16 (2006) [hereinafter *Covenants Not to Compete*].

<sup>8</sup> Ronald J. Gilson, *The Legal Infrastructure of High Technology Industrial Districts: Silicon Valley, Route 128, and Covenants Not to Compete*, 74 N.Y.U. L. REV. 575, 575 (1999).

<sup>9</sup> *Id.* at 629.

<sup>10</sup> *See, e.g.*, LOBEL, *supra* note 6, at 200 (arguing that even when removing the Bay Area to control for the possible outlier effect of California sunshine, “states where noncompetes are not enforced or weakly enforced more venture capital results in higher levels of entrepreneurship, more patenting, and better employment rates”); Viva R. Moffat, *Making Non-Competes Unenforceable*, 54 ARIZ. L. REV. 939, 945-46 (2012) [hereinafter *Making Non-Competes Unenforceable*] (discussing California and North Dakota “policy [that] rests on the belief that an absence of restrictions on the free flow of labor will promote commercial activity”); Viva R. Moffat, *The Wrong Tool*

Despite the scholarly praise for California's approach, most states enforce non-competes that are reasonable as to duration, geographic reach, and scope of work covered.<sup>11</sup> That may change, however, as state governments have renewed their efforts to provide a welcoming environment for knowledge workers and technology businesses.<sup>12</sup> States that currently serve as the home to innovation seem particularly keen to implement an innovation-friendly legal infrastructure, hoping to avoid the fate of Route 128.<sup>13</sup> No state governor or legislature wants to be accused of losing its innovative edge by failing to update its non-compete laws. Several states are considering legislation to ban non-competes and others are being urged to do so.<sup>14</sup> Indeed, some scholars argue that non-competes should be banned uniformly across the nation.<sup>15</sup> But do states really need to ban non-competes in order to provide the optimal legal infrastructure for innovation?

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*for the Wrong Job: The IP Problem with Noncompetition Agreements*, 52 WM. & MARY L. REV. 873, 873 (2010) [hereinafter *The Wrong Tool*] (arguing that employee noncompetition agreements ought to be unenforceable); see also Sampsa Samila & Olav Sorenson, *Non-Compete Covenants: Incentives to Innovate or Impediments to Growth*, 57 MGMT. SCI. 425, 425 (2010). As explained *infra*, Professor Gilson predicted that other approaches could work as well as California's ban on non-competes, but Gilson's article is often cited as proof of California's superior approach to non-competes and that message has been the one emphasized by many scholars since Gilson.

<sup>11</sup> See, e.g., MICH. COMP. LAWS § 445.774 (2015); discussion *infra* Part I (discussing common law and statutory approaches to non-competes).

<sup>12</sup> See Bishara, *Covenants Not to Compete*, *supra* note 7, at 299 (“[I]t is clear that states are interested in promoting knowledge-based industries impacted by [non-compete] policy.”).

<sup>13</sup> According to Bloomberg Business News, the top homes for innovation include: Arizona, California, Colorado, Connecticut, District of Columbia, Florida, Illinois, Kansas, Maryland, Massachusetts, Michigan, Minnesota, New Jersey, New York, North Carolina, Ohio, Oregon, Pennsylvania, Texas, Utah, Virginia, Washington, and Wisconsin. See *Most Innovative in U.S.: States*, BLOOMBERG (Nov. 18, 2013), <http://www.bloomberg.com/visual-data/best-and-worst/most-innovative-in-u-dot-s-states>.

<sup>14</sup> Moffat, *The Wrong Tool*, *supra* note 10, at 880 (reporting that various legislatures have considered or passed non-compete statutes, and that the ALI is drafting non-compete provisions as part of its RESTATEMENT (THIRD) OF EMPLOYMENT LAW). The Alliance for Open Competition (“AOC”) is lobbying nationwide for a ban on non-competes. See ALLIANCE FOR OPEN COMPETITION, <http://opencompetition.wordpress.com/> (last visited Dec. 19, 2014). The AOC has been particularly active in Massachusetts of late. See *infra* Part II.B. Even Washington State is considering a ban. See H.B. 1926, 64th Leg., Reg. Sess. (Wash. 2015) (restricting noncompetition agreements). Hawaii recently passed legislation prohibiting non-competes for any employee of a “technology business.” See 2015 Haw. Sess. Laws 158.

<sup>15</sup> See Moffat, *Making Non-Competes Unenforceable*, *supra* note 10, at 943 (proposing a uniform state law).

To date, scholars have focused their attention on California's climate for innovation as it compares to Massachusetts, and to a lesser extent other states with innovative industrial districts.<sup>16</sup> Curiously, one state seldom gets discussed: the state of Washington.<sup>17</sup> This omission stands out because Washington equals California as a launching pad for innovation; it also stands out because non-competes are enforceable in Washington. If banning non-competes provides California with its comparative advantage, then why has Washington been able to provide an equally attractive climate for innovation with a completely different approach?<sup>18</sup>

The answer is that technology businesses seldom enforce non-competes — in other words, non-competes are very leaky.<sup>19</sup> My

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<sup>16</sup> See, e.g., Jason S. Wood, *A Comparison of the Enforceability of Covenants Not to Compete and Recent Economic Histories of Four High Technology Regions*, 5 VA. J.L. & TECH. 14 (2000) (comparing California, Massachusetts, Texas, and North Carolina, and concluding that Gilson's theory about the importance of a ban on non-competes is not borne out by the evidence from Texas or North Carolina); Christine O'Malley, Note, *Covenants Not to Compete in the Massachusetts Hi-Tech Industry: Assessing the Need for a Legislative Solution*, 79 B.U. L. REV. 1215 (1999) (focusing on policy concerns and non-compete governance in Massachusetts and suggesting options for legislative action).

<sup>17</sup> The two primary exceptions are: Susan E. Corisis, Note, *Postemployment Restrictive Covenants: Client Base Protection in Washington*, 65 WASH. L. REV. 209, 209-15 (1990); Sarah J. Taylor, Comment, *Fostering Economic Growth in the High-Technology Field: Washington Should Abandon Its Recognition of the Inevitable Disclosure Doctrine*, 30 SEATTLE U. L. REV. 473, 473 (2007). Occasionally, Washington gets mentioned briefly in the context of the lawsuit between Google and Microsoft over Google's hiring of Kai-Fu Lee. See, e.g., Michael J. Garrison & John T. Wendt, *The Evolving Law of Employee Noncompete Agreements: Recent Trends and an Alternative Policy Approach*, 45 AM. BUS. L.J. 107, 107-10 (2008) (describing briefly the Washington court's narrow reading of Lee's Microsoft Employment Agreement that allowed for a "preliminary injunction restricting Lee's activities" but did not keep Lee from working for Google).

<sup>18</sup> See Norman D. Bishara, *Fifty Ways to Leave Your Employer: Relative Enforcement of Covenants Not to Compete, Trends, and Implications for Employee Mobility Policy*, 13 U. PA. J. BUS. L. 751, 786-87 (2011) [hereinafter *Fifty Ways to Leave*] (rating each state's enforceability strength); Mark J. Garmaise, *Ties That Truly Bind: Noncompetition Agreements, Executive Compensation, and Firm Investment*, 27 J.L. ECON. & ORG. 376, 420 (2009) (rating each state's enforceability strength using a different measure than Professor Bishara).

<sup>19</sup> Scholars have noted leakiness in various other intellectual property contexts. See, e.g., Mark A. Lemley, *Ignoring Patents*, 2008 MICH. ST. L. REV. 19 (discussing leakiness in patents); R. Polk Wagner, *Information Wants to Be Free: Intellectual Property and Mythologies of Control*, 103 COLUM. L. REV. 995 (2003) (discussing leakiness in intellectual property contexts); Tim Wu, *Tolerated Use*, 31 COLUM. J.L. & ARTS 617, 620 (2008) (suggesting an "opt-in" copyright enforcement system where copyright owners must give notice "before the usage of a work becomes infringing");

research shows that Washington's technology employers engage in regular economically rational selective enforcement; and Washington's knowledge workers engage in systematic, intelligent, efficient breach of non-competes. Despite an on-paper right to enforce non-competes, knowledge workers move freely from one technology business to another in Washington just as they do in California, except when an employer is faced with a significant threat of trade secret disclosure. It is fair to say that in Washington's technology sector, non-competes do not regularly prevent spillovers of useful information but do, periodically, protect critical trade secrets.

Taking a fresh look at California's approach to non-competes seems especially apt now that we know California's story about freedom of employee movement is far less rosy than previously thought. Recent litigation by employees at Adobe, Apple, Google, Intel, Intuit, LucasFilm, and Pixar Animation revealed secret promises between top technology businesses in California not to poach key employees.<sup>20</sup> These promises not to poach<sup>21</sup> were pursued aggressively by

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Diane Leenheer Zimmerman, *Modern Technology, Leaky Copyrights, and Claims of Harm: Insights from the Curious History of Photocopying*, 61 J. COPYRIGHT SOC'Y U.S.A. 1 (2013) (arguing that some "leaks" in the copyright system are permissible and that "adequate copyright protection does not mean virtually airtight control over works by their owners"). This leakiness occurs despite concerns that the threat of enforcing non-competes creates a chilling effect on employees who respect contractual obligations or fear legal complications. See *infra* Part III. For sources describing this concern, see Richard P. Rita Pers. Servs. Int'l, Inc. v. Kot, 191 S.E.2d 79, 81 (Ga. 1972) (declining to apply the severance theory to an unenforceable restrictive covenant); Reddy v. Cmty. Health Found. of Man, 298 S.E.2d 906, 916 (W. Va. 1982) (detailing what the employer must show for a presumptively enforceable non-compete and what the employee can show to rebut the presumptive enforceability); Arnow-Richman, *Cubewrap Contracts*, *supra* note 5, at 963 (exploring courts' approach to non-competes and suggesting that the "rules of enforcement might be reshaped to avoid dilution of employee bargaining power and encourage better contracting practices on the part of employers"); Blake, *supra* note 3, at 682-83 (acknowledging the possibility of *in terrorem* effects of non-competes but arguing that courts need discretion through a "general approach" to "tailor the covenant to provide such protection with a minimum burden to the employee" where the restraints on the employee are generally fair and designed to protect the employer's legitimate interests); Moffat, *The Wrong Tool*, *supra* note 10, at 888-90 (discussing the *in terrorem* effects of employer overreach in non-competes).

<sup>20</sup> See David Streitfeld, *In Silicon Valley Thriller, a Settlement May Preclude the Finale*, N.Y. TIMES, Apr. 20, 2014, at B1. An intriguing question — beyond the scope of this Article — is whether California's ban on non-competes contributed in any measure to the anti-poaching behavior. In other words, if California had a leaky non-compete infrastructure, would companies have seen the same need to engage in the anti-poaching tactics?

<sup>21</sup> See generally David K. Haase & Darren M. Mungerson, *Agreements Between*



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executives at the highest levels of the company, including by Steve Jobs of Apple and Eric Schmidt of Google.<sup>22</sup>

This Article explores Washington State's legal infrastructure for innovation as a case study, focusing on the impact of non-competes on so-called "creative workers" — those who create and invent in the information economy.<sup>23</sup> It shows how Washington achieves the advantages of liberal employee mobility and regular knowledge spillovers without the downsides of a flat-out ban on non-competes. The Washington way may be superior to California's approach because Washington gives employers a tool of last resort against threats of trade secret disclosure by key employees that California lacks.<sup>24</sup> The point of this Article is not that Washington is exceptional; the point is that states do not need to ban non-competes in order to foster innovation as many scholars have contended. Washington's leaky non-compete legal infrastructure is exemplary, but other states can offer (and perhaps already do offer)<sup>25</sup> an inviting legal platform for innovation without banning non-competes by taking steps to assure that non-compete enforcement is leaky. I offer several proposals in this Article to improve beneficial leakiness in every state by addressing the potential chilling effect of non-competes.

To be clear, I do not advocate for unfettered and indiscriminate use of non-competes.<sup>26</sup> Commentators have rightly condemned this

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*Employers Not to Hire Each Other's Employees: When Are They Enforceable?*, 21 LAB. LAW. 277, 277-302 (2006) (comparing courts' "antitrust," contracts in "restraint on trade," and "restrictive covenant" approaches to validity of "no-switching" agreements); David L. Johnson, *The Parameters of "Solicitation" in an Era of Non-Solicitation Covenants*, 28 A.B.A. J. LAB. & EMP. L. 99 (2012) (providing national case survey of enforceable and unenforceable non-solicitation agreements for prior customers and former co-workers).

<sup>22</sup> See David Streitfeld, *Tech Giants Settle Antitrust Hiring Suit*, N.Y. TIMES, Apr. 24, 2014, at B1.

<sup>23</sup> See Bishara, *Covenants Not to Compete*, *supra* note 7, at 315-16 (distinguishing "creative" workers from "service" workers who also have high levels of education but are engaged in providing services to other elements of the knowledge economy).

<sup>24</sup> Although California law may provide an equivalent tool as an exception to its ban on non-competes, recent cases have cast doubt on its availability, but this Article argues that California should embrace that "exception" as discussed *infra* Parts I-IV.

<sup>25</sup> Further research likely will reveal that states other than Washington also have a leaky non-compete legal infrastructure but some evidence suggests that not all states do at the present time. See Ruth Simon & Angus Loten, *Litigation over Noncompete Clauses Is Rising*, WALL ST. J. (Aug. 14, 2013, 8:06 PM ET), <http://www.wsj.com/articles/SB10001424127887323446404579011501388418552> (reporting on research conducted for the WSJ by the law firm of Beck Reed Riden showing that since 2002 non-compete cases rose 61% across the U.S. to 760 published cases).

<sup>26</sup> See Froma Harrop, *To Keep Good Workers, Some Employers Are Trapping Them*,

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practice for a multitude of good reasons and courts have the tools and should have the will to refuse enforcement in these cases. Instead, I show the value of targeted enforcement of non-competes when the loss of trade secrets is genuinely at risk.<sup>27</sup>

Following this Introduction, Part I introduces the law of non-competes in the United States, including the commonly used “rule of reason” approach and California’s ban on non-competes. Part II presents the rising crescendo for states to adopt California’s approach to non-competes, as states compete to attract and retain technology-related businesses. Part II explains how this trend began with Professor Gilson’s influential article but has been fueled by recent scholarship that draws on business management and behavioral science research. Part III describes Washington’s law on non-competes, presents research showing how the actual enforcement of non-competes in Washington’s technology sector is very leaky, and explains the pragmatic reasons for the leakiness. Part III also addresses why the potential chilling effects of non-compete litigation are less significant than scholars might fear. Part III concludes by showing how a leaky approach to non-compete enforcement creates a useful legal infrastructure for innovation that is on par with California’s approach and indeed provides some notable advantages for protecting valuable trade secrets. Using insights from the Washington case study, Part IV outlines a series of proposals directed to courts and legislators in every state to reduce potential chilling effects of non-competes and improve the state’s legal infrastructure for innovation. It also explains why California should embrace the so-called “trade secret exception” to its ban on non-competes in order to improve California’s legal

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SEATTLE TIMES, June 7, 2015, at A13 (“Originally designed to stop tech whizzes from taking company secrets to higher bidders, these noncompete agreements are being forced on workers loading boxes at warehouses or assembling sandwiches so that they can’t go to the warehouse or sandwich shop down the block.”); Danny Westneat, *Low-Paying Job Includes Noncompete Clause*, SEATTLE TIMES, Nov. 12, 2014, at B1 (commenting on reports of non-competes used at Seattle’s ServiceMaster water damage cleaner and the Jimmy John’s sandwich shop: “It’s hard to conjure what intellectual property or trade secrets are at stake in making the Turkey Tom. Or wet-vacating carpets. It’s one thing to make engineers or lawyers sign noncompetes. But cleaners?”); Ray Henry, *Scrutiny on Worker Non-Compete Deals*, ASSOCIATED PRESS (Jan. 3, 2015, 8:32 PM EST), <http://bigstory.ap.org/article/76a057287c844f59a3bee39be9926395/scrutiny-worker-non-compete-deals> (reporting on non-competes at Jimmy John’s sandwich shop and Super Maid housecleaning services).

<sup>27</sup> Unfortunately, the unfettered and indiscriminate use of non-competes gives legitimate uses a bad name (getting a bad name happens in copyright law as well). See Jane C. Ginsburg, *How Copyright Got a Bad Name for Itself*, 26 COLUM. J.L. & ARTS 61, 61-62 (2002). Thus, this Article proposes several ways to deter the heavy-handed uses of non-competes. See *infra* Part IV for a discussion of these proposals.

infrastructure for start-ups and established firms that rely on robust trade secret protection.

## I. THE LAW OF COVENANTS-NOT-TO-COMPETE

### A. English Origins

A covenant-not-to-compete forbids a departing employee from competing with a former employer either as an employee of an established rival firm or by starting a new firm.<sup>28</sup> Non-competes have become ubiquitous in employment contracts for highly skilled employees who work in the software and information technology sector.<sup>29</sup> However, non-competes did not originate in the modern information economy.

Non-competes can be traced back to the master-apprentice relationship in England. In this relationship, the master invested time and effort in training an apprentice in the skills of a trade and the apprentice, in turn, provided services back to the master for a specified period of time.<sup>30</sup> If the apprentice left early to compete against the master, British courts of equity enforced non-competes to enable the

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<sup>28</sup> *Google, Inc. v. Microsoft Corp.*, 415 F. Supp. 2d 1018, 1019 (N.D. Cal. 2005) (“While employed at Microsoft and for a period of one year thereafter, I will not (a) accept employment or engage in activities competitive with products, services, or projects (including actual or demonstrably anticipated research or development) on which I worked or about which I learned confidential or proprietary information or trade secrets while employed at Microsoft . . .”).

<sup>29</sup> According to one commentator, it is “generally and logically assumed that non-compete clauses in employment contracts are widely utilized. However, there is not much evidence available on this point.” Bishara, *Fifty Ways to Leave*, *supra* note 18, at 759-60; *see also* Norman D. Bishara, Kenneth J. Martin & Randall S. Thomas, *An Empirical Analysis of Noncompetition Clauses and Other Restrictive Postemployment Covenants*, 68 VAND. L. REV. 1, 3 (2015) (empirical study of the prevalence of non-competes for CEOs of 500 large companies); Garmaise, *supra* note 18, at 396 (reporting evidence that 70.2% of top executives sign noncompetes); Matt Marx, *The Firm Strikes Back: Non-Compete Agreements and the Mobility of Technical Professionals*, 76 AM. SOC. REV. 695, 700 (2011) (interviews with small sample of high tech workers); Samila & Sorenson, *supra* note 10, at 425 (citing surveys finding that nearly 90% of technical workers and upper level management sign non-competes); Stewart J. Schwab & Randall S. Thomas, *An Empirical Analysis of CEO Employment Contracts: What Do Top Executives Bargain For?*, 63 WASH. & LEE L. REV. 231, 234 (2006) (concluding that non-competes are widely used for CEOs at large public companies).

<sup>30</sup> *See* Blake, *supra* note 3, at 625-46 (reviewing the extensive history of restrictive employment covenants); *see also* Dan Messeloff, Note, *Give the Green Light to Silicon Alley Employees: No-Compete Agreements Between Internet Companies and Employees Under New York Law*, 11 FORDHAM INTELL. PROP. MEDIA & ENT. L.J. 711, 711-23 (2001) (providing a historical account).

master to protect the master's training investment. Over time, when enforcement of non-competes became too harsh, English courts began to hold that employers could only enforce reasonable limitations on departing employees.<sup>31</sup>

### B. Modern American Law: Two Paths

#### 1. Majority Path: Enforceable When Reasonable

Most states in the United States follow the English tradition of enforcing non-competes if they are reasonable. As in early England, non-competes can protect an American employer's investment in training its employees. This training often involves specific technical training. In economic terms, non-competes provide an incentive for employers to invest in employee training. This benefits employers, of course, but also benefits employees who, ultimately, can deploy their new skills elsewhere. Unlike early English law, modern United States law does not enforce non-competes simply to protect an employer's investment in human capital. This interest is not compelling enough to outweigh the employee's strong interest in freedom of movement and the right to earn a living.<sup>32</sup>

The modern rationale for enforcing non-competes goes beyond protecting an employer's investment in training. Today, the rationale often focuses on the relationship between non-competes and the protection of intellectual property, especially trade secrets.<sup>33</sup> When employees create copyrightable works, patentable inventions, or trademarks in the course of their employment, the employer owns this intellectual property either by operation of law or through an industry standard assignment of rights. Trade secrets present a bigger challenge.

For one thing, trade secret protection lasts only as long as the information remains secret.<sup>34</sup> If a departing employee discloses the information to a competitor, then the secret is irretrievably lost. This may be particularly devastating if the trade secret provides the comparative advantage that the employer has (or had) over its

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<sup>31</sup> See Blake, *supra* note 3, at 638-39.

<sup>32</sup> See Anenson, *supra* note 6, at 118.

<sup>33</sup> See Blake, *supra* note 3, at 668-71. *But see* Moffat, *The Wrong Tool*, *supra* note 10, at 898 (arguing that "the IP justification fails. Noncompetes are simply the wrong tool for the IP job").

<sup>34</sup> UNIFORM TRADE SECRETS ACT § 1(4) (amended 1985) (trade secret protection exists only for information not generally known); *see* RESTATEMENT (FIRST) OF TORTS § 757(b) (1939).

competitor. For another thing, because some trade secret information resides only (or primarily) in the mind of the employee, this information may be lost to the employer if the employee leaves without documenting the information. Finally, it is often difficult to separate an employee's general skill and knowledge from an employer's trade secret. In light of this ambiguity, a non-compete provides an insurance policy for the employer against the disclosure of intermingled information. As articulated by the Court in *Comprehensive Technologies International v. Software Artisans*, "[w]hen an employee has access to confidential and trade secret information critical to the success of the employer's business, the employer has a strong interest in enforcing a covenant not to compete because other legal remedies often prove inadequate."<sup>35</sup>

Freedom of contract provides another justification for enforcing non-competes. Independent actors should be free to enter into agreements of their choosing and courts should not interfere with the substance of those agreements absent procedural or substantive unconscionability. In the context of non-competes, however, American law has departed from a slavish application of this principle. It recognizes that employment agreements are rarely negotiated, that employees often lack sophistication and bargaining power, and that consideration is often inadequate or absent.<sup>36</sup>

Drawing on these guiding principles, states enforce non-competes tempered by a rule of reason.<sup>37</sup> The RESTATEMENT (SECOND) OF

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<sup>35</sup> *Comprehensive Techs. Int'l, Inc. v. Software Artisans, Inc.*, 3 F.3d 730, 739 (4th Cir. 1993) *vacated on petition for reh'g* (1993); see also James P. Pooley, *Update on Trade Secret Law*, INTELL. PROP. COUNS., Oct. 2008, at 5 available at <http://media.mofo.com/docs/pdf/081009Pooley.pdf> (stating covenants restricting an employee's right to compete following termination are one way to avoid the cost and unpredictability of trade secret litigation).

<sup>36</sup> See Blake, *supra* note 3, at 647-50.

<sup>37</sup> Some states (about 30%) address non-competes by statute and the others through common law. See generally BRIAN M. MALSBERGER, COVENANTS NOT TO COMPETE, A STATE-BY-STATE SURVEY (4th ed. 2004 & Supp. 2014) (analyzing non-compete case law across the nation with particular emphasis on significant splits of authority); KURT E. DECKER, COVENANTS NOT TO COMPETE (2d ed. 1993 & Supp. 2004) (detailing protectable interests in non-competes through a step-by-step litigation guide). For a statutory approach, see COL. REV. STAT. § 8-2-113(2) (2015) (widely permitting non-competes for executive and management level employees); LA. REV. STAT. ANN. § 23:921 (2015) (restricting non-competes to two years or less within a specific geographic area); see also Melissa Ilyse Rassas, Comment, *Explaining the Outlier: Oregon's New Non-Compete Agreement Law & The Broadcast Industry*, 11 U. PA. J. BUS. L. 447, 450-52 (2009).

CONTRACTS captures the general<sup>38</sup> approach: in considering whether to enforce a non-compete, a court must consider (1) whether “the restraint is greater than needed to protect the [employer’s] legitimate interest”; (2) the “hardship to the [employee]”; and (3) “the likely injury to the public.”<sup>39</sup> Each state reflects the RESTATEMENT’S formulation differently, as illustrated below by the tests in New York and Virginia (the tests for Massachusetts, North Carolina, Texas, and Washington will be discussed *infra* in Sections II and III):

In New York, a restraint is reasonable only if it: (1) is not greater than necessary for the protection of the legitimate interest of the employer, (2) does not impose undue hardship on the employee, and (3) is not injurious to the public. A non-compete must also be reasonable temporally and geographically.<sup>40</sup>

In Virginia, (1) covenants in restraint of trade are not favored, will be strictly construed and, in the event of an ambiguity, will be construed in favor of the employee; and (2) the employer bears the burden to show that the restraint is no greater than necessary to protect a legitimate business interest, is not unduly harsh or oppressive in curtailing an employee’s ability to earn a livelihood, and is reasonable in light of sound public policy.<sup>41</sup>

To implement the rule of reason, many courts will reform an unreasonable non-compete contract.<sup>42</sup> Some courts do this by excising unreasonable terms and then enforcing reasonable terms that remain, provided the covenant remains grammatically coherent.<sup>43</sup> This is

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<sup>38</sup> Some scholars describe state non-compete law as nuanced but relatively consistent over time. See Bishara, *Fifty Ways to Leave*, *supra* note 18, at 754. Other scholars characterize this diversity as “a mess.” See Moffat, *Making Non-Competes Unenforceable*, *supra* note 10, at 943.

<sup>39</sup> RESTATEMENT (SECOND) OF CONTRACTS § 188 (1981).

<sup>40</sup> See *Natural Organics, Inc. v. Kirkendall*, 860 N.Y.S.2d 142, 143 (App. Div. 2008).

<sup>41</sup> See *Modern Env’ts, Inc. v. Stinnett*, 561 S.E.2d 694, 696 (Va. 2002).

<sup>42</sup> Statutes in Florida, Michigan, and Texas specifically allow a court to reform a non-compete. See FLA. STAT. ANN. § 542.335(1) (2015); MICH. COMP. LAW ANN. § 445.774a (2015); TEX. BUS. & COM. CODE ANN. § 15.51(c) (2015). See generally Griffin Toronjo Pivateau, *Putting the Blue Pencil Down: An Argument for Specificity in Noncompete Agreements*, 86 NEB. L. REV. 672 (2008) (describing the various permutations of the blue pencil doctrine and outlining the arguments for and against each approach).

<sup>43</sup> Wisconsin, by contrast, voids any overbroad non-compete. See WIS. STAT. § 103.465 (2015).

known as the “blue pencil” approach.<sup>44</sup> Other courts will simply enforce the non-compete only to the extent it is reasonable. This is known as the partial enforcement approach.<sup>45</sup>

Moreover, some states require additional consideration for non-competes entered into once the employment relationship has begun. In these states, continued employment is not sufficient consideration.<sup>46</sup> This adds an additional hurdle for employers who seek, even for legitimate reasons, to restrain employee mobility.

In sum, modern American law on non-competes has not strayed too far from its roots in the English law of equity.<sup>47</sup> American courts do not enforce non-competes unequivocally but, instead, they look for a business justification that outweighs the individual rights of the employee to work and to move, and the public’s interest in keeping the skill of the employee productively employed in the economy.<sup>48</sup> As in English courts of equity, non-competes can be enforced in the United States, but not if they are too harsh (for individuals or society).

## 2. California’s Path: Never Enforceable

Initially, California followed the common law rule that non-competes are valid as long as they are reasonably imposed.<sup>49</sup> However, in 1872 California changed course, settling on a public policy that favored unfettered competition and employee mobility.<sup>50</sup> The legislature enacted this policy in then Civil Code Section 833 (now California Business and Professions Code section 16600): “Except as provided in this chapter, every contract by which anyone is restrained

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<sup>44</sup> See *Ferrofluidics Corp. v. Advanced Vacuum Components, Inc.*, 968 F.2d 1463, 1469 (1st Cir. 1992) (describing the blue pencil approach).

<sup>45</sup> *Id.* (describing the partial enforcement approach).

<sup>46</sup> See, e.g., *Stevenson v. Parsons*, 384 S.E.2d 291, 293 (N.C. Ct. App. 1989) (describing covenants not to compete in North Carolina); *George W. Kistler, Inc. v. O’Brien*, 347 A.2d 311, 316 (Pa. 1975) (describing covenants not to compete in Pennsylvania); *Labriola v. Pollard Grp., Inc.*, 100 P.3d 791, 794-96 (Wash. 2004) (describing covenants not to compete in Washington).

<sup>47</sup> See *Blake*, *supra* note 3, at 630-31, 643-46.

<sup>48</sup> See, e.g., *Systems & Software, Inc. v. Barnes*, 886 A.2d 762, 764 (Vt. 2005) (“We have stated that ‘we will proceed with caution’ when asked to enforce covenants against competitive employment because such restraints run counter to public policy favoring the right of individuals to engage in the commercial activity of their choice.”).

<sup>49</sup> See *Wright v. Ryder*, 36 Cal. 342, 357 (1868).

<sup>50</sup> *Edwards v. Arthur Andersen LLP*, 189 P.3d 285, 288-91 (Cal. 2008).

from engaging in a lawful profession, trade, or business of any kind is to that extent void.”<sup>51</sup>

Section 16600 did not result from the foresight of the California legislature, but instead, can be traced to the nineteenth century codification movement in American law led by David Dudley Field and his “Field Code.”<sup>52</sup> The California Supreme Court has ruled that Section 16600 “prohibits employee noncompetition agreements unless the agreement falls within a statutory exception.”<sup>53</sup> California’s strong rule against the enforceability of non-competes has been replicated in Hawaii, North Dakota, Montana, and Oklahoma<sup>54</sup> although the courts in Montana and Oklahoma have interpreted their statutes to permit the enforcement of non-competes in certain circumstances.<sup>55</sup> Although not going as far as California, Colorado and Oregon limit enforcement of non-competes to managers and professional workers.<sup>56</sup>

## II. THE RISING CRESCENDO FOR THE CALIFORNIA APPROACH

### A. *Professor Saxenian, Professor Gilson, and Mr. Wood*

Scholars have identified the key conditions that incubate high technology innovation in a region. The consensus factors include a significant university or research center, access to capital, a robust

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<sup>51</sup> Cal. Bus. & Prof. Code Ann. § 16600 (2015); *see also* Gilson, *supra* note 8, at 613-19.

<sup>52</sup> *See* Gilson, *supra* note 8, at 613-14 (noting the role of “serendipity” and “historical accident” in the enactment of section 16600 and observing “It is impossible to know exactly what Field had in mind in this sequence”). *See generally* LAWRENCE M. FRIEDMAN, A HISTORY OF AMERICAN LAW 391 (2d ed. 1985) (describing Field’s codification efforts).

<sup>53</sup> *Arthur Andersen LLP*, 189 P.3d at 288; *see also* *Muggill v. Reuben H. Donnelley Corp.*, 398 P.2d 147, 149 (Cal. 1965). The “statutory exceptions” apply to noncompetition agreements in the sale or dissolution of corporations (16601), partnerships (16602), and limited liability corporations (16602.5).

<sup>54</sup> *See* 2015 Haw. Sess. Laws 158 (prohibiting non-competes for employees of technology businesses); MONT. CODE ANN. § 28-2-703 (2015); N.D. CENT. CODE. § 9-08-06 (2015); OKLA. STAT. tit. 15, § 217 (2015); *see also* GA. CONST. art III, § 6, para. V(c) (prohibiting the general assembly from authorizing contracts that inhibit competition).

<sup>55</sup> *See* *Dobbins v. Rutherford*, 708 P.2d 577, 579 (Mont. 1985); *Thayne A Hedges Reg’l Speech & Hearing Ctr., Inc. v. Baughman*, 996 P.2d 939, 941 (Okla. Civ. App. 1998).

<sup>56</sup> COLO. REV. STAT. § 8-2-113(d) (2015); OR. REV. STAT. § 653.295(1)(a)–(b) (2015). Since highly skilled employees contribute the most to knowledge spillovers, Oregon’s and Colorado’s approaches protect low skilled workers from unfair treatment but do not address the key issue addressed in this article.



infrastructure, and an environment for a high quality of life.<sup>57</sup> Following in this line of research, Professor AnnaLee Saxenian, a sociologist, studied the rise of Silicon Valley's high-technology sector during the 1980's as it compared to the relative stagnation of the Route 128 region of Massachusetts.<sup>58</sup> Saxenian's focus was not on the initial conditions needed for innovation, but rather the conditions that allow a region to sustain and regenerate innovative activity. Saxenian attributed Silicon Valley's relative success largely to its culture: small firms with no fear of failing, frequent employee crossover, and a culture of information sharing.<sup>59</sup> By contrast, Route 128 was dominated by large integrated firms with minimal employee crossover and a culture of secrecy.<sup>60</sup> The knowledge spillovers that occurred in Silicon Valley, in Saxenian's estimation, fostered its rapid development of new technologies and positive economic growth.

Professor Ronald Gilson built on Saxenian's work, arguing that California's approach to non-competes provided the legal infrastructure for the success of Silicon Valley as a high technology engine.<sup>61</sup> Gilson pointed out that California's non-enforcement approach to non-competes maximizes employee movement between firms and thus knowledge spillovers.<sup>62</sup> By contrast, Massachusetts follows the rule of reason approach to the enforcement of non-competes, which can impede knowledge spillovers by restricting employee movement

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<sup>57</sup> For recent discussions of these factors, see Maggie Theroux Fieldsteel, *Building a Successful Technology Cluster*, U.S. ENVTL. PROT. AGENCY, OFFICE OF RESEARCH AND DEV., ENVTL. TECH. INNOVATION CLUSTERS PROGRAM 14-20 (Mar. 12, 2013) (reviewing the factors in the context of three different clusters, defined as "dense regional networks of companies, universities, research institutions, and other stakeholders involved in a single industry"); Rustam Lalkada, *Technology Business Incubation: A Toolkit on Innovation in Engineering, Science and Technology*, U.N. EDUC., SCI. AND CULTURAL ORG. (2006).

<sup>58</sup> See generally ANNALEE SAXENIAN, *REGIONAL ADVANTAGE: CULTURE AND COMPETITION IN SILICON VALLEY AND ROUTE 128* (1994) (comparing the technology industry in California versus Massachusetts).

<sup>59</sup> *Id.* at 2-3, 29-57.

<sup>60</sup> *Id.* at 3-4, 59-82.

<sup>61</sup> Gilson, *supra* note 8, at 579 ("The different legal rules governing postemployment covenants not to compete in California and Massachusetts help explain the differences in employee job mobility and therefore the knowledge transfer that Saxenian identifies as a critical factor in explaining the differential performance of Silicon Valley and Route 128."). Like most other commentators, Gilson assumed without presenting much evidence that use of non-competes was widespread in Massachusetts. See *id.* at 603-06.

<sup>62</sup> *Id.*

between firms.<sup>63</sup> According to Gilson, the critical differentiator between Silicon Valley and Route 128 is law not just culture.<sup>64</sup>

Professor Gilson's article has been extremely influential. It is hard to find a law review article that does not cite Gilson or use his article as a point of departure.<sup>65</sup> Indeed, the crescendo of scholarly support for Gilson's thesis has been rising in recent years.<sup>66</sup> However, significant aspects of Gilson's article are often overlooked. These portions of Gilson's work provide words of caution against a full-fledged embrace of California's approach to non-competes. It is important to highlight these points because Gilson's work is so foundational.

Gilson did not suggest that California's approach is right for every state. To the contrary, he warned: ". . . I think caution is in order in assessing the policy implications of Silicon Valley's history."<sup>67</sup> He ends his article with this advice: "[t]hus, it may well be that a state concerned with regional developments today should not blindly seek to replicate the historical source of Silicon Valley's success. Given the opportunity to act by design rather than by historical accident, the better approach may be to craft a legal infrastructure that has the flexibility to accommodate the different balance between external economies and intellectual property rights protection that may be optimal in different industries."<sup>68</sup>

And what legal infrastructure might accommodate this important "flexibility?" Gilson suggests: "[r]ather than emulating California's blanket prohibition (which, after all, exists by historical accident not design), it may be that the rule of reason currently applied to post-employment covenants . . . is flexible enough . . . In assessing the validity of a particular covenant under this legal regime, a court balances against the employer's interest in enforcing the covenant not only the employee's interest in mobility, but also the public interest."<sup>69</sup>

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<sup>63</sup> *Id.* at 603-08.

<sup>64</sup> *Id.* at 594.

<sup>65</sup> See, e.g., Bishara, Martin & Thomas, *supra* note 29, at 14 (citing Gilson and remarking "Perhaps the most active discussion regarding the propriety of [non-competes] relates to the well-known academic argument that the economic growth of Silicon Valley was made possible in part because of California's ban on noncompetes"); Garrison & Wendt, *supra* note 17, at 170-171 (providing brief synopsis of Professor Gilson's arguments).

<sup>66</sup> See Bishara, Martin & Thomas, *supra* note 29, at 15 (referring to the "burst of recent scholarship" about the California effect); see also *infra* Part II.B (describing recent scholarship urging a California approach).

<sup>67</sup> Gilson, *supra* note 8, at 627.

<sup>68</sup> *Id.* at 629.

<sup>69</sup> *Id.* at 628.

Professor Gilson was not the only one examining the effect of non-competes on innovation at that time. Mr. Jason S. Wood, an attorney in North Carolina, published an article the year after Gilson's piece, comparing Silicon Valley not only to Route 128, but also to high tech hotbeds in Austin, Texas ("Austin") and North Carolina's Research Triangle Park ("RTP").<sup>70</sup> Compared to the fame of Gilson's article, Wood's work has been largely ignored by scholars,<sup>71</sup> but it is highly instructive.

Wood acknowledged that Gilson had described significant differences in the histories and legal infrastructure of Silicon Valley and Route 128. However, Wood suggested that the predictive usefulness of California's approach to non-competes could be tested by comparing it with other thriving high technology sectors such as Austin and the RTP as well as Route 128. Thus, Wood's article first analyzed the law of non-competes in California, Massachusetts, Texas, and North Carolina, and then evaluated whether the enforcement posture of each state's law tracked the relative vibrancy of each state's high tech sector.

Wood noted that Texas and North Carolina, like Massachusetts, take a rule of reason approach to enforcing non-competes. Both Texas and North Carolina test the reasonableness of a non-compete by considering the typical factors.<sup>72</sup> However, Wood pointed out some differences of note. North Carolina's courts go farther in protecting employees by requiring that the non-compete be signed, in writing, and entered into at the time and as part of the contract of employment.<sup>73</sup> North Carolina's pro-employee twist may be offset, according to Wood, by the tendency of North Carolina's courts to grant injunctive relief in non-compete cases upon showing a likelihood of success on the merits without proof of actual harm.<sup>74</sup>

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<sup>70</sup> Wood, *supra* note 16, at 26-28.

<sup>71</sup> According to a LEXIS search on January 26, 2015, Professor Gilson's article has been cited 182 times compared to 17 citations to Mr. Wood's article.

<sup>72</sup> Namely, whether (1) the restraint is reasonable to protect the employer's legitimate business interest; (2) the scope of the restraint is reasonable; (3) valuable consideration is given; and (4) the covenant is consistent with public policy in North Carolina. See *United Labs., Inc. v. Kuykendall*, 370 S.E.2d 375, 379-81 (N.C. 1988); *Kadis v. Britt*, 29 S.E.2d 543, 545-49 (N.C. 1944); see also *Welcome Wagon v. Morris*, 224 F.2d 693, 698 (4th Cir. 1955) (collecting North Carolina cases on non-competes). In Texas the rule of reason test is codified. See TEX. BUS. & COM. CODE ANN. § 15.50(a) (2015).

<sup>73</sup> See *Triangle Leasing Co. v. McMahon*, 393 S.E.2d 854, 857-58 (N.C. 1990); *Whittaker Gen. Med. Corp. v. Daniel*, 379 S.E.2d 824, 826-28 (N.C. 1989).

<sup>74</sup> See *A.E.P. Indus., Inc. v. McClure*, 302 S.E.2d 754, 759-60 (N.C. 1983); see also

Texas courts, on the other hand, often seem unwilling to enforce non-competes in practice even though they are clearly enforceable under state law, including Texas statutory law.<sup>75</sup> Wood's bottom line is that if you put the four states on a spectrum, Massachusetts' legal infrastructure for non-competes would be the most restrictive of knowledge spillovers, followed by North Carolina, Texas, and California.<sup>76</sup> Based on that spectrum, Wood compared the relative rate of growth in each state to see whether the state growth rates followed the restrictiveness pattern.

Wood found that Silicon Valley, Austin, and the RTP had all experienced very high levels of economic success and all were experiencing similar relative growth spurts, but just at different orders of magnitude.<sup>77</sup> The same held true for venture capital dollars invested and venture capital deals completed — similar relative growth across regions.<sup>78</sup> He also found that Route 128 had recovered its momentum.<sup>79</sup> In the final analysis, Wood concluded that “. . . it would appear that the results one would expect from the effects of Gilson's theory are being obscured by other factors, or that his argument does not possess significant predictive value and may not play quite the significant role that he would suggest.”<sup>80</sup> Wood called for additional study over a longer period of time to determine which factors truly correlated with creating a multigenerational economy of technological innovation.<sup>81</sup>

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John Reid Parker, Jr., *Injunctive Russian Roulette and Employment Noncompetition Cases: A.E.P. Industries, Inc. v. McClure*, 63 N.C. L. REV. 222, 223-27 (1984). Even after the Supreme Court's *eBay* decision, it may be easier to get pre-trial injunctive relief in a trade secret case than in a copyright or patent case. See *Core Labs. LP v. Spectrum Tracer Servs., LLC*, 532 Fed. App'x. 904, 907-11 (Fed. Cir. 2013).

<sup>75</sup> See Wood, *supra* note 16, at 36.

<sup>76</sup> See *id.* In comparison, Professor Bishara also put non-compete enforceability on a spectrum, rating each state's enforceability strength on a scale of 1 to 51, with 51 signaling the weakest enforcement. See Bishara, *Fifty Ways to Leave*, *supra* note 18, at 787. California received a score of 50, North Carolina scored 35, Texas 32, and Massachusetts 18. *Id.* In Professor Garmaise's "Noncompetition Enforceability Index," California received a score of 0, Texas 3, North Carolina 4, and Massachusetts 6. See Garmaise, *supra* note 18, at 420.

<sup>77</sup> Wood, *supra* note 16, at 44, 48, 58.

<sup>78</sup> See *id.* at 51.

<sup>79</sup> *Id.* at 39, 44, 51. Wood pointed out that many Silicon Valley firms had established large presences in the Boston area to benefit from Boston's resurgence. See *id.* at 39.

<sup>80</sup> *Id.* at 51.

<sup>81</sup> *Id.* at 65 (suggesting that research should occur over the span of at least an entire technological life cycle).

B. *Recent Scholarship Urging a California Approach*

Scholars continue to clamor for a move to the California approach.<sup>82</sup> For example, Professor Viva Moffat (like many other scholars) argues that non-competes are the product of an inherently flawed bargaining process that has the potential to create harmful chilling effects on employees.<sup>83</sup> She goes farther, however, arguing that non-competes cannot be justified as a tool to protect trade secrets or other intangible assets because non-competes fundamentally upset the balance inherent in trade secret law by extending protection farther than the law provides on its own.<sup>84</sup> Finally, Professor Moffat argues that the diversity of approaches to enforcement of non-competes in states applying the rule of reason has become so muddled and unproductive that the states should adopt a uniform rule of unenforceability of non-competes based on the California model.<sup>85</sup>

Recently, scholars have gone beyond legal and policy-based arguments to hold up the advantages of the California model, drawing on business management, economics, sociology, and organizational research.<sup>86</sup> Professor Orly Lobel, for example, relies heavily on this research in a recent book<sup>87</sup> and introduces her own experimental behavioral study in a recent article.<sup>88</sup> Some business management

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<sup>82</sup> California's ban on non-competes does not always benefit California as creative workers can and do flow to firms in other states. See Tim Higgins & Dana Hull, *Want Elon Musk to Hire You at Tesla? Work for Apple*, BLOOMBERG BUS. NEWS (Feb. 5, 2015, 2:28 PM PST), <http://www.bloomberg.com/news/articles/2015-02-05/want-elon-musk-to-hire-you-at-tesla-work-for-apple?cmpid=yahoo> (describing Nevada-based Tesla's hiring of California-based Apple designers).

<sup>83</sup> See Moffat, *The Wrong Tool*, *supra* note 10, at 885-99.

<sup>84</sup> See *id.* at 911-21.

<sup>85</sup> See Moffat, *Making Non-Competes Unenforceable*, *supra* note 10, at 965-84.

<sup>86</sup> Amir & Lobel, *supra* note 6, at 860 (concluding that the results of a study by management scholars "clearly support the existence of a 'California effect' — a growth advantage for states that do not enforce noncompetes"); Matt Marx, Deborah Strumsky & Lee Fleming, *Mobility, Skills, and the Michigan Non-Compete Experiment*, 55 MGMT. SCI. 875, 879-87 (2009); Moffat, *The Wrong Tool*, *supra* note 10, at 896-98 (discussing social science studies); see also Garmaise, *supra* note 18, at 380-414; Samila & Sorenson, *supra* note 10, at 428-29; Toby E. Stuart & Olav Sorenson, *Liquidity Events and the Geographic Distribution of Entrepreneurial Activity*, 48 ADMIN. SCI. Q. 175, 176-78 (2003) (drawing on organizational demography and sociologically informed literature).

<sup>87</sup> See Amir & Lobel, *supra* note 6, at 837-38; Orly Lobel, *The New Cognitive Property: Human Capital Law and the Reach of Intellectual Property*, 93 TEX. L. REV. 789, 825-28, 840-42, 846-48 (2015). See generally LOBEL, *supra* note 6 (describing Lobel's recent research regarding trade secrets and non-competes).

<sup>88</sup> Amir & Lobel, *supra* note 6, at 852-68.

scholars cast doubt on the predictive qualities of this research,<sup>89</sup> but the crescendo for the California approach seems to be rising as states look for a comparative advantage in creating a haven for innovation.<sup>90</sup> An organization called the Alliance for Open Competition (“AOC”) has been lobbying nationwide for a ban on the enforcement of non-competes.<sup>91</sup> Most prominently, AOC has been supporting efforts to change the law in Massachusetts for Route 128, resulting in legislative activity focused on passage of California-style legislation.<sup>92</sup>

But should all states ban non-competes? Is that the best way to facilitate knowledge spillovers and stimulate innovation or is there a better way? Have Gilson’s words of caution about California’s approach been put to rest and Wood’s call for additional research been satisfied? As previously noted, many scholars now think that the answer is a resounding “yes,” but before reaching that conclusion, let’s examine a previously unexplored but particularly relevant real world case study in legal infrastructure: the law, and most importantly, the practice of enforcing non-competes in the state of Washington.

The next Part begins by showing that Washington rivals California as a state for innovators. It then describes Washington’s law of non-

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<sup>89</sup> “Stepping back and examining these studies as a group from a legal scholarship perspective reveals some inconsistencies and shortcomings of the basis for these empirical studies . . . . Moreover, the verdict on the importance of noncompete law and mobility policy — in terms of helping or harming business activity or workers’ rights — and the role of noncompetes in key issues such as mobility of all types of workers and knowledge transfer is not yet clear.” Bishara, *Fifty Ways to Leave*, *supra* note 18, at 767-68. *See also id.* at 759-67 (surveying and analyzing the research).

<sup>90</sup> *See supra* note 14 and accompanying text.

<sup>91</sup> The AOC “is a group of entrepreneurs, employees, investors and executives dedicated to fostering innovation throughout the US. We seek to breakdown a major barrier to entrepreneurialism: the use of non-competition agreements mandated by employers that force employees to sign away their rights to engage in any business of a competitive nature when they leave their present jobs.” ALLIANCE FOR OPEN COMPETITION, *supra* note 14.

<sup>92</sup> *See also* Carolyn Y. Johnson, *Contract Clauses Called Stifling: Sparking Capital Asks Patrick to Eliminate Noncompete Accords*, BOSTON.COM (Dec. 7, 2007), [http://www.boston.com/business/technology/articles/2007/12/07/contract\\_clauses\\_called\\_stifling/](http://www.boston.com/business/technology/articles/2007/12/07/contract_clauses_called_stifling/). *See generally* Scott Kirsner, *Dear Captains of Industry: Where Is the Data to Support Your Position on Noncompetes?*, BOSTON.COM (Aug. 4, 2009, 7:20 AM), [http://www.boston.com/business/technology/innoeco/2009/08/dear\\_captains\\_of\\_industry\\_wher.html](http://www.boston.com/business/technology/innoeco/2009/08/dear_captains_of_industry_wher.html) (discussing proposed legislation in Massachusetts to make non-competes less restrictive and make sure employees are more informed about non-competes). Legislation to ban non-competes has also been active in Washington State. *See* Todd Bishop, *Cracking Down on Non-Compete Deals: Bill Would Change Wash. State Law to Mirror Calif. Approach*, GEEKWIRE (Feb. 9, 2015, 9:06 AM), <http://www.geekwire.com/2015/cracking-non-compete-deals-bill-change-washington-state-employment-law-mirror-californias-approach/>.

competes, presents research suggesting that enforcement of non-competes is very leaky in practice, and explains the pragmatic reasons for the leakiness. This Part also addresses why the potential chilling effects of non-competes are less significant than scholars fear. Finally, it explains why Washington's leaky enforcement approach to non-competes is superior to California's non-enforcement approach because it better balances knowledge spillovers and trade secret protection.

### III. WASHINGTON AS A PLATFORM FOR INNOVATION AND ITS LEAKY NON-COMPETE LEGAL INFRASTRUCTURE

#### A. *Washington Is a Leading State for Creators and Innovators*

In the past five years, Washington has consistently placed in the top 10 growing states in terms of size,<sup>93</sup> economy,<sup>94</sup> technological advancement,<sup>95</sup> and startup culture.<sup>96</sup> This is due in part to Seattle's status as the fastest growing big city in the U.S.<sup>97</sup> and one of the top 5 cities for tech startups.<sup>98</sup> In fact, Bloomberg recently declared that Washington is the most innovative state in America.<sup>99</sup>

Washington ranked first because it did well in all of Bloomberg's categories.<sup>100</sup> Bloomberg took into account the percentage of each state's population that worked in STEM fields, the percentage with science and technology degrees, the proportion of utility patents

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<sup>93</sup> Ilyce Glink, *Top 10 Fastest-Growing States*, CBS NEWS (Jan. 18, 2014, 6:46 AM), <http://www.cbsnews.com/media/top-10-fastest-growing-states/3/>.

<sup>94</sup> *The 11 States with the Fastest-Growing Economies*, DAILY FINANCE, <http://www.dailyfinance.com/photos/the-states-with-the-fastest-growing-economies/> (last visited Aug. 25, 2014).

<sup>95</sup> *The Top 10 States for Technology*, CNBC, <http://www.cnbc.com/id/48058147/page/6> (last visited Aug. 25, 2014).

<sup>96</sup> See Emily Coyle, *The Top 6 Regions with the Most High-Tech Startups*, WALL ST. CHEAT SHEET (Nov. 11, 2013), <http://wallstcheatsheet.com/stocks/the-top-6-states-with-the-most-high-tech-startups.html?a=viewall>.

<sup>97</sup> Gene Balk, *Census: Seattle Is the Fastest-Growing Big City in the U.S.*, SEATTLE TIMES (May 22, 2014, 12:05 AM), <http://blogs.seattletimes.com/fyi-guy/2014/05/22/census-seattle-is-the-fastest-growing-big-city-in-the-u-s/>.

<sup>98</sup> Catherine Clifford, *The 25 Best U.S. Cities for Tech Startups*, ENTREPRENEUR (Aug. 14, 2013), <http://www.entrepreneur.com/article/227829>.

<sup>99</sup> Dina Bass, *Microsoft, Amazon Propel Washington to Most Innovative State*, BLOOMBERG (Dec. 18, 2013, 9:01 PM), <http://www.bloomberg.com/news/2013-12-19/microsoft-amazon-propel-washington-to-most-innovative-state.html>; Bloomberg Rankings, *Top 20 Most Innovative States*, BLOOMBERG (Dec. 18, 2013, 6:42 PM), <http://www.bloomberg.com/slideshow/2013-12-18/top-20-most-innovative-states.html#slide21>.

<sup>100</sup> *Most Innovative in U.S.: States*, *supra* note 13.

granted to its residents, its government spending on research and development, the gross state product per employed person, its three-year change in productivity, and the percentage of its public companies focused on technology. California had the highest percentage of utility patents granted but had also had a negative three-year change in productivity. Massachusetts had the highest percentage of STEM professionals but a low state government spending rates on R&D. Virginia had high percentages of both STEM professionals and science degree holders but had a low gross state product per worker and a negative three-year productivity change. Texas did well in many categories but had noticeably lower percentages of STEM professionals and holders of science and technology degrees than other top-ranking states. North Carolina had similar results as Texas but had lower gross state products per employed person and a three-year productivity change that was close to zero. Washington, through a balance of a well-educated population, strong economic foundation, and a positive future trajectory, has earned Bloomberg's nod as the most innovative state in America.<sup>101</sup>

#### B. Law of Non-Competes in Washington

Like many other states, Washington has adopted the rule of reason approach and wrestled with how to make enforcement of non-competes as fair as possible for both employers and employees.<sup>102</sup> One of the earliest Washington Supreme Court cases addressing the enforceability of non-compete agreements was *Racine v. Bender*.<sup>103</sup> Bender was a Certified Public Accountant who worked in Racine's

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<sup>101</sup> See generally Jon Talton, *Amazon.com Just Tip of Seattle Boom*, SEATTLE TIMES, April 19, 2015, at D1, D6 (discussing reasons behind Seattle-area tech boom). Technology businesses continue to be attracted to Washington. See Brier Dudley, *Apple Joins the Party, Opens Seattle Office*, SEATTLE TIMES, Nov. 4, 2014, at A7-A8 [hereinafter *Apple Joins the Party*] (reporting that Apple has opened a campus in Washington, joining Twitter, Facebook, Google, and Oracle); Brier Dudley, *Dropbox Dropping into Seattle, Joining Cloud Crowd*, SEATTLE TIMES, Dec. 3, 2014, at A12; Brier Dudley, *Facebook Likes Seattle in a Big Way with New Digs*, SEATTLE TIMES, Feb. 18, 2015, at A1, A10 ("New South Lake Union office . . . is doing some of [Facebook's] most forward projects."); Hanna Hull & Julie Johnsson, *SpaceX Chief Has High Hopes for Seattle Office*, SEATTLE TIMES, Jan. 14, 2015, at A1 (reporting that Elon Musk will be opening a Seattle engineering office to develop and launch space satellites and other high technology ventures).

<sup>102</sup> See generally BRIAN M. MALSBERGER, COVENANTS NOT TO COMPETE: A STATE-BY-STATE SURVEY 4619-60 (7th ed. Supp. 2011) (reviewing Washington's law).

<sup>103</sup> 252 P. 115 (Wash. 1927).



accounting company.<sup>104</sup> Bender left and started his own accounting company, soliciting some of the clients that he had worked for at Racine's company. Racine sought an injunction against Bender, claiming that Bender had violated the warranty found at the bottom of each report that Bender submitted to Racine.<sup>105</sup> This warranty contained language that, in modern terms, would be referred to as a non-compete. The Supreme Court of Washington stated that these restrictions were enforceable "if they meet the test of showing that they are not greater than are reasonably necessary to protect the business or good will of the employer, even though they restrain the employee of his liberty to engage in a certain occupation or business, and deprive the public of the services, or restrain trade."<sup>106</sup>

The Supreme Court of Washington then decided *Wood v. May*.<sup>107</sup> In that case, Wood took on May as his horseshoeing apprentice and made him agree that, if May left or was fired, he would not work in horseshoeing or blacksmithing within one hundred miles of Wood for five years.<sup>108</sup> Using the reasoning from *Racine*, the Court upheld the non-compete but agreed with the trial court that the area restriction in the agreement was unreasonable because it was "both unduly harsh to respondent in curtailing his legitimate efforts to earn a livelihood and unnecessary for the protection of the legitimate interests of appellant."<sup>109</sup> The Court remanded the case to the trial court, ruling that the non-compete could be reformed by the trial court to make it reasonable (i.e., blue penciled) as long as "partial enforcement is possible without injury to the public and without injustice to the parties."<sup>110</sup>

The Washington Court of Appeals in *Alexander & Alexander, Inc. v. Wohlman*<sup>111</sup> distilled the holdings of *Racine* and *Wood* into a 3-factor test of reasonableness that now has become the standard articulation of the test in Washington: "(1) whether restraint is necessary for the protection of the business or good will of the employer, (2) whether it

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<sup>104</sup> *Id.* at 115.

<sup>105</sup> *Id.* at 116.

<sup>106</sup> *Id.* at 116-17.

<sup>107</sup> 438 P.2d 587 (Wash. 1968).

<sup>108</sup> *Id.* at 588.

<sup>109</sup> *Id.* at 589-90.

<sup>110</sup> *Id.* at 591; see also *Sheppard v. Blackstock Lumber Co., Inc.*, 540 P.2d 1373, 1377 (Wash. 1975) (finding forfeiture clause unreasonable and remanding the case to see if the non-compete could be reasonably enforced).

<sup>111</sup> *Alexander & Alexander, Inc. v. Wohlman*, 578 P.2d 530 (Wash. Ct. App. 1978); see also *Amazon, Inc. v. Powers*, No. C12-1911RAJ, 2012 WL 6726538, at \*8 (W.D. Wash. Dec. 27, 2012) (stating the three factor test found in the Court of Appeals decision).

imposes upon the employee any greater restraint than is reasonably necessary to secure the business of the employer or the good will thereof, and (3) whether the degree of injury to the public is such loss of the service and skill of the employee to warrant nonenforcement of the covenant.”<sup>112</sup> After using this test to evaluate the reasonableness of the non-compete, the court is to enforce the agreement only so far as is reasonable.<sup>113</sup>

More recently, the Supreme Court of Washington addressed the type of consideration that is needed for an enforceable non-compete, particularly whether continuing employment in an at-will relationship suffices.<sup>114</sup> In *Labriola v. Pollard Group, Inc.* the employee had signed a non-compete 5 years after being hired, but the employer paid no additional compensation for the non-compete.<sup>115</sup> The Court held that on-going employment is not sufficient consideration for a non-compete signed after the hiring date nor is on-the-job training when the employee comes to the employer with experience and training.<sup>116</sup>

In looking at the development of non-compete law in Washington over the years, the federal district court in *Amazon, Inc. v. Powers* observed that “Washington courts have typically looked favorably on

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<sup>112</sup> *Alexander & Alexander*, 578 P.2d at 539.

<sup>113</sup> *Id.* Cases after *Alexander & Alexander* include: *Perry v. Moran*, 748 P.2d 224, 230 (Wash. 1987) (determining that prohibition on providing accounting services to former employer’s clients is less restrictive than geographic limitation); *Emerick v. Cardiac Study Ctr., Inc.*, 286 P.3d 689, 693-94 (Wash. Ct. App. 2012) (remanding case because trial court had not properly addressed employer’s protectable business interest); *Copier Specialists, Inc. v. Gillen*, 887 P.2d 919, 920 (Wash. Ct. App. 1995) (affirming trial court’s judgment that training acquired during short-term employment “without more, does not warrant enforcement of the covenant not to compete”); *Knight, Vale & Gregory v. McDaniel*, 680 P.2d 448, 452 (Wash. Ct. App. 1984) (finding that “public policy requires us to carefully examine covenants not to compete, even when protection of a legitimate business interest is demonstrated, because of equally competing concerns of freedom of employment and free access of the public to professional services”); *Armstrong v. Taco Time Int’l, Inc.*, 635 P.2d 1114, 1118 (Wash. Ct. App. 1981) (holding that for the non-compete to be reasonable it should read “during the term of the franchise agreement” rather than the broader during the term of the franchise).

<sup>114</sup> Another recent development has been a statute, which makes non-competes in the broadcast industry void if the broadcaster is terminated without just cause. See WASH. REV. CODE § 49.44.190 (2015).

<sup>115</sup> *Labriola v. Pollard Group, Inc.*, 100 P.3d 791, 792 (Wash. 2004).

<sup>116</sup> *Id.* at 836-37; see also *McKasson v. Johnson*, 315 P.3d 1138, 1141 (Wash. Ct. App. 2013) (“Valid incorporation of a non-compete clause requires the employer to give the employee consideration in exchange for the employee’s employment restriction; consideration in this context is an employer’s promise to do something for the employee or to give the employee an additional benefit in exchange for the employee’s agreement to the restriction.”).

restrictions against working with an employee's former clients or customers."<sup>117</sup> However, "Washington courts have been more circumspect when considering restrictions that would prevent an employee from taking on any competitive employment. These general restrictions on competition are more suspect than mere bans on working with former clients or customers."<sup>118</sup> General restrictions will only be supported if the employer can show that their particular field of work necessitates such restrictions.<sup>119</sup> Additionally, Washington courts have no problem limiting the duration or geographic scope of non-compete agreements, especially when the employer cannot demonstrate that such duration or scope is necessary.<sup>120</sup>

Washington's approach to enforcing non-competes is well within the mainstream when compared with other rule of reason jurisdictions. Scholars have developed rating systems to compare the law of non-competes of the different states. For example, Professor Norman Bishara rates each state's enforceability strength on a scale of 1 to 51, with 51 signaling the weakest enforcement. In Professor Bishara's rating system California received a score of 50 and Washington 13. By comparison, Virginia scored 38, North Carolina 35, Texas 32, Massachusetts 18, Michigan 15, and Illinois 4.<sup>121</sup> In Professor Mark Garmaise's "Noncompetition Enforceability Index," rating states from 0 to 9, California received a score of 0 and Washington received a score of 5. Washington's enforceability score ranked higher than North Carolina's 4, Virginia's 3, and Texas' 3; the same as Illinois' and Michigan's 5; and lower than Massachusetts' 6.<sup>122</sup>

Legal scholars since Professor Gilson have evaluated the utility of non-competes by looking primarily at statutes and a handful of reported cases. That is a significant part of the story to be sure but when it comes to knowledge spillovers in high technology sectors, another part of the story is more important: how frequently employers actually enforce non-competes.<sup>123</sup> If creative workers flow from firm to

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<sup>117</sup> *Amazon, Inc. v. Powers*, No. C12-1911RAJ, 2012 WL 6726538, at \*8 (W.D. Wash. Dec. 27, 2012).

<sup>118</sup> *Id.* at \*9.

<sup>119</sup> *Id.*

<sup>120</sup> *Id.*

<sup>121</sup> Bishara, *Fifty Ways to Leave*, *supra* note 18, at 787; see also Evan Starr, *Training the Enemy? Firm-Sponsored Training and the Enforcement of Covenants Not to Compete*, 5-8 (Jan. 25, 2015), [http://www-personal.umich.edu/~starre/papers/JMP/Starr\\_JMP\\_NoAppendix.pdf](http://www-personal.umich.edu/~starre/papers/JMP/Starr_JMP_NoAppendix.pdf) (suggesting modest improvements to Bishara's model).

<sup>122</sup> Garmaise, *supra* note 18, at 420.

<sup>123</sup> See Bishara, Martin & Thomas, *supra* note 29, at 15 ("[V]ery little is understood about the actual deployment of [non-competes] and other postemployment

firm regularly even though an employer could, potentially, enforce a non-compete, then the economy in fact gains the vaunted advantages of knowledge spillovers. Using research from Washington State, I show that the enforcement of non-competes in the technology sector is very leaky. The use of non-competes may be ubiquitous, but enforcement of them is not. Rarely do high technology firms enforce non-competes against employees who depart either to join another firm or to start their own firm. The next Section presents that research. It also addresses why the potentially chilling *in terrorem* effect of non-competes does not significantly slow knowledge spillovers. Indeed, the *in terrorem* effect and the leakiness of non-compete enforcement are related. If creative workers know that firms rarely enforce non-competes, then they will not be frozen in fear of changing firms or starting a new firm.

### C. Washington's Leaky Non-Compete Legal Infrastructure

#### 1. Non-Compete Enforcement Is Very Leaky

I wanted to discover how often Washington's technology firms sue their departing employees to enforce a non-compete. To do that, I performed research to learn: (1) how many non-compete enforcement cases employers filed in Washington's state and federal trial courts, and (2) how many of those cases were related to workers in technology fields.<sup>124</sup> I found that between the years 2005 and 2014,<sup>125</sup> employers filed a total of 32 non-compete enforcement cases against

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restrictions on employee activities in modern business relationships.”); *id.* at 49 (noting that previous papers “used the mere possibility of [non-compete] enforceability regardless of the likelihood of enforcement”). A study by Beck Reed Riden LLP studied only reported non-compete cases. See Russell Beck, *Trade Secret and Noncompete Survey — National Case Graph 2015*, FAIR COMPETITION LAW (Jan. 17, 2015), <http://faircompetitionlaw.com/2015/01/17/trade-secret-and-noncompete-survey-national-case-graph-2015/>.

<sup>124</sup> Using Bloomberg Law's Docket Search tool that tracks court filings for the cases in its database, we searched for all case filings in Washington's state and federal courts that included the terms “noncompete,” “noncompetition,” “not to compete,” and “non-compete.” We then manually looked through the results, determining whether each case was actually related to a non-compete and whether it was in the field of technology. We also searched news databases to see if we could turn up additional cases dealing with non-competes. The searches were performed by my research assistant Peter Montine with assistance from the librarians at the Gallagher Law Library, University of Washington School of Law.

<sup>125</sup> The Bloomberg Law Docket Search database begins with cases in 2005 so that was our starting point.

departing employees in Washington courts.<sup>126</sup> Of those 32 cases, 11 were brought by employers who produce technology-related products or services although at least 3 of those 11 cases involved departing salespeople rather than workers who invent or create<sup>127</sup> and 1 focused on financial information rather than inventive or creative ideas.<sup>128</sup> During that same period of time, however, hundreds of creative workers changed technology firms in Washington.<sup>129</sup>

The details of these cases reveal interesting facts about the leakiness of the non-compete enforcement landscape in Washington's technology sector. Technology giants Microsoft and Amazon.com brought only one case each in the ten-year period, both in response to an employee departing to work for rival Google.<sup>130</sup> Both of these cases settled within a year, allowing the departing employee to work at Google.<sup>131</sup> The balance of the lawsuits came from small to medium sized firms in a wide variety of technology sub-sectors: restoration and

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<sup>126</sup> Appendix A contains a table showing the complete results of our research.

<sup>127</sup> See, e.g., *Gill v. DePuy Spine, Inc.*, No. 2-13-CV-00252-LRS (E.D. Wash. July 9, 2013) (Bloomberg Law); *Fluke Elecs. Corp. v. Cordex Instruments*, No. C12:2082JLR, 2013 WL 566949 (W.D. Wash. Feb. 13, 2013); *CH20, Inc. v. Bernier*, No. C11-5153RJB, 2011 WL 1485604 (W.D. Wash. Apr. 18, 2011).

<sup>128</sup> See *Axtman v. KC Distance Learning, Inc.*, No. C10-1022JLR, \*5 (W.D. Wash. Jan. 9, 2012) (Bloomberg Law).

<sup>129</sup> See also Brier Dudley, *Cuts Come at Hopeful Time for Company, Job Seekers*, SEATTLE TIMES, Sept. 19, 2014, at A8-A9 (describing the good prospects of workers laid off by Microsoft to work at Google, Amazon, and other technology firms); Coral Garnick, *Ignition Partners Ready to Invest Again*, SEATTLE TIMES, May 22, 2015, at A12, A14 (quoting the CEO of a venture capital firm: "You can't find a company these days that doesn't have former Microsoft and Amazon employees"); Vivian Giang, *A New Report Ranks America's Biggest Companies Based on How Quickly Employees Jump Ship*, BUSINESS INSIDER (July 25, 2013, 8:14 PM), <http://www.businessinsider.com/companies-ranked-by-turnover-rates-2013-7>. Cf. Gene Balk, *The Californians Keep Coming, but King County Gives Back*, SEATTLE TIMES (Aug. 30, 2015, 3:35 PM), <http://www.seattletimes.com/seattle-news/data/the-californians-keep-coming-but-king-county-gives-back/> (reporting on the back and forth flow of employees between California and tech hub King County: "Here's a switch: Pretty soon, it might be Californians who get to complain about all the folks from Seattle who keep moving down there").

<sup>130</sup> See *Microsoft Corp. v. Kai-Fu Lee, Google, Inc., and Amazon.com Inc. v. Powers* *infra* Appendix A. Another case involves a non-compete between Microsoft and another software firm that does not involve a departing employee. See *Veritas Operating Corp. v. Microsoft Corp.*, No. C06-0703-JCC, 2008 WL 687117 (W.D. Wash. Mar. 11, 2008) (adopting report and recommendation and granting plaintiff's motion for summary judgment that defendant was not entitled to recover damages for claim infringement, and of non-infringement and invalidity).

<sup>131</sup> See *infra* Appendix A.

environmental control products;<sup>132</sup> health care payment and claims processing software;<sup>133</sup> low cost computer parts;<sup>134</sup> spinal treatment products;<sup>135</sup> wireless electrocardiogram patches;<sup>136</sup> electronics;<sup>137</sup> chemical products used in agriculture and water treatment;<sup>138</sup> litigation discovery software;<sup>139</sup> and online education services.<sup>140</sup> On average these cases settled in less than a year.<sup>141</sup> Apart from the Microsoft and Amazon.com cases mentioned previously,<sup>142</sup> none of the lawsuits garnered any news coverage to speak of.

In sum, the volume of lawsuits brought to enforce non-competes against departing knowledge workers (about 1 per year) was miniscule. The suits were dispersed among many technology sub-sectors, so that no sub-sector was disproportionately impacted by non-compete litigation. Start-up technology ventures were not targeted disproportionately (as some have feared).<sup>143</sup> Cases concluded quickly

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<sup>132</sup> See, e.g., *Dri-Eaz Prods., Inc. v. Nguyen*, No. C11-1654Z, 2012 WL 1537598 (W.D. Wash. May 1, 2012) (litigating company was a restoration products company).

<sup>133</sup> See, e.g., *Edifecs Inc. v. Singh*, No. 2:10-CV-0067-RSL (W.D. Wash. Jan. 11, 2010) (Bloomberg Law) (litigating company provides software solutions).

<sup>134</sup> See, e.g., *Compuvest Corp. v. Dolinsky*, No. C07-1524RAJ, 2009 WL 1604525 (W.D. Wash. June 5, 2009) (litigating company sold computer parts).

<sup>135</sup> See, e.g., *Gill v. DePuy Spine, Inc.*, No. 2:13-CV-00252-LRS (E.D. Wash. July 9, 2014) (Bloomberg Law) (defending company sells spinal products).

<sup>136</sup> See, e.g., *Bardy v. Cardiac Sci. Corp.*, No. C13-0778JLR, 2014 WL 294526 (W.D. Wash. Jan. 27, 2014) (litigating company manufactures medical devices).

<sup>137</sup> See, e.g., *Fluke Elecs. Corp. v. Cordex Instruments*, No. C12-2082JLR, 2013 WL 566949 (W.D. Wash. Feb. 13, 2013) (litigating company manufactures electronic devices).

<sup>138</sup> See, e.g., *CH20, Inc. v. Bernier*, No. C11-5153RJB, 2011 WL 1485604 (W.D. Wash. Apr. 18, 2011) (litigating company manufactures chemical products).

<sup>139</sup> See, e.g., *Elec. Evidence Discovery Inc. v. Chepalis*, No. C07-1929RSL, 2007 WL 4376194 (W.D. Wash. Dec. 13, 2007) (litigating company manufactures software products).

<sup>140</sup> See, e.g., *Axtman v. KC Distance Learning, Inc.*, No. C10-1022JLR (W.D. Wash. Jan. 9, 2012) (Bloomberg Law) (litigating company provides educational software).

<sup>141</sup> Non-compete cases in Washington involving technology firms settled in 11.8 months on average, compared to an average settlement time of 13.7 months for all non-compete cases in Washington. See *infra* Appendix A.

<sup>142</sup> See, e.g., Press Release, Microsoft Corp., Statement from Microsoft Regarding Legal Action Against Google and Former Executive (July 19, 2005), available at <https://news.microsoft.com/2005/07/19/statement-from-microsoft-regarding-legal-action-against-google-and-a-former-executive/> (Microsoft's press release explaining its position in the Kai-Fu Lee litigation); Juan Carlos Perez, *Microsoft, Google Spar in Kai-Fu Lee Case*, INFOWORLD (Sept. 6, 2005), <http://www.infoworld.com/article/2671497/operating-systems/microsoft--google-spar-in-kai-fu-lee-case.html> (reporting on the litigation between Microsoft and Google over Kai-Fu Lee's departure from Microsoft).

<sup>143</sup> See Simon & Loten, *supra* note 25. See generally Evan Starr, Natarajan

with little or no publicity. This evidence suggests that non-compete lawsuits did not significantly block technology-related knowledge spillovers in Washington.

## 2. Pragmatic Reasons For Leaky Enforcement

The evidence of pervasive leakiness of non-competes in Washington should not come as a surprise. Employers are simply making smart business decisions to ignore non-competes; that is, they are engaging in economically rational selective enforcement.<sup>144</sup> Firms need a good reason to bring a lawsuit, a reason that justifies the cost and hassle of litigation and the negative vibe that reverberates when a technology firm gets too aggressive. Pervasive leakiness is perfectly rational, and there is a long list of reasons why it makes sense for employers to enforce non-competes only infrequently.<sup>145</sup>

*Reason Number 1 — Litigation Cost.* Small firms do not have the resources to pay lawyers to bring suit very often or to prolong litigation for too long. Large firms may<sup>146</sup> have more financial resources for litigation but they also have more departing employees to track and worry about. On top of attorneys' fees and court costs, litigation taxes the employer in other ways as well. An employer-plaintiff's employees (often senior executives and key technical

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Balasubramanian & Mariko Sakakibara, *Enforcing Covenants Not to Compete: The Life-Cycle Impact on New Firms* 3, U.S. Census Bureau Center for Economic Studies Paper No. CES-WP-14-27 (Jun 15, 2014), available at [https://faircompetitionlaw.files.wordpress.com/2015/02/more-noncompete-enforcement-equals-fewer-but-better-startups-start\\_nv.pdf](https://faircompetitionlaw.files.wordpress.com/2015/02/more-noncompete-enforcement-equals-fewer-but-better-startups-start_nv.pdf) (evaluating the pros and cons of non-compete enforcement on new firms, including entry rate, size, growth, and survival).

<sup>144</sup> See, e.g., STEVEN LEVY, IN THE PLEX: HOW GOOGLE THINKS, WORKS, AND SHAPES OUR LIVES 282-83 (2011) (reporting that, roughly a year before the Kai-Fu Lee case, Microsoft deeply lamented its loss of key technical executive Mark Lucovsky to Google but apparently took no legal action); DAVID A. VISE, THE GOOGLE STORY 259-60 (2008) (reporting that Google had hired many Microsoft employees before Microsoft eventually sued Kai-Fu Lee).

<sup>145</sup> This list reflects insights gained from my 15-plus years of law practice representing employees and employers of all sizes in the technology industry. See Blake, *supra* note 3, at 691 (noting that employer's now understand that non-competes "are not always costless"). See generally David Barnhizer, *Abandoning an "Unethical" System of Legal Ethics*, 2012 MICH. ST. L. REV. 347, 391-412 (describing factors involved in performing case evaluation); William Lynch Schaller, *Secrets of the Trade: Tactical and Legal Considerations from the Trade Secret Plaintiff's Perspective*, 29 REV. LITIG. 729 (2010) (generally describing the considerations in bringing trade secret litigation).

<sup>146</sup> I say "may" have more resources because it seems unlikely that an unprofitable large company will choose to spend its precious resources on low utility non-compete litigation.

workers) need to spend many hours working with litigation counsel on strategy, discovery, pleadings, affidavits and evidence development, motions, and protective orders. This takes time and focus away from core business and creative activities<sup>147</sup> and most (if not all) creative workers have little patience for it. Litigation is an expensive and disruptive proposition even for a plaintiff, a reality that larger companies know as well or better than smaller ones.

*Reason Number 2 — Counter-Litigation Risk.* Once the employer brings suit, the employee can counterclaim. An employee might counterclaim for unpaid overtime pay or other compensation, breach of contract, or raise an unfair competition claim. These counterclaims often pose risks for the employer that exceeds the expense and potential gains of enforcing a non-compete. These counterclaims persist even if the employer loses the non-compete case. If a trial court dismisses a non-compete case or refuses to grant pre-trial injunctive relief, then the employer probably wants to terminate the litigation but, instead, gets stuck defending a case that it provoked by its own aggressive actions. Even when counterclaims do not seem dangerous to the employer in a given case, there is a danger that an aggressive litigation posture will draw unwanted attention from government agencies such as the Federal Trade Commission, Department of Justice, and the State Attorney General.

*Reason Number 3 — Trade Secret Disclosure Risk.* Many non-compete lawsuits also involve trade secrets. After the employer files suit, the employer must disclose during discovery the particular trade secret information that the employer claims the employee has or might risk misappropriating.<sup>148</sup> The employer must disclose this information not only to the court but also to the employee's litigation counsel and, in many cases, the in-house counsel and certain employees of the competitor who hired the employee (such as Google in the *Microsoft v. Kai-Fu Lee* case). A protective order lessens the risk of improper trade secret disclosure in the course of litigation<sup>149</sup> but many technology

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<sup>147</sup> The Wright brothers' obsession with litigation at the expense of innovation is a good and well known cautionary tale. See LAWRENCE GOLDSTONE, *BIRDMEN: THE WRIGHT BROTHERS, GLENN CURTISS, AND THE BATTLE TO CONTROL THE SKIES* 293-315 (2014).

<sup>148</sup> See generally Dale Kotchka-Alanes, *Trade Secret Misappropriation: Tell Me Your Secret Before I Tell You Whether I Have It*, NAT. L. REV. (Nov. 25, 2014), <http://www.natlawreview.com/article/trade-secret-misappropriation-tell-me-your-secret-i-tell-you-whether-i-have-it> (“[A] number of courts have held that plaintiffs must sufficiently identify their trade secrets before discovery concerning those trade secrets can commence.”).

<sup>149</sup> See, e.g., UNIFORM TRADE SECRETS ACT § 5 (amended 1985) (describing secrecy



firms calculate that the potential danger of disclosure during litigation is greater than the potential benefit of winning a non-compete case. In addition, trial courts in Washington have shown a propensity to scale back the veil of secrecy sought by the litigants in trade secret cases in response to concerns raised about the transparency and openness of public judicial proceedings.<sup>150</sup>

*Reason Number 4* — Proof Problems and Uncertain Outcomes. Employers can enforce a non-compete in Washington courts but they know that it is not easy. Washington's rule of reason was developed by the courts to discourage regular non-compete litigation and it works just that way in practice.<sup>151</sup> Recall that in Washington the employer must prove that (1) the restraint is necessary for the protection of the business or good will of the employer, (2) the restraint does not impose on the employee any greater restraint than is reasonably necessary to secure the business or goodwill of the employer, and (3) the degree of injury to the public caused by loss of the service and skill of the employee is not too great.<sup>152</sup> After using this test to evaluate the reasonableness of the non-compete, the court enforces the non-compete only so far as is reasonable which includes the often difficult task of proving that the departing employee is doing "competitive" work.<sup>153</sup> Employers know that Washington courts often carve back the scope of a non-compete.<sup>154</sup> This creates uncertainty for the employer

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in judicial proceedings, including protective orders).

<sup>150</sup> See *Dreiling v. Jain*, 93 P.3d 861, 870-71 (Wash. 2004); *Seattle Times Co. v. Ishikawa*, 640 P.2d 716, 724 (Wash. 1982).

<sup>151</sup> Some scholars see this as a nation-wide trend: "The emerging law of employee noncompete agreements significantly restricts the power of employers to impose postemployment restrictions on competition. . . . These opinions [in recent cases] have made it more difficult for employers to draft and enforce covenants not to compete in the employment setting." Garrison & Wendt, *supra* note 17, at 148. See *Systems & Software, Inc. v. Barnes*, 886 A.2d 762, 764 (Vt. 2005) ("We have stated that 'we will proceed with caution' when asked to enforce covenants against competitive employment because such restraints run counter to public policy favoring the right of individuals to engage in the commercial activity of their choice.").

<sup>152</sup> See *Amazon, Inc. v. Powers*, No. C12-1911RAJ, 2012 WL 6726538, at \*8 (W.D. Wash. Dec. 27, 2012) (applying the test from *Perry v. Moran*). The burden of proof is on the employer. See BRIAN M. MALSBERGER, COVENANTS NOT TO COMPETE: A STATE-BY-STATE SURVEY 4628 (7th ed. Supp. 2011); see also *Pac. Aerospace & Elecs., Inc. v. Taylor*, 295 F. Supp. 2d 1188, 1198 (E.D. Wash. 2003) (discussing burden of proof for injunctive relief in non-compete case). See generally *Riverview Floral, Ltd. v. Watkins*, 754 P.2d 1055 (Wash. Ct. App. 1988) (for preliminary injunction, employer must establish that an enforceable non-compete exists and has been or is about to be breached).

<sup>153</sup> *Amazon, Inc.*, 2012 WL 6726538, at \*1.

<sup>154</sup> See, e.g., *id.* at \*8 ("If a court finds a restraint unreasonable, it can modify the

who is trying to assess whether litigation to enforce a non-compete will be worth it or not. In the face of this uncertainty, employers normally bring cases where the risk of failing to enforce a non-compete is particularly high, often because the risk of trade secret disclosure is particularly acute. If the departing employee goes to work for a competitor doing work that is not directly competitive or not particularly core to the employer, then it will not be worth the employer's while to sue.<sup>155</sup>

*Reason Number 5* — Public Relations Risk. The public relations risk of non-compete litigation for technology employers is no small matter. They want to hire the best and brightest out of college, away from other firms,<sup>156</sup> or have the opportunity to acquire an entire start-up enterprise primarily for the talented workers.<sup>157</sup> Technology employers want to present their firm as an attractive place for creative workers to come. Non-compete litigation presents a negative vibe that can turn off and turn away creative workers. It might be more descriptive and precise to call this risk a “yuck” or “jerk” concern than a typical public relations issue because it's not just a simple matter of looking bad to customers and the public at large.

*Reason Number 6* — Boomerang Effect. Creative workers change jobs a lot in the information economy.<sup>158</sup> The nature of creative work and the culture of creative workers facilitate this movement.<sup>159</sup> A

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agreement by enforcing it only ‘to the extent reasonably possible to accomplish the contract's purpose.’”); *Wood v. May*, 438 P.2d 587, 590 (Wash. 1968) (ruling that courts should “modify [restrictions] on the basis of [their] factual findings” and not feel “obligated to either accept or reject restrictions In toto”).

<sup>155</sup> Many scholars have expressed concern that a trial court's blue pencil power provides an incentive for employers to write overly broad non-competes with the associated in chilling effect on employees who fear enforcement. Those concerns are important, to be sure, but scholars have failed to note how the uncertainty of outcome that the blue pencil power creates for employers can discourage an employer from enforcing a non-compete.

<sup>156</sup> See RANDALL E. STROSS, *THE MICROSOFT WAY: THE REAL STORY OF HOW THE COMPANY OUTSMARTS ITS COMPETITION* 32-45 (1996) (reporting how attracting excellent programmers makes it easier to attract other programmers of the same caliber).

<sup>157</sup> See John F. Coyle & Gregg D. Polsky, *Acqui-Hiring*, 63 DUKE L.J. 281, 293-94 (2013); Andres Sawicki, *Buying Teams*, 38 SEATTLE U. L. REV. 651, 654 (2015).

<sup>158</sup> See Giang, *supra* note 129.

<sup>159</sup> Several scholars have noted that the work environment for creative workers in the information economy is characterized by mobility and flexibility. See, e.g., PETER CAPELLI, *THE NEW DEAL AT WORK: MANAGING THE MARKET-DRIVEN WORKPLACE* 18 (1999) (characterizing today's typical employment relationship as “an open-ended negotiation based on market power”); Rachel S. Arnow-Richman, *Bargaining for Loyalty in the Information Age: A Reconsideration of the Role of Substantive Fairness in*

software developer, for example, may start her career at one firm, leave to work as an independent contractor for a time, then join a start-up venture, and ultimately return to her first employer. Technology firms know about and expect this boomerang effect.<sup>160</sup> An aggressive approach by an employer to enforcing a non-compete creates a “yuck” factor that may discourage a valuable worker from returning. This makes employers careful not to enforce non-competes unless the circumstances are particularly compelling.<sup>161</sup>

*Reason Number 7* — Talent Quality and Fit Factors. A technology firm may not be sad to see a particular creative worker depart. Some workers do not meet the high expectations of their demanding employer or may be a poor cultural fit for various reasons.<sup>162</sup> Many technology firms want to retain only the most inventive and creative workers who jive with the firm’s mission and work style.<sup>163</sup> These highly competitive technology firms may be pleased if a mediocre or underperforming or misfit employee departs to work for a rival (unless, of course, the employee poses a serious risk of trade secret disclosure).

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*Enforcing Employee Noncompetes*, 80 OR. L. REV. 1163, 1167 (2001) [hereinafter *Bargaining for Loyalty*] (suggesting that employers will turn to non-competes to enforce prior “notions of obligation and commitment” in increasingly short-term modern employment relationships that are contrary to “traditional notions of employee loyalty”); Katherine V.W. Stone, *Knowledge at Work: Disputes over the Ownership of Human Capital in the Changing Workplace*, 34 CONN. L. REV. 721, 722 (2002) (discussing a management consultant’s strategy to “attract and retain valued employees . . . [by] permit[ting] people to customize their jobs to suit their own ambitions and lifestyles”).

<sup>160</sup> Perhaps Steve Jobs and Apple are the most famous boomerang story in the technology industry. See WALTER ISAACSON, *STEVE JOBS* 305-26 (2011). Another interesting story is the near-boomerang of former Microsoft senior vice-president Paul Maritz who became CEO of Microsoft competitor VMWare and then was on the short list to replace Steve Ballmer as CEO of Microsoft. These senior executive boomerangs make headlines but boomerangs are quite ordinary among rank and file creative workers.

<sup>161</sup> See Coyle & Polsky, *supra* note 157, at 302-10.

<sup>162</sup> Google is a good case in point. See KEN AULETTA, *GOOGLED: THE END OF THE WORLD AS WE KNOW IT* 46-65 (2009); LEVY, *supra* note 144, at 121-66; VISE, *supra* note 144, at 240-83. Amazon.com is also a good case in point. See Jodi Kantor & David Streitfeld, *Inside Amazon: Wrestling Big Ideas in a Bruising Workplace*, N.Y. TIMES (Aug. 15, 2015), [http://www.nytimes.com/2015/08/16/technology/inside-amazon-wrestling-big-ideas-in-a-bruising-workplace.html?\\_r=0](http://www.nytimes.com/2015/08/16/technology/inside-amazon-wrestling-big-ideas-in-a-bruising-workplace.html?_r=0) (describing employee turnover due to ill fit in an intense work environment).

<sup>163</sup> A clever disgruntled employee who wishes to leave an unsatisfactory situation can foster his or her employer’s indifference by performing solid but unspectacular work or by working a bit slower than the employer’s hectic pace requires for a top performance review.

*Reason Number 8 — MAD Effect.* It is striking that our research did not uncover many lawsuits between large well-resourced technology firms in Washington. Microsoft and Amazon.com make their home in Washington, of course, but Google, Facebook, Adobe, and Apple (among others) also have significant presences in Washington, all for the express purpose of capitalizing on Washington's excellent market for creative workers.<sup>164</sup> Employees move regularly between these fierce competitors<sup>165</sup> in significant numbers yet the volume of non-compete litigation is tiny. One explanation is that these firms know how to place departing employees in productive but safe (from a non-compete standpoint) positions. In addition, these firms likely fear a steady barrage of non-compete lawsuits in which they take turns playing the role of plaintiff and defendant. This state of "mutually assured destruction ('MAD')"<sup>166</sup> (to borrow the cold war nomenclature), keeps non-compete litigation to a low level.<sup>166</sup>

*Reason Number 9 — Win-Win Effect.* One of the most significant and overlooked reasons that technology firms do not enforce non-competes is that the employee's departure represents a "win-win." That may be true, as explained above, in the context of the Talent Quality and Fit Factor. But often a valued creative worker departs to work for a firm or to start a firm that produces complementary technology or services, or that makes productive use of technology or ideas that an employer has shelved or discarded.<sup>167</sup> These workers leave with (or later receive) the blessing of the former employer; sometimes they also leave with a technology license and perhaps seed funding because they play a critical role in the ecosystem for the employer's technology by contributing to its overall value proposition for customers and to positive network effects.<sup>168</sup>

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<sup>164</sup> See generally Dudley, *Apple Joins the Party*, *supra* note 101 (discussing Apple's presence in Washington).

<sup>165</sup> See Ananya Bhattacharya, *Want to Get a Job at Google or Amazon? Work at Microsoft First*, INC.COM (Feb. 13, 2015), <http://www.inc.com/ananya-bhattacharya/where-tech-firms-look-for-workers.html>.

<sup>166</sup> Another possible reason for low litigation numbers in Washington may be the kind of secret non-poaching agreement that led to litigation in California.

<sup>167</sup> See, e.g., Brier Dudley, *Microsoft Backs Ex-Workers in Taking Its Lync Worldwide*, SEATTLE TIMES, Feb. 26, 2015, at A6, A7 (describing Microsoft's support of a venture by ex-Microsoft employees). In addition, former Microsoft creative worker Gabe Newell founded Valve, which makes highly successful games for the Xbox console, Stephen Purpura founded "big data" analysis company Context Relevant, and Gilad Odinak founded Spoken Communications which develops cloud-based call center software.

<sup>168</sup> See Shira Ovide, *Microsoft's Satya Nadella Makes Peace With Silicon Valley*, WALL ST. J. (Feb. 4, 2015, 12:57 PM), <http://www.wsj.com/articles/microsofts-satya-nadella-makes-peace-with-silicon-valley-1423072674> (describing the importance of building

In sum, from the employer's point of view, an employee's departure normally triggers indifference, enthusiasm or relief, so there is no sensible reason to sue its departing employees over a non-compete. Even when a particular departure triggers concern, employers must weigh the extent of the concern, picking those battles that truly justify the litigation costs of all kinds that I described above. Even when trade secrets are involved, the departing employee may have taken an idea that was too insignificant to justify litigation. Contrary to popular belief, non-compete litigation is anything but a "no brainer."

### 3. Plugging Significant Trade Secrets Leaks

The prior section discussed the reasons why employers do not pursue non-compete litigation but one reason stands out for bringing suit: the risk of significant trade secret loss.<sup>169</sup> The employer can bring a standalone trade secret case, of course, but adding a cause of action for breach of a non-compete augments the trade secret claim.<sup>170</sup> In a trade secret case, the employer must prove that the employee misappropriated trade secret information.<sup>171</sup> This presents two challenges: first, the employer must separate its trade secrets from the employee's general skill and knowledge;<sup>172</sup> and second, the employer must prove that the employee took trade secrets through improper means.<sup>173</sup> These items are often more difficult to prove<sup>174</sup> than that the

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an ecosystem through partnering with other technology firms).

<sup>169</sup> One scholar reports that over two-thirds of all trade secret cases involve departing employees. See David S. Almeling et al., *A Statistical Analysis of Trade Secret Litigation in State Courts*, 46 GONZ. L. REV. 57, 59-60 (2011); see, e.g., *Pacific Aerospace & Elecs., Inc. v. Taylor*, 295 F. Supp. 2d 1188, 1203 (E.D. Wash. 2003) (determining the scope of the injunction to protect trade secrets while still allowing defendant to pursue work through fair competition).

<sup>170</sup> See Arnow-Richman, *Bargaining for Loyalty*, *supra* note 159, at 1204-05; Cynthia Estlund, *Between Rights and Contract: Arbitration Agreements and Non-Compete Covenants as a Hybrid Form of Employment Law*, 155 U. PA. L. REV. 379, 416 (2006); Stone, *supra* note 159, at 747.

<sup>171</sup> See UNIFORM TRADE SECRETS ACT § 1 (amended 1985); RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 40 (1995); RESTATEMENT (FIRST) OF TORTS § 757 (1939).

<sup>172</sup> See *SI Handling Sys. v. Heisley*, 753 F.2d 1244, 1266-69 (3d Cir. 1985). See generally RESTATEMENT (SECOND) OF AGENCY § 396(b) (1958) (describing an employee's right to use his or her skills and general knowledge).

<sup>173</sup> *Economic Analysis of Labor and Employment Law in the New Economy: Proceedings of 2008 Annual Meeting, Association of American Law Schools, Section on Law and Economics*, 12 EMP. RTS. & EMP. POL'Y J. 327, 340 n.43 (2008).

<sup>174</sup> See, e.g., *Loftness Specialized Farm Equip. Inc. v. Twiestmeyer*, 742 F.3d 845, 850-51 (8th Cir. 2014) (discussing burden of proof).

employee went to work for a competitor on competitive technology.<sup>175</sup> Indeed, one of the most sympathetic sorts of non-compete cases, and thus one of the easiest to win, is a case in which the employer faces a serious threat of trade secret loss to the employer's direct competitor via the inevitable disclosure of trade secret information by a departing employee.<sup>176</sup> If a non-compete case can help plug a dangerous trade secret leak, then an employer may well decide that it makes good sense to pursue it.<sup>177</sup>

#### 4. Assessing Potential Chilling Effects: More Freedom Than Fear

The lawsuits themselves are only part of the story, of course. We worry that the threat of litigation, reinforced by the knowledge that employers do in fact bring lawsuits against departing employees, keeps creative workers on the sidelines.<sup>178</sup> To what extent does this potential chilling effect prevent knowledge spillovers in Washington? To ask the question in a different way in light of the research presented above: are a few, widely dispersed, quickly concluded, rarely publicized lawsuits deterring hundreds of creative workers from changing firms or starting new firms in Washington? Or, perhaps, are the workers getting a different message from the leakiness — a message of freedom rather than of fear? I turn now to these questions.

Scholars have often voiced concerns about the chilling effects of non-compete litigation, the so-called *in terrorem* effect.<sup>179</sup> This concern

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<sup>175</sup> See *Comprehensive Tech. Int'l Inc. v. Software Artisans, Inc.*, 3 F.3d 730, 739 (4th Cir. 1993) *vacated on petition for reh'g* (1993) ("It will often be difficult, if not impossible, to prove that a competing employee has misappropriated trade secret information belonging to his former employer.").

<sup>176</sup> See, e.g., *Reed, Roberts Assocs. v. Strauman*, 353 N.E.2d 590, 593-94 (N.Y. 1976) (holding that non-competes are unenforceable if the former employer's customer list was not stolen, the employee's knowledge does not qualify as trade secret, and employee's services are not unique or extraordinary).

<sup>177</sup> See, e.g., *Newell Rubbermaid, Inc. v. Storm*, No. 9398-VCN, 2014 WL 1266827, at \*10-11 (Del. Ch. Mar. 27, 2014) (granting temporary restraining order where it is likely that plaintiff will suffer irreparable harm without interim injunctive relief).

<sup>178</sup> See *Richard P. Rita Pers. Servs. Int'l, Inc. v. Kot*, 191 S.E.2d 79, 81 (Ga. 1972); *Reddy v. Cmty. Health Found. of Man*, 298 S.E.2d 906, 916-17 (W. Va. 1982); see also *Simon & Loten*, *supra* note 25 (stating that more than 60% of former employees get sued by their former employers).

<sup>179</sup> See, e.g., *Blake*, *supra* note 3, at 683 (acknowledging the possibility of *in terrorem* effects of non-competes but arguing that courts need discretion through a general approach to "tailor the covenant to provide such protection with a minimum burden to the employee" where the restraints on the employee are generally fair and designed to protect the employer's legitimate interests); Phillip J. Closius & Henry M. Schaffer, *Involuntary Nonservitude: The Current Judicial Enforcement of Employee*

makes good sense. Everyone can imagine a departing employee complying with a non-compete simply out of fear of being sued. We picture a risk adverse worker, perhaps lacking legal sophistication, without the financial means to withstand a non-compete lawsuit. We see in our minds a worker frozen in his or her current position or forced out of the work force through fear of litigation. We also imagine an employer with the knowledge, will, incentive, and financial means to pursue non-compete litigation. We picture a real and present danger. But, unfortunately, this stylized story deceives us. By and large, both employees<sup>180</sup> and employers<sup>181</sup> in the technology sector approach non-competes in a more nuanced, sophisticated way than this simple sketch suggests. The closer we look and the more we learn, the more we see that the *in terrorem* effect is less than meets the eye.

Let's return to the setting described in the prior section.<sup>182</sup> Every day, hundreds of creative workers in Washington who have signed non-competes change firms or start new firms. Rarely does a technology firm sue a departing employee to enforce the non-compete. Even when a firm brings suit, the potential chilling effect is dispersed among various technology sub-sectors and not widely publicized. Sometimes the litigation impact is muted because the departing employee's new firm (e.g., Google in the *Microsoft v. Kai-Fu Lee* case) or a venture capitalist (for a hot start-up) funds the employee's legal expenses and provides savvy advice on how to navigate around, defend or settle a non-compete suit. Typically the lawsuit ends quickly with the worker joining the new firm within a short period of time.

In other words, there is no data suggesting that Washington's creative workers should fear non-compete lawsuits and, as the saying goes, "No data is data." Except when the threat of trade secret loss is particularly acute, technology employers signal through leaky enforcement of non-competes that creative workers can move freely. The abiding lesson that most creative workers take from the pattern of systematic non-compete non-enforcement in Washington State is that

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*Covenants Not to Compete — A Proposal for Reform*, 57 S. CAL. L. REV. 531, 532 (1984) ("Regardless of their validity and enforceability, covenants not to compete chill the free movement of employees and eliminate competition among actual and potential employers."); Moffat, *The Wrong Tool*, *supra* note 10, at 888-90 (discussing the *in terrorem* effects of employer overreach in non-competes).

<sup>180</sup> Professor Harlan's seminal article from the early 1960's indicates that even in that era highly trained technical, engineering, and research personnel were often sophisticated enough to negotiate non-competes. See Blake, *supra* note 3, at 627.

<sup>181</sup> *Id.* at 687-89 (outlining a nuanced approach to non-competes that should be undertaken by employers).

<sup>182</sup> See *supra* Part III.C.1.

they have little to fear from non-competes. Departing employees experience more freedom than fear. Thus, Washington's creative workers are simply (and quite rationally) engaged in the efficient breach of non-competes on a large scale.

The worker's feeling of safety from non-compete litigation is enhanced because an employer seldom knows where the departing employee is working next. If the departing employee is starting a new venture, it often takes a significant amount of time to incubate a technology start-up — to develop the firm's technology, raise capital, and write the business plan. By that time, the non-compete has expired or lost its potency because it has nearly expired.<sup>183</sup> This natural stealth effect means that, from a practical standpoint, technology employers only enforce non-competes when they discover a particular dangerous or egregious situation presented by a departing employee.

In addition, creative workers are clever enough to find productive but not directly competitive work in their next position. For example, a software programmer that worked on operating system memory management code might take a position working on file system or directory software. In the information economy the types of inventive and creative works that need to be produced are so plentiful and so diverse that there is little concern that a worker will find himself or herself without something productive to do. In other words, if an employee leaves Microsoft, he or she will have little difficulty finding interesting and productive but not dangerously competitive work at Amazon.com, Apple, Facebook, or Google. Indeed, creative workers are accustomed to applying their knowledge and talent in different contexts because many technology firms think it is a best practice to rotate their creative workers through many different types of assignments so that they can apply new insights and perspectives that they bring from prior assignments.<sup>184</sup>

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<sup>183</sup> The more time that passes after the employee's departure, the less inclined a court might be to grant an emergency temporary restraining order or preliminary injunction because the danger does not seem particularly imminent or acute. See *EarthWeb, Inc. v. Schlack*, 71 F. Supp. 2d 299, 312 (S.D.N.Y. 1999); Bishara, Martin & Thomas, *supra* note 29, at 36 (reporting that most non-compete lengths were 1–2 years).

<sup>184</sup> See Joseph P. Fishman, *Creating Around Copyright*, 128 HARV. L. REV. 1333, 1334 (2015) (drawing on work from cognitive psychology, management studies, and art history to show the overlooked creative upside of constraints); Stine Grodal & Grid Thoma, *Cross-Pollination in Science and Technology: Concept Mobility in the Nanobiotechnology Field*, ANNALES D'ECONOMIE ET DE STATISTIQUE, 3-4 (2009), available at <http://ssrn.com/abstract=1394375> (discussing cross-pollination of knowledge among different institutional environments); Charles Coy, *Why Rotating Employees Through Your Company Is a Win-Win*, CORNERSTONE BLOG (Apr. 24, 2013), <http://www>.



In this environment, creative workers have little to fear from non-competes and they know it.<sup>185</sup> They are sophisticated enough to realize that even if they get sued, someone may pick up their legal expenses, the suit will end quickly, and in the end they can work for the new firm with relatively minor wrinkles.<sup>186</sup> At worst, a lawsuit provides an opportunity for the employer and departing employee to “right size” the scope of the non-compete to fit the specific circumstances that have arisen. However, it’s not a perfectly rational world, of course, so sometimes technology firms sue creative workers over non-competes when sound reason should dictate otherwise and when it is unfair to drag the employee into litigation. These types of lawsuits contribute strongly to the danger of an *in terrorem* effect, so Part IV offers some proposals to reduce this concern.

##### 5. The Comparative Advantage of the Washington Way

Washington’s leaky legal infrastructure for non-competes enables capacious knowledge spillovers just as California’s ban on non-competes does. This may come as a surprise to scholars who cite Professor Gilson’s article for the proposition that California’s approach is uniquely situated to foster innovation. It will not come as a surprise, however, to those who noticed Gilson’s ultimate conclusion that a rule of reason approach could support innovation equally well.<sup>187</sup> Indeed, Washington’s way of approaching non-compete enforcement possesses one important advantage over California’s approach: in Washington, technology firms (large and small)<sup>188</sup> can use non-competes to help plug significant trade secret leaks.

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cornerstoneondemand.com/blog/employee-rotation-works#.VV5aqZO2oYt.

<sup>185</sup> *But see* Marx, *supra* note 29, at 695 (“In-depth interviews with 52 randomly sampled patent holders in a single industry, coupled with a survey of 1,029 engineers across a variety of industries” suggest that “ex-employees subject to non-competes are more likely to . . . involuntarily leave their technical field to avoid a potential lawsuit.”); Marx, Strumsky & Fleming, *supra* note 86, at 875 (arguing that “enforcement of noncompetes attenuates mobility” and that noncompete enforcement decreases mobility most sharply for inventors with “firm-specific skills and for those who specialize in narrow technical fields”).

<sup>186</sup> *See* LEVY, *supra* note 144, at 281-83 (reporting how Kai-Fu Lee contacted Google while still employed as a Vice President at Microsoft and describing the non-compete lawsuit brought by Microsoft against Mr. Lee and Google which ended in a settlement allowing Mr. Lee to work at Google).

<sup>187</sup> Professor Gilson’s article counseled against adopting the inevitable disclosure doctrine, which he believed would impede knowledge spillovers in states using the rule of reason approach. *See* Gilson, *supra* note 8, at 622-27.

<sup>188</sup> Scholars note that trade secret protection is particularly important to small

On its face, California's ban on non-competes seems so clear and so absolute that use of a non-compete to protect a trade secret is out of the question.<sup>189</sup> As the California Supreme Court put it in *Edwards v. Arthur Andersen*: "Under the statute'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."<sup>190</sup> Nonetheless, some courts have suggested that California law contains a trade secret exception to California's ban on non-competes but the California Supreme Court in *Edwards* declined to address whether such an exception exists.<sup>191</sup> Part IV explains why California courts should adopt the trade secret exception.

#### IV. PROPOSALS FLOWING FROM THE WASHINGTON CASE STUDY

##### A. California Should Recognize Its "Trade Secret Exception"

Section 16600 voids any contract "by which anyone is restrained from engaging in a lawful profession, trade, or business." The California Supreme Court in *Edwards v. Arthur Andersen* ruled that it will not allow judicially created exceptions to Section 16600. That ruling, however, does not mean that California's ban on non-competes is incompatible with the protection of trade secrets provided by California's version of the Uniform Trade Secrets Act ("UTSA").<sup>192</sup> Trade secret protection is particularly important for California's start-up businesses and established firms such as Google that rely on trade secret protection more than patents.<sup>193</sup>

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firms that drive innovation in developing fields. See Josh Lerner, *The Importance of Trade Secrecy: Evidence from Civil Litigation* (Harv. Bus. School, Working Paper No. 95-043, 1999).

<sup>189</sup> Interestingly, a recent study of large company CEO employment contracts involving sophisticated parties represented by legal counsel showed that over 60% of sample employment contracts of firms headquartered in California contained a non-compete. Bishara, Martin & Thomas, *supra* note 29, at 34.

<sup>190</sup> *Edwards v. Arthur Andersen*, 189 P.3d 285, 289 (Cal. 2008).

<sup>191</sup> See *id.* at 291 n.4. The possible trade secret exception can be traced to language in *Gordon v. Landau*, 321 P.2d 456, 457-58 (Cal. 1958), and *Muggill v. Reuben H. Donnelley Corp.*, 398 P.2d 239, 242-43 (Cal. 1965). See also *Fowler v. Varian Assocs., Inc.*, 241 Cal. Rptr. 539, 545 (Ct. App. 1987) (noting that agreements designed to protect proprietary information do not violate section 16600).

<sup>192</sup> CAL. CIV. CODE tit. 5 § 3426 (2015); see Todd M. Malynn, *Edwards v. Arthur Andersen LLP: The End of Judicially Created Restraints on Competition*, 18 J. ANTI. & UNFAIR COMP. L. SEC. ST. B. CAL. 35, 36-37 (2009) (discussing California's Uniform Trade Secrets Act).

<sup>193</sup> See ROBERT P. MERGES ET AL., INTELLECTUAL PROPERTY IN THE NEW

The UTSA provides a collection of remedies that courts can award for trade secret misappropriation, including emergency pre-trial injunctive relief, which is typically the most important remedy in trade secret litigation.<sup>194</sup> The UTSA permits a court to enjoin both actual and “threatened” misappropriation.<sup>195</sup> This raises the distinct possibility that a court could order a departing employee to avoid certain work assignments due to the imminent threat of improper use or disclosure of trade secrets. The focus of the court’s action in this case is not the enforcement of a contract restraining an employee from engaging in his or her “profession, trade, or business.” Rather, the focus is on fashioning the most (and often the only) meaningful remedy under the UTSA. An employee’s Non-disclosure Agreement (“NDA”) may be part of the equation to be sure<sup>196</sup> but the court is not primarily concerned with enforcing a contract; the court is concerned with remedying the threat of trade secret misappropriation, separate and apart from and over and above, the contract.

When viewed in this light, perhaps it is unhelpful to say that Section 16600 needs a “trade secret exception.”<sup>197</sup> Section 16600 is concerned with voiding private contracts that restrain an employee’s freedom to work; the UTSA is concerned with preventing actual and threatened trade secret misappropriation using all the remedies specified in the statute.<sup>198</sup>

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TECHNOLOGICAL AGE 35 (5th ed. 2012).

<sup>194</sup> UNIFORM TRADE SECRETS ACT § 2 (1985).

<sup>195</sup> *Id.* § 2(a).

<sup>196</sup> The UTSA requires that trade secret holders use reasonable measures to protect their trade secrets. *Id.* § 1(4)(ii). A Non-disclosure Agreement (“NDA”) is an industry standard trade secret protection measure which uses contract law to help guard against the improper use or disclosure of trade secrets. *See* GOMULKIEWICZ ET AL., LICENSING INTELLECTUAL PROPERTY: LAW & APPLICATION 298-99 (3d ed. 2014). The UTSA prohibits the misappropriation of trade secrets in the absence of a NDA, of course, but a NDA serves useful signaling and notice functions.

<sup>197</sup> It is also unhelpful to think of this in terms of the so-called “evitable disclosure doctrine” which Professor Gilson frowned on and has been rejected by a California court of appeals. *See* Whyte v. Schlage Lock Co., 125 Cal. Rptr. 2d 277, 293-94 (Ct. App. 2002). Indeed, some commentators note that the “inevitable disclosure doctrine” is mislabeled as a “doctrine” and that it is better understood simply as an equitable tool. *See* Brandy L. Treadway, *An Overview of Individual States’ Application of Inevitable Disclosure: Concrete Doctrine or Equitable Tool?*, 55 SMU L. REV. 621, 649 (2002).

<sup>198</sup> *See* David Lincicum, Note, *Inevitable Conflict?: California’s Policy of Worker Mobility and the Doctrine of “Inevitable Disclosure,”* 75 S. CAL. L. REV. 1257, 1274-80 (2002) (concluding that there is no conflict between the UTSA and section 16600 so long as disclosure of a trade secret is truly inevitable and it would be impossible for the employee to perform in the new job without violating the duty of confidentiality to the previous employer); *see also* Jennifer L. Saulino, Note, *Locating Inevitable Disclosure’s Place in Trade Secret Analysis*, 100 MICH. L. REV. 1184, 1190-91 (2002).

Indeed, in almost every case, the court will allow the departing employee to work for a competitor although the court will often provide parameters for how the employee can work in a manner that adequately protects its former employer's trade secrets. In other words, to borrow a fact pattern from a recent case,<sup>199</sup> an injunction that orders a software programmer to avoid working on smart phone operating systems for a period of time is a UTSA allowed, judicially tailored remedy to channel a departing employee's scope of work in a safe direction, rather than enforcement of a contract that restrains an employee from engaging in a profession that runs afoul of Section 16600.

Even if enforcement of the UTSA is called a "trade secret exception" to Section 16600, California should embrace it. California trial courts need to deploy all remedies allowed by the UTSA, including remedies that limit work to the extent necessary to protect trade secrets, so that the statute can fully do its important work to foster innovation. With this approach, California can create a legal infrastructure comparable to Washington's leaky non-compete infrastructure but coming at it from a different direction.

Trial courts, of course, should avoid granting injunctive relief that looks like the overly broad language found in many non-competes.<sup>200</sup> Instead, trial courts should grant injunctions that look like the settlement agreements that employers and departing employees enter into which right-size the employee's new job description to avoid trade secret misappropriation issues.<sup>201</sup> That approach encourages safe and fair competition, which are two of the primary goals of trade secret law.<sup>202</sup> Part IV.B proposes guiding principles for trial courts to

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<sup>199</sup> See *Amazon.com, Inc. v. Powers*, No. C12-1911RAJ, 2012 WL 6726538, at \*3-4 (W.D. Wash. Dec. 27, 2012).

<sup>200</sup> Some scholars believe that recent cases indicate that trial courts are already giving heightened scrutiny to non-competes. Garrison & Wendt, *supra* note 17, at 135.

<sup>201</sup> See LEVY, *supra* note 144, at 283 (reporting that trial judge Steven Gonzalez prohibited Kai-Fu Lee from sharing proprietary information or helping Google with competitive technologies such as search and speech recognition but allowing him to participate in the establishment of Google's operation in China which was the primary reason that Google had recruited Mr. Lee); see also *EarthWeb, Inc. v. Schlack*, 71 F. Supp. 2d 299, 304-05 (S.D.N.Y. 1999) (discussing how knowledge may become quickly obsolete in the digital world).

<sup>202</sup> Trade secret law has roots in tort law, which remedies injurious appropriation of someone's valuable secret information. Early trade secret cases in the United States drew on principles set out in the first Restatement of Torts. See *RESTATEMENT (FIRST) OF TORTS* § 757 (1939). In addition to its tort underpinnings, trade secret law has roots in the law of unfair competition. See *Balboa Ins. Co. v. Trans Global Equities*, 267 Cal. Rptr. 787, 795 (Ct. App. 1990) ("[A]t bottom, trade secret protection is itself but a branch of unfair competition law."). As a result, the third Restatement of Unfair

follow that encourage this targeted, context driven approach to injunctive relief in departing employee cases.<sup>203</sup>

### B. Guiding Principles for Granting Pre-Trial Injunctive Relief

The trial court's approach to granting remedies in non-compete cases plays a critical role in patrolling the boundary between protecting legitimate knowledge spillovers and preventing trade secret misappropriation.<sup>204</sup> Given the importance of pre-trial injunctive relief in non-compete cases,<sup>205</sup> I propose a set of four guiding principles for assessing whether a trial court should grant a temporary restraining order or preliminary injunction. These guiding principles focus the trial court's attention on trade secret protection where the argument for enforcement of non-competes is strongest. The guiding principles can be illustrated by this chart:

#### Likelihood of Injunctive Relief

LESS	MORE
Trade secret value low	Trade secret value high
Employment not directly competitive	Employment directly competitive
Misappropriation threat remote	Misappropriation threat imminent
Misappropriation injury unclear	Misappropriation injury clear

These guiding principles suggest that a trial court should only grant pre-trial injunctive relief in cases where the employer's trade secrets are valuable and the departing employee will be working for a

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Competition contains a detailed articulation of trade secret law. See RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 39 (1995).

<sup>203</sup> See Garrison & Wendt, *supra* note 17, at 110 ("The court read the noncompetition and nonsolicitation paragraph of Lee's Microsoft Employment Agreement narrowly."); *supra* Part IV.B.

<sup>204</sup> Commentators have noted the importance of remedies for maintaining balance in intellectual property law. See Orit Fischman Afori, *Flexible Remedies as a Means to Counteract Failures in Copyright Law*, 29 CARDOZO ARTS & ENT. L.J. 1, 18-24 (2011); Robert W. Gomulkiewicz, *Fostering the Business of Innovation: The Untold Story of Bowers v. Baystate Technologies*, 7 WASH. J.L. TECH. & ARTS 445, 457-64 (2012); Peter Lee, *The Evolution of Intellectual Infrastructure*, 83 WASH. L. REV. 39, 102-03 (2008); see also Robert W. Gomulkiewicz, *Enforcement of Open Source Licenses: The MDY Trio's Inconvenient Complications*, 14 YALE J.L. & TECH. 106, 124-25 (2011) (arguing for a remedies-based approach).

<sup>205</sup> See Bishara, Martin & Thomas, *supra* note 29, at 46.

competitor doing work that is actually competitive with the work that the employee did for the former employer. Moreover, the trial court must be convinced that the threat of trade secret misappropriation is imminent and the injury to the former employer is clear.<sup>206</sup>

### C. Two Ways to Reduce In Terrorem Effects of Non-Competes

As discussed above, one of the gravest concerns about non-competes is their potential *in terrorem* effect. Part III explained why the chilling effect of non-competes is less than feared when non-compete enforcement is leaky. However, more can and should be done to reduce any fears that creative workers have of unfair enforcement of non-competes by their former employers.

#### 1. Non-Compete Litigation Insurance

Every automobile driver fears the consequences of getting in an automobile accident. Drivers reduce that fear by purchasing insurance. Auto insurance eliminates two important concerns: (1) litigation costs and (2) damages. Non-compete litigation insurance could eliminate the same two fear factors for creative workers in the technology industry.<sup>207</sup> Indeed, purchasing insurance which guarantees pre-paid, well qualified legal counsel in a non-compete lawsuit would be particularly useful because finding and paying for lawyers is the often the biggest concern of a departing employee who is sued by his or her former employer. The insurance could also compensate the worker for wages lost if the former employer successfully enforces the non-compete. Many creative workers in the technology industry would be sophisticated enough to pursue non-compete litigation insurance but for those who cannot or do not pursue insurance, the next section suggests another way to reduce *in terrorem* risks of non-competes.

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<sup>206</sup> See Lincicum, *supra* note 198, at 1277.

<sup>207</sup> In response to potential threats of patent litigation for use of open source Linux software, insurance companies offered insurance to reduce users' fear of litigation. See Steven Vaughan-Nichols, *Open-Source Insurance Provider Finds Patent Risks in Linux*, EWEEK (Aug. 2, 2004), <http://www.eweek.com/c/a/Linux-and-Open-Source/OpenSource-Insurance-Provider-Finds-Patent-Risks-in-Linux>; see also Jennifer E. Rothman, *Best Intentions: Reconsidering Best Practices Statements in the Context of Fair Use and Copyright Law*, 57 J. COPYRIGHT SOC'Y U.S.A. 371, 374-75 (2010) (describing insurance for claims of copyright fair use).

## 2. Attorneys' Fees Legislation

As just mentioned, one of the most serious threats that a departing creative worker faces (and fears acutely) is the cost of non-compete litigation. Even if the employee ultimately prevails or the case settles, he or she may be saddled with a large bill for attorneys' fees. State legislation could address this concern. A state could pass legislation that allows a trial court to award attorneys' fees to a prevailing employee in a non-compete lawsuit.

Several states allow the prevailing party to recover attorneys' fees via their unfair competition<sup>208</sup> or general civil law<sup>209</sup> statutes, which may apply to non-compete litigation. A few states specifically address non-competes. Florida, for example, permits the prevailing party in a non-compete case (employer or employee) to recover its attorneys' fees,<sup>210</sup> and state statutes that target non-competes in the broadcast industry allow the employee to recover attorneys' fees.<sup>211</sup> Texas law takes a particularly nuanced approach. The Texas statute addressing non-competes contains the following provision:

If . . . the [employee] promisor establishes that the promisee knew at the time of the execution of the agreement that the covenant did not contain limitations as to time, geographical area, and scope of activity to be restrained that were

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<sup>208</sup> See, e.g., IOWA CODE ANN. § 553.12 (2015) (allowing for recovery of "the necessary costs of bringing suit, including a reasonable attorney fee" for prohibited restraint on trade or commerce); MINN. STAT. ANN. § 325D.57 (2015) (permitting treble damages, costs, disbursements, and reasonable attorneys' fees for unlawful restraint of trade); MO. STAT. § 416.031, .121 (2015) (awarding treble damages, reasonable attorneys' fees, and costs of suit for unlawful restraint of trade).

<sup>209</sup> See, e.g., ARIZ. REV. STAT. ANN. § 12-341.01 (2015) (authorizing the court to award reasonable attorney fees for "contested action arising out of a contract, express or implied"); ARK. CODE ANN. § 16-22-308 (2015) (permitting collection of attorney's fee as costs in civil actions unless otherwise prohibited by law or contract); IDAHO CODE ANN. § 12-120 (2015) (requiring plaintiff to make written demand on defendant for attorney's fees in some instances).

<sup>210</sup> FLA. STAT. § 542.335(k) (2015).

<sup>211</sup> See, e.g., CONN. GEN. STAT. § 31-50b(c) (2015) (allowing broadcast employees to recover damages", together with court costs and reasonable attorney's fees" for violations of the section); D.C. CODE § 32-533 (2015) ("Any broadcasting industry employer who violates § 32-532 shall be liable for damages, attorney's fees, and costs."); 820 ILL. COMP. STAT. 17/10 § 15 (2015) (providing that violations of prohibition on "post-employment covenants not to compete" are remedied through award of civil damages, attorney's fees, and costs); MASS. GEN. LAWS ANN. Ch. 149, § 186 (2015) (permitting recovery of "reasonable attorneys' fees and costs associated with litigation" of a void and unenforceable post-employment area and time restriction).

reasonable and the limitations imposed a greater restraint than necessary to protect the goodwill or other business interest of the promisee, and the promisee sought to enforce the covenant to a greater extent than was necessary to protect the goodwill or other business interest of the promisee, the court may award . . . reasonable attorney's fees.<sup>212</sup>

On the surface, giving both the employer and the employee the ability to recover attorneys' fees seems even handed. However, if an employer can recover attorneys' fees, then this may actually increase the chilling effect of non-competes. Not only will the departing employee fear paying a large bill to his or her lawyers, the employee will further fear paying a large bill of the employer's lawyers.<sup>213</sup> Thus, an attorneys' fees statute in the non-compete arena should rebalance the unequal bargaining position<sup>214</sup> between employer and employee and reduce chilling effects by allowing only prevailing employees to recover attorneys' fees.<sup>215</sup> Texas' statute provides one model for this approach. It allows an employee to recover attorneys' fees if an employer overreaches as it attempts to enforce a non-compete. However, the Texas law only applies if the employer knew at the time of the agreement that the non-compete was overly broad. Simply allowing a prevailing employee to recover attorneys' fee would be cleaner and better at reducing chilling effects. Indeed, this is the approach taken by Hawaii<sup>216</sup> and in several

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<sup>212</sup> TEX. BUS. & COM. CODE ANN. § 15.51 (2015).

<sup>213</sup> Cf. Robert A. Brown & James P. Clements, *A Patent-Troll Bill with Bad College Grades*, WALL ST. J. (Apr. 14, 2015, 6:48 PM), <http://www.wsj.com/articles/a-patent-troll-bill-with-bad-college-grades-1429051694> (objecting to a "loser pays" attorneys' fee provision in proposed patent troll legislation as creating the wrong litigation incentives).

<sup>214</sup> Note, however, that for small firms the inequality in bargaining power is less clear and, moreover, since small firms lean heavily on trade secret protection, they often have a particularly compelling need to enforce a non-compete.

<sup>215</sup> States that decide to reduce chilling effects by allowing only employees to recover attorneys' fees in non-compete cases may also need to consider potentially conflicting attorneys' fees provisions in general civil law and unfair competition statutes that allow the "prevailing party" to recover fees. For example, several states provide that if a contract allows one party to recover attorneys' fees, then the other party is entitled to recover attorneys' fees as well. See CAL. CIV. CODE § 1717 (2015); FLA. STAT. § 57.105(7) (2015); MONT. CODE ANN. § 28-3-704 (2015); ORE. REV. STAT. § 20.096(1) (2015); UTAH CODE ANN. § 78B-5-826 (2015); WASH. REV. CODE § 4.84.330 (2015). A state could, by statute, void any contractual provision in a non-compete that allows the employer to recover fees if it prevails or limit the recovery of fees to situations where the employer's trade secrets or good will are threatened. Cf. FLA. STAT. 542.335(k) (2015) ("A court shall not enforce any contractual provision limiting the court's authority under this section.").

<sup>216</sup> HAW. REV. STAT. § 607-9 (2015).



state statutes aimed at protecting employees in the broadcast industry from unfair non-competes.<sup>217</sup>

Moreover, the statute could define an employee “prevailing” in litigation to include a case in which the trial court blue pencils or only partially enforces a non-compete because of its over breadth. By doing this, the legislation encourages employers to draft more reasonable non-competes on the front end<sup>218</sup> rather than drafting broad non-competes and hoping for the best in enforcement litigation (an approach that scholars fear enhances the *in terrorem* effect of non-competes).<sup>219</sup> The legislation could require an employer to inform an employee of the attorneys’ fees legislation at the same time that the employee is asked to agree to the non-compete as well as in any demand letter that the employer sends to the departing employee threatening non-compete litigation. This type of notice would maximize the fear-reducing nature of the legislation

#### D. *The Washington Way Is Not Just Washington’s Way*

Part III described Washington State’s leaky non-compete legal infrastructure. I called this “the Washington way.” However, I doubt that the Washington way is only Washington’s way. I would not be surprised if future research revealed leaky non-compete enforcement in the technology sector of many other states that take a rule of reason approach to enforcing non-competes.<sup>220</sup> In those states where enforcement of non-competes may not be leaky at present, courts should duly note the advantages for innovation of relatively capacious knowledge spillovers and encourage leakiness by enforcing non-competes with pre-trial injunctive relief only when valuable trade secrets are genuinely at risk of misappropriation.<sup>221</sup> Lawyers counseling

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<sup>217</sup> See *supra* note 211.

<sup>218</sup> See Blake, *supra* note 3, at 687-89 (discussing the importance of drafting appropriately scoped non-competes).

<sup>219</sup> A court may refuse to enforce an overbroad non-compete if it finds that the employer did not act in good faith. See, e.g., Cent. Adjustment Bureau, Inc. v. Ingram, 678 S.W.2d 28, 37 (Tenn. 1984) (rule of reason allows enforcement of non-competes that “are reasonably necessary to protect employer’s interest” “unless the circumstances indicate bad faith on the part of the employer”); RESTATEMENT (SECOND) OF CONTRACTS § 184 (1981) (reformation permitted “if the party who seeks to enforce the term obtained it in good faith and in accordance with reasonable standards of fair dealing”).

<sup>220</sup> Scholars already report that courts in certain states such as Texas seem particularly hostile to the enforcement of non-competes. See Wood, *supra* note 16, at 36.

<sup>221</sup> Non-compete enforcement may not be leaky in all states. See Simon & Loten, *supra* note 25 (reporting on research conducted for the WSJ by the law firm of Beck Reed Riden showing that since 2002 non-compete cases rose 61% across the U.S. to

employers in the technology industry can encourage leakiness too by reminding the employer (especially an emotional client caught up in the heat of the moment) of the long list of pragmatic reasons for holding back from bringing a non-compete lawsuit.<sup>222</sup>

#### CONCLUSION

Do states need to ban non-competes as California has done in order to provide the optimal legal infrastructure for innovation? This Article provides an answer to that important and intriguing question by examining, for the first time, whether technology firms actually enforce non-competes. Evidence from Washington State indicates that technology firms rarely enforce non-competes. In other words, non-competes are very leaky — creative workers move freely from one technology business to another in Washington just as they do in California. The Washington case study has crucial implications for all states. It suggests that states do not need to adopt California's approach in order to foster innovation. It also shows that leaky non-competes provide better protection for trade secrets than a complete ban provides. States can offer a fertile legal infrastructure for innovation without banning non-competes by taking steps to assure that non-compete enforcement is leaky, including measures to address the potential chilling effect of non-competes. California, for its part, should embrace the so-called "trade secret exception" to its ban on non-competes to improve California's legal infrastructure for start-ups and established firms that rely on robust trade secret protection.

#### APPENDIX A

Approx. Time to Settlement		Light gray = technology industry non-compete case	Dark gray = trade secret at issue involved technology information
Tech NC Case Average (months)	Total Case Average (months)		
11.8	13.7		

760 published cases).

<sup>222</sup> See *supra* Part III.C.2.

Case Info		Noncomplete Info					Posture									
Tech Case	Case Name	Court	Filing Date	Order to Dismiss	Time to Settlement (Months, Approx.)	Subject Matter	Tech/ Software?	Type(s) of Trade Secret(s)	Departing Employee?	Departer's Profession	TRIO?	Preliminary Injunction?	Permanent Injunction?	Settled?	Trial?	Other
	Guidance Residential v. Hussain, Mohammed A	King County Superior Court	11/25/2013	N/A		Banking	No	Financial info; customer list	Yes	Regional manager		Denied		No		Continuance
X	Amazon.com Inc v. Powers	Western Dist of WA (Seattle)	10/29/2012	2/12/2013	4	Software & technology	Yes	Financial info; technology	Yes	Vice President of Sales for Web Services	Terminated	Granted in Part		Yes		Order to dismiss granted
	Allied Old English, Inc v. Uwajinaya, Inc and John Does 1-100	Western Dist of WA (Seattle)	8/28/2012	3/22/2013	7	Commercial (grocery stores)	No	Financial info (trade-marks & trade secrets)	No	N/A				Yes		
	MCD Super Fast Pizza, LLC v. Chang	Western Dist of WA (Seattle)	8/10/2012	3/6/2014	19	Commercial & IP	No	Financial info (trade-marks, trade secrets, goodwill)	Yes	Co-founder				Yes		
	International Paper Co. v. Midland Paper Co.	Western Dist of WA (Seattle)	12/21/2011	4/2/2013	16	Commercial (paper product)	No	Financial info; customer list	Yes	Vice President; Customer Service				Yes		
X	Dri-Eaz Products, Inc v. Nguyen	Western Dist of WA (Seattle)	10/4/2011	3/29/2013	18	Restoration & environmental products	Yes	Tech info; financial info	Yes	Vice President of Global Supply Management				Yes		Orders to dismiss granted

Case Info				Noncompete Info				Posture						
	Crane, Eleanora R v. Bahrer London	King County Superior Court	2/10/2011	12/7/2012	22	Fashion industry	No	Financial info (salon services)	Yes (fired)	Creative Director			Yes	Order to dismiss granted
	Obero Sausage Co. v. JBS S.A.	Western Dist. of WA (Seattle)	12/17/2010	N/A		Food industry (beef jerky)	No	Financial info (beef jerky industry know-how)	No	N/A		Granted	No	Stayed
X	Edifices Inc v. Singh	Western Dist. of WA (Seattle)	1/11/2010	10/22/2010	9	Health care software	Yes	Tech info, financial info, customer list	Yes	Vice President of Consulting Solutions		Granted	Yes	Stayed protective order, order to dismiss
	Bandy American, LLC v. Hawkeye Transportation, LLC	Western Dist. of WA (Seattle)	6/15/2009	5/26/2010	11	Commercial car rental franchise	No	Financial info (truck rental business model)	Yes	Franchisee		Granted	Yes	
	Trachline, Inc. v. Dyn	Western Dist. of WA (Tacoma)	6/5/2009	N/A		Commercial (temp agency)	No	Customer list, financial info	No	Senior executive	Granted		No	Voluntary dismissal by P
X	Compest Corporation v. Dolinsky	Western Dist. of WA (Seattle)	9/28/2007	2/26/2010	29	Technology & computer parts	Yes	Customer list	Yes	Sale manager, customer service		Granted in part	Yes	Protective order granted
	UAP Holding Corp. v. Matloza	Western Dist. of WA (Seattle)	9/15/2006	10/6/2008	25	Agricultural supplies	No	Customer list, financial info	Yes	Vice President Sales reps (non-corp)			Yes	
	Rick Gross v. Conover Insurance Inc.	Ninth Circuit	10/11/2011	N/A		Basketball team coaches	No	N/A (fired for coaching baseball)	No	Insurance agent			No	Summary judgment for D affirmed

Case Info		Noncompetitive Info					Posture							
Case No.	Case Name	Case Location	Case Date	Case Duration	Case Type	Spinal treatment center	Customer info	Tech info	Yes	Sales representative	Granted	Denied	Yes	Dismissed and/or dismissed before settlement could occur
X	DePuy Spines, Inc. v. Gill	Eastern Dist of WA (Spokane)	10/29/2013	N/A		Yes	Customer info	Yes	Yes	Sales representative			No	Dismissed and/or dismissed before settlement could occur
	USNKR v. Raptor Co. Inc.	Western Dist of WA (Tacoma)	11/14/2011	12/19/2013	25	No	Tech info	No	No	Senior Project Manager			Yes	
	C.H. Robinson Worldwide Inc. v. West Coast Carriers, LLC	Western Dist of WA (Tacoma)	6/30/2008	7/21/2009	13	No	Customer info	Yes	Yes	Sales representative	Granted	Granted	Yes	Dismissed by parties
	Merrill Lynch Pierce v. Patrick	Western Dist of WA (Seattle)	1/10/2003	2/4/2003	1	No	Customer info	Yes	Yes	Financial advisors	Granted		Yes	
	All For Kids, Inc. v. Around The World Toys Entertainment Co.	Western Dist of WA (Seattle)	6/30/2008	N/A		No	Financial info	Yes	Yes	Performers		Denied	No	Going to arbitration
X	Bardy v. Cardiac Science Corp.	Western Dist of WA (Seattle)	5/22/2013	7/11/2014	14	Yes	Tech info	Yes (terminated)		Consulting cardiologist			Yes	Mediation failed, dismissed by parties
X	Fluke Electronics Corp. v. Cordex Instruments	Western Dist of WA (Seattle)	11/29/2012	9/25/2013	10	Yes	Tech info	Yes	Yes	Sales manager, accounts manager			Yes	Dismissed by judge

Case Info	Noncompete Info	Posture						
Garlic Jim's Franchise International, Inc. v. Mo Corp. (Seattle)	Pizza franchises - IP	Financial info (trade-mark)	Yes	Franchisee	Terminated by party		Yes	Dismissed by parties
5/29/2012	8/3/2012	2	No					Protective order granted, summary judgment granted (later stricken)
Cabela Wholesale Inc. v. Hawks Prairie Investment LLC	Hunting goods stores	Financial info (ability to open a new store)	No	N/A			No	
11/29/2011	N/A		Yes	Account manager, sales representative			No	
CH2O Inc v. Bemier (Tacoma)	Agricultural chemicals and water treatment	Customer info	Yes				No	CH2O filed for bankruptcy
2/24/2011	N/A		Yes	VP of Regional Operations	Denied		Yes	Dismissed by parties
Electronic Evidence Discovery Inc. v. Chernalis (Seattle)	Discovery software	Tech info, customer info	Yes				Yes	
A G Design & Associates LLC v. Irtanman Lantern Company Inc.	Train lantern patent	Tech info	No	Potential buyer	Granted		No	Default judgment
3/30/2007	N/A		No					Protective order granted, summary judgments granted.
Veritas Operating Corp. v. Microsoft Corp. (Seattle)	Volume management technology	Tech info	No	Microsoft			Yes	
3/18/2006	4/2/2008	26	No					

Case Info		Noncompete Info					Posture				Motion			
	Mullman v. Sysco Spokane Inc	Eastern Dist of WA (Spokane)	8/15/2013	10/15/2014	14	Meat suppliers	No	Financial info (meat suppliers)	No (fired)	N/A			Yes	Motion for partial summary judgment granted
	Roadlink Workforce Solutions, LLC v. Malpass	Western Dist of WA (Tacoma)	6/11/2013	N/A		Warehouse and workforce logistics	No	Financial info	Yes	Regional manager			No	Order of voluntary dismissal granted
X	Axman v. KC Distance Learning, Inc	Western Dist of WA (Seattle)	6/21/2010	1/9/2012	18	Online education providers	Yes	Financial info (online schools business model)	Yes	Vice Presidents			Yes	Protective order granted, case dismissed
	Keystone Fruit Marketing, Inc v. Brownfield	Eastern Dist of WA (Spokane)	8/31/2005	N/A		Produce marketing	No	"Tech" info (testing customer info)	Yes	Sales manager, sales assistant		Denied	No	Writ of garnishment granted
X	Google, Inc. v. Microsoft Corp.	Northern Dist of CA (San Jose)	9/29/2005	12/27/2005	3	Computer science	Yes	Tech info; financial info	Yes	Vice President for Research and Development			Yes	Motion to stay granted