Cahill

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New York's Proposed Non-Compete Ban Remains in a Holding Pattern

On June 20, 2023, the New York State Assembly passed bill A1278B (previously passed by the New York State Senate as bill S3100A), which would establish a ban on non-compete agreements between employers and all employees, from entry-level employees all the way to C-Suite executives. While Governor Kathy Hochul still has not indicated what action she intends to take regarding this bill (which would become known as New York Labor Law Section 191-d), in remarks to the press, the governor recently signaled her desire to see the law modified to focus on protecting low and middle-income workers,[1] i.e., by potentially limiting the ban to individuals earning less than $250,000/year.[2] Numerous states have enacted legislation in recent years prohibiting employers from entering into non-competes with employees being paid below a specified annual salary or hourly wage (or precluding non-competes with hourly workers entirely), and this appears to be the governor's preferred approach.[3]

Current Status of the Bill

While the governor has not given a timeline for taking action on this bill specifically, she has indicated her intention to address most outstanding legislation before the end of the year, although this bill may not be addressed until early 2024.[4] Should the bill be delivered to the governor in its current form while the legislature is out of session for the remainder of 2023, the governor would have 30 days to sign or veto the bill, or take no action and "pocket veto" the bill. As an alternative to a veto, the governor could also work with the legislature and propose changes to the bill in a practice known in New York as "chapter amendments," which would then need to be agreed to by the legislature. The use of chapter amendments, as opposed to an outright veto of the bill, may be the more likely outcome, as the governor has signaled her openness to the non-compete legislation subject to certain revisions.

Description of the Current Bill

Total Ban on Non-Compete Agreements

Under Section 191-d(2) under the current bill, "no employer or its agent, or the officer or agent of any corporation, partnership, limited liability company, or other entity, shall seek, require, demand or accept a non-compete agreement from any covered individual."

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[1] Lauren Weber and Jimmy Vielkind, *New York Considers Ban on Noncompete Pacts*, WALL ST. J., Dec. 7, 2023.

[2] While a threshold of $250,000 has been floated by the governor, it is not yet clear what types of payments (*e.g.,* salary, bonus, commission) would be taken into consideration when determining an individual's compensation for purposes of the bill.

[3] See *infra* note 7.

[4] Weber, *supra* note 1.

Key Definitions

The key definitions provided in the bill (Section 191-d(1)) are as follows:

- "non-compete agreement" is defined as any agreement, or clause contained in any agreement, between an employer and a covered individual that prohibits or restricts such covered individual from obtaining employment, after the conclusion of employment with the employer included as a party to the agreement; and
- "covered individual" is defined as any other person who, whether or not employed under a contract of employment, performs work or services for another person on such terms and conditions that they are, in relation to that other person, in a position of economic dependence on, and under an obligation to perform duties for, that other person.

Exceptions for Restrictive Covenants other than Non-Competes

Section 191-d(5) provides carve-outs for agreements with covered individuals that: (i) establish a fixed term of service, (ii) prohibit disclosure of trade secrets or confidential and proprietary client information or (iii) prohibit solicitation of clients of the employer that the covered individual learned about during employment, with the rather ambiguous proviso for all of the aforementioned exceptions *that such agreement does not otherwise restrict competition in violation of Section 191-d*. The carve-out for client non-solicit clauses permits employers to apply such restriction to clients the employee learned about during the period of employment, without requiring that the employee had any involvement with such client. Notably, however, the bill is silent as to covenants not to solicit a former employer's employees.

No Sale-of-Business Exception

Section 191-d does not reference non-competes entered into in the sale-of-business context. Given that the aim of the bill is to encourage employee mobility, however, such transactions might not be impacted. In particular, a sale transaction involving parties with no existing employment relationship may fall outside the scope of the bill, as such a seller might not fall within the definition of "covered individual." The lack of an explicit exception does, however, create uncertainty as to the enforceability of non-competes entered into in such sale transactions generally, as well as non-competes entered into with a seller who, in connection with such sale, accepts employment with the buyer. The lack of an explicit sale-of-business exception may be another aspect of the bill that could be addressed through the chapter amendments process. A lack of such exception would make New York's non-compete ban potentially even more restrictive than the non-compete ban in California, which has long prohibited employee non-competes but does provide for an explicit sale-of-business exception.[5]

Private Right of Action

In addition to providing a blanket prohibition on employee non-competes, a notable aspect of this bill is the private right of action established under Section 191-(d)(4). Under this section, a covered individual may bring a civil action against an employer or persons alleged to have violated Section 191-(d), provided that such action is brought within two years of the later of when (i) the prohibited non-compete agreement was signed, (ii) the covered individual learns of the prohibited non-compete agreement, (iii) the employment or contractual relationship is terminated or (iv) the employer takes any step to enforce the non-compete agreement. This section further provides that a court shall

[5] See CAL. BUS. & PROF. CODE, § 16,601.

have jurisdiction to void any such non-compete agreement and to order all appropriate relief, including enjoining the conduct of any person or employer, ordering payment of liquidated damages (capped at $10,000) and awarding lost compensation, damages, reasonable attorneys' fees, and costs. With respect to the awarding of liquidated damages, Section 191-d(4)(b) provides that "the court *shall* award liquidated damages to every covered individual affected under this section, in addition to any other remedies permitted by this section."

Effective Date

While the effective date language of the bill would be expected to be straightforward, that provision itself creates ambiguity regarding the applicability of the ban to existing non-competes. The bill states that, once effective (which would be 30 days after signing), it shall apply to contracts entered into *or modified* on or after the effective date. However, it is not clear from the bill what kind of modification to an existing contract would result in a non-compete no longer being enforceable (e.g., would the modification need to be material?), or if any amendment or change to such a contract would void the non-compete.[6] This lack of clarity could lead employees to assert (in the common situation in which a non-compete is included within an individual's employment contract, rather than as a standalone agreement) that changes to provisions entirely unrelated to the non-compete, such as an amendment reflecting a change in salary or title, or merely extending the term of the agreement, would constitute a modification within the meaning of the bill and therefore void the non-compete going forward.

Broader Non-Compete Landscape

As noted above, several states have enacted legislation in recent years to limit the use of employee non-competes with lower wage workers, with laws in Colorado, Illinois, Maine, Maryland, Massachusetts, Nevada, New Hampshire, Oregon, Rhode Island, Virginia and Washington establishing salary or hourly wage thresholds (or prohibiting non-competes with hourly workers).[7] By contrast, only California, North Dakota, Oklahoma and Minnesota (which enacted a non-compete ban this year) have complete bans on the use of such restrictive covenants with employees.[8]

New York's proposed non-compete legislation also follows the federal government's efforts through agency actions to restrict the ability of employers to enter into non-compete agreements with employees. As discussed in Cahill's Firm Memorandum, dated June 22, 2023, the General Counsel of the National Labor Relations Board recently issued a memorandum articulating the position that, except in limited circumstances, non-compete agreements entered into with non-management employees violate the National Labor Relations Act. Moreover, the Federal Trade Commission's Proposed Non-Compete Rule, if enacted, would establish a national ban on employee non-competes, which would not distinguish between rank-and-file employees and members of senior management (but would include a carve-out for a sale of a business).

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[6] The sponsor of the bill, Senator Sean Ryan, has stated that should Governor Hochul reopen negotiations on the bill, he may consider proposing language to nullify existing non-competes. See Weber, *supra* note 1.

[7] See COLO. REV. STAT. ANN. § 8-2-113(2)(a)–(b) (2022); 820 ILL. COMP. STAT. 90/10(a) (2017); ME. REV. STAT. ANN. tit. 26, § 599-A (3) (2019); MD. CODE ANN., LAB.& EMPL. § 3-716(a)(1)(i) (2019); MASS. GEN. LAWS ANN. Ch. 149, § 24L(c) (2021); NEV. REV. STAT. § 613.195(3) (2021); N.H. REV. STAT. ANN. § 275:70-a(II) (2019); OR. REV. STAT. § 653.295(1)(e) (2022); R.I. GEN LAWS § 28-59-3(a)(1) (2020); VA. CODE ANN. § 40.1-28.7:8(B) (2020); WASH. REV. CODE ANN. §§ 49.62.020(1)(b), 49.62.030(1) (2020).

[8] See CAL. BUS. & PROF. CODE, § 16,600; N.D.C.C. § 9-08-06; OKLA. STAT. ANN, ART. XV § 218; MINN. STAT. § 181.988.

Looking Ahead

With Governor Hochul now having publicly commented on the need for revisions to the bill, along with the push-back the bill has received from business groups and other interested parties, it appears unlikely that the current version of the bill will be signed into law without changes. Should New York's non-compete legislation come into effect, it will continue a national trend toward limiting or outright prohibiting employee non-competes and, while the actions at the federal level may be slow-moving, such a law in New York may serve as a catalyst for other states to examine passing similar legislation.

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If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to call or email authors Geoffrey E. Liebmann (partner) at 212.701.3313 or gliebmann@cahill.com; Joel Kurtzberg (partner) at 212.701.3120 or jkurtzberg@cahill.com; Mark Gelman (counsel) at 212.701.3061 or mgelman@cahill.com; Lauren Perlgut (counsel) at 212.701.3558 or lperlgut@cahill.com; or Eric Scher (senior attorney) at 212.701.3984 or escher@cahill.com; or email publicationscommittee@cahill.com.