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## *Essays*

# Would a Successful FTC Noncompete Ban Reduce Lawsuits Against Employees Who Change Jobs?

CHARLES TAIT GRAVES<sup>†</sup>

If the Federal Trade Commission (FTC) succeeds in prohibiting employee noncompetition covenants under its rule announced in April 2024<sup>1</sup>—something this Author strongly supports—will that cause a major increase in employer lawsuits against departing employees for trade secret misappropriation? Said differently, would we merely be replacing one category of lawsuits against employees with another?

Although some commentators have suggested so,<sup>2</sup> the correct answer is “mostly no.” While there would likely be a net increase in trade secret lawsuits if the noncompete ban makes it through the courts, trade secret claims are not a 1:1 substitute for lawsuits over noncompetition covenants. As a result, the overall number of lawsuits filed against departing employees will almost certainly decrease if the FTC wins out—a salutary outcome. This Essay explains why.

The answer turns on the distinction between suing a departing employee for competing and suing an employee for violating the intellectual property laws. Those are two different things, with different requirements. The latter is substantially more difficult than the former.

A noncompetition covenant permits an employer to sue an employee who leaves their job with the employer to join a competitor for better pay, a promotion, or better opportunities, or to escape an unsatisfactory workplace

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1. *See* Non-Compete Clause Rule, 89 Fed. Reg. 38342 (proposed Jan. 19, 2023) (to be codified at 16 C.F.R. pt. 910).

2. Peter Coy, *The Mostly Persuasive Logic Behind the New Ban on Noncompetes*, N.Y. TIMES (Apr. 26, 2024), <https://www.nytimes.com/2024/04/26/opinion/ftc-noncompetes-ban.html> (“‘You can’t work for a competitor for a year’ is a pretty clear rule; ‘you can’t use our secrets at a competitor’ will mean more lawsuits.”) (quoting Matt Levine, *The FTC Comes for Noncompetes*, BLOOMBERG (Apr. 24, 2024, 11:35 AM PDT), <https://www.bloomberg.com/opinion/articles/2024-04-24/the-ftc-comes-for-noncompetes>).

environment, and allows the employer ask a judge to stop the employee from taking the new job. The employer often can make that request without evidence of the employee's wrongdoing, usually without having to prove that it owns valid intellectual property, and with no downside risk of having to pay the employee's attorneys' fees if it loses. Simply threatening such a lawsuit in a letter drafted by a law firm can scare off a potential new employer of an employee who wishes to leave the firm.

For the many attorneys and law firms around the country who represent employers in such cases, this is almost too good to be true. They can easily satisfy angry clients who want to attack departing employees. They need not understand the science or technology an employee may specialize in in order to file a lawsuit. They can argue in court that competition by an employee, in and of itself, is wrongful. They can posture that "trade secrets" need to be protected without having to prove that valid trade secrets exist or have been misused, and they can portray a departing employee as a bad actor without evidence of misconduct.

It's important to recognize the sociological dimension to such lawsuits, because none of this happens in a vacuum. Companies are Janus-faced: They are happy when they are able to hire from competitors, but executives can become angry, even enraged, when employees depart for a competitor. In turn, companies represent repeat business opportunities for lawyers. Individual employees do not. Because lawyers find that their status positioning within their law firm often depends on driving revenues, repeat business is more valuable than one-off matters. Thus, law firms generally work for employers, and that means they draft employment agreements and file lawsuits on their behalf. To be sure, this can also mean defending an employer-client who has hired an employee from another company. But the financial incentive to please companies who are angry when they lose talented employees to competitors results in an overall posture among those law firms that competition by former employees is intolerable. The prospect of a continuing revenue stream that litigating noncompetition agreements against departing employees offers is attractive. The upshot is that even if banning noncompetes benefits the broader American economy through greater competition and resulting innovation, many lawyers have a financial self-interest, and a personal fear of losing status positioning within law firms should their practice areas decline, that results in disproportionate opposition to such a ban. Small wonder that some prominent law firms have published client alerts where the tone is oppositional to, if not outright bemoaning, the FTC's rulemaking.<sup>3</sup>

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3. See, e.g., Jennifer S. Baldocchi, Carson H. Sullivan, Patrick W. Shea, Jessica E. Mendelson, Sarah Guinee & Michael S. Wise, *FTC Announces Expansive and Unprecedented Non-compete Ban*, PAUL HASTINGS (Apr. 24, 2024), <https://www.paulhastings.com/insights/client-alerts/ftc-announces-expansive-and-unprecedented-non-compete-ban> (describing the FTC rule as "unprecedented"); *New FTC Rule Banning Virtually All Non-compete Agreements Sends Shockwaves Through Every Sector of U.S. Business*, REED SMITH

If employers and law firms could simply substitute a trade secret lawsuit against a departing employee for a noncompetition covenant lawsuit with ease, we might not see a lawsuit from the Chamber of Commerce<sup>4</sup> or such negative commentary from law firms. But a trade secret lawsuit is not a synonym to a noncompete. A trade secret lawsuit is something quite different and poses real risk to employers who sue their departing employees out of anticompetitive motives alone.

To start, a trade secret plaintiff must—obviously—establish that valid trade secrets exist and that a departing employee has misappropriated them. That can be hard to do, as so much information about customers, as well as scientific information, exists readily on the internet, in academic publications, conference proceedings, and other standard public domain sources.<sup>5</sup> Moreover, in order to separate the wheat from the chaff, courts increasingly require a trade secret plaintiff to identify its alleged trade secrets early, and not engage in obfuscatory generalizing.<sup>6</sup> For this reason, courts also refuse to enter broadly-worded injunctions that vaguely prohibit misuse of trade secrets, without specific details

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(Apr. 25, 2024), <https://www.reedsmith.com/en/perspectives/2024/04/new-ftc-rule-banning-virtually-all-non-compete-agreements-sends> (noting as well that the FTC rule is “unprecedented”); *FTC Issues Final Rule Banning Most Non-Compete Agreements*, CROWELL (Apr. 24, 2024), <https://www.crowell.com/en/insights/client-alerts/ftc-issues-final-rule-banning-most-non-compete-agreements> (“[T]he FTC’s nationwide expansion of the ban on non-compete agreements nevertheless raises significant concerns around IP theft . . . [C]ompanies seeking the return of misappropriated trade secrets through litigation should consider whether they can fill the gap left by the FTC’s ban on non-compete agreements through the ‘inevitable disclosure’ doctrine.”); Chuck Boyars, Dawn H. Dawson, Ian G. John, Andrea Agathoklis Murino, Joshua L. Simmons, Dennis Williams, Brittany Lischinsky Burke, Michael Falk, R.D. Kohut, Risa M. Salins & Michael B. Slade, *FTC Issues Final Rule Banning Non-Compete Agreements; Significant Enforceability Challenges Likely*, KIRKLAND & ELLIS (Apr. 24, 2024), <https://www.kirkland.com/publications/kirkland-alert/2024/04/ftc-issues-final-rule-banning-noncompete-agreements> (“[C]onsider structuring employment terms with the following concepts[:]. . . fixed-term employment agreements with non-competes during the employment term, as well as notice or garden leave periods.”); *FAQs About the FTC Final Rule Banning Worker Noncompete Agreements*, JONES DAY (2024), <https://www.jonesday.com/en/insights/2024/04/faqs-about-the-ftc-final-rule-banning-worker-noncompete-agreements> (discussing how one might challenge the FTC’s rule).

4. *See Chamber of Commerce to Sue FTC Over Unlawful Power Grab on Noncompete Agreements Ban*, U.S. CHAMBER OF COM. (Apr. 23, 2024), <https://www.uschamber.com/finance/antitrust/u-s-chamber-to-sue-ftc-over-unlawful-power-grab-on-noncompete-agreements-ban>.

5. *See, e.g.,* Calendar Research LLC v. StubHub, Inc., No. 2:17-cv-04062-SVW-SS, 2020 U.S. Dist. LEXIS 11231, at \*22 (C.D. Cal. May 13, 2020) (finding no trade secret where former employer tried to claim rights in publicly available information and recognizing that employees may carry general skills of the trade from job to job).

6. *See* JJ Plank Co., v. Bowman, No. 3:18-CV-00798, 2018 U.S. Dist. LEXIS 123792, at \*7–8 (W.D. La. July 23, 2018) (collecting cases requiring early identification of alleged trade secrets); *see also* Coda Dev. S.R.O. v. Goodyear Tire & Rubber Co., No. 5:15-cv-1572, 2019 U.S. Dist. LEXIS 202114, at \*11 (N.D. Ohio Nov. 21, 2019) (“[G]iven the nature of and burdens imposed by trade secret cases, many courts across the country recognize the ‘growing consensus’ in favor of ‘requiring those plaintiffs bringing claims of trade secret misappropriation to identify, with reasonable particularity, the alleged trade secrets at issue.’”); Sedona Conference, *Commentary on the Proper Identification of Asserted Trade Secrets in Misappropriation Cases*, 22 SEDONA CONF. J. 223, 247–62 (2021) (collecting nationwide cases).

that separate what is secret from what is public and lawfully usable by a defendant.<sup>7</sup>

All of this is a far cry from a noncompetition lawsuit, where little of the sort need be established. While courts in noncompete cases sometimes refer to protection of trade secrets, they generally do not require that the employer to do the work to establish the existence of valid trade secrets, much less identify each of them with specificity, much less demonstrate a misappropriation by the departing employee. Generic rhetoric is too often sufficient.<sup>8</sup>

For example, in 2022, the Arkansas Court of Appeals affirmed a noncompete ruling against a former employee because the employer was able to cite the existence of such things as its “title plant and pricing plans” and customer information as an interest to justify the restriction.<sup>9</sup> But the employer did not have to prove that any of this was actually a trade secret—the court simply noted that the employee signed a confidentiality agreement.<sup>10</sup> And in a 2023 Ohio case, the former employer failed to establish that it had valid trade secrets, but was nonetheless still permitted to enforce a noncompetition covenant to prevent customer solicitation – the former employee had “violated that prohibition early and often.”<sup>11</sup> As the United States District Court for the Southern District of Ohio explained, the state’s restrictive covenant law protects customer relationships, even where “information-based claims fall short.”<sup>12</sup>

Many noncompete cases do not even address intellectual property and are naked efforts to stop competition. In a 2015 Florida case decided under Tennessee law, a physician had entered into a joint venture with the plaintiff to operate an ambulatory surgery facility, and then left and competed.<sup>13</sup> The

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7. See *Mallet and Co. v. Lacayo*, 16 F.4th 364, 387 (3rd Cir. 2021) (reversing preliminary injunction where plaintiff pointed only to general concepts and categories instead of defining its alleged trade secrets); *Capstone Logistics Holdings, Inc. v. Navarrete*, 838 Fed. App’x 588, 590 (2d. Cir. 2020) (same where the text of the injunction did not identify the alleged trade secrets); *uSens, Inc. v. Shi Chi*, 2018 U.S. Dist. LEXIS 175570, at \*6 (N.D. Cal. Oct. 11, 2018) (denying request for preliminary injunction; “First, Plaintiff has not adequately identified the information it alleges are trade secrets.”).

8. I have previously detailed the way in which courts enforcing noncompetition covenants use the rhetoric of protecting intellectual property without actually requiring that such property be established. See Charles T. Graves, *Analyzing the Non-Competition Covenant as a Category of Intellectual Property Regulation*, 3 HASTINGS SCI. & TECH. L.J. 69–70 (2011).

9. *Combs v. Elite Title Co.*, 646 S.W.3d 230, 234–36 (Ark. Ct. App. 2022) (affirming issuance of preliminary injunction).

10. See *id.*

11. See *Total Quality Logistics, LLC v. EDA Logistics, LLC*, 2023 U.S. Dist. LEXIS 132862, at \*14–15 (S.D. Ohio July 31, 2023) (issuing injunction following bench trial).

12. See *id.* at \*29–30 (“In sum, the Court concludes that [plaintiff] possesses trade secret information, but that it has failed to show that [employee] left [plaintiff] with, or is currently using, any actionable trade secret information. Thus, the trade secret claim fails.”). It should be noted the different states construe noncompetition clauses differently, and some will reject enforcement in the absence of protectable information. See, e.g., *Henderson v. Patel*, 82 N.Y.S.3d 800, 805 (N.Y. Civ. Ct. 2018) (denying enforcement of noncompete under New York law where, among other things, “defendant demonstrated as a matter of law that the list of ‘potential clients’ is not a trade secret rendering the noncompete clause further unenforceable.”).

13. See *Amsurg New Port Richey FL, Inc. v. Vangara*, 159 So. 3d 260, 261–62 (Fla. Dist. Ct. App. 2015).

plaintiff did not discuss protectable information at all. The District Court of Appeal enjoined the physician, even when taking note of the American Medical Association's opposition to noncompetes, on the thesis that the restrictive covenant did not stop him from practicing medicine, and instead only barred him from competing with the plaintiff.<sup>14</sup>

Cases like these demonstrate that litigating a trade secret claim poses materially higher hurdles for a former employer than does suing over a noncompetition covenant, where standards are comparatively lax.

But there is an even bigger stumbling block to substituting a trade secret claim for a claim of breach of a restrictive covenant: A plaintiff that files a baseless trade secret case against a departing employee may have to pay the defendant's attorneys' fees if the sole motive for the lawsuit was to stop competition. Under federal trade secret law and in most states, a trade secret plaintiff that files or maintains a lawsuit in "bad faith" must pay such fees.<sup>15</sup>

In many cases, this means that precisely what is legitimate in a noncompetition covenant lawsuit—the employer's overt desire to prevent competition—is illegitimate under trade secret law. We can see this most clearly in California "bad faith" cases. California is a jurisdiction where noncompetition agreements have long been illegal, and thus one where the pressure on employer-side lawyers to accommodate client demands to file baseless trade secret claims is highest. In one 2009 case, the appellate court found that a former employer had filed a trade secret lawsuit in "bad faith" in part because the company's CEO had openly expressed an anticompetitive motive. "When asked why the action was filed, [plaintiff] CEO Earl Lewis testified that 'we can't tolerate a direct competitive threat by [the two former employee-defendants].' Lewis had no evidence of wrongdoing but was bothered that respondents planned to compete with [plaintiff] in the future."<sup>16</sup>

Similarly, a California appellate court in 2015 found "bad faith" where there was "an inference that the purpose of the lawsuit was to impose a financial penalty upon, and thereby deter, [defendant's] attempts to hire [plaintiff's] technical employees. Indeed, it might be inferred that the purpose of the lawsuit was to inhibit not only [the defendant] but other competitors as well from attempting to engage in the same, entirely lawful conduct."<sup>17</sup> Here again, the court used the CEO's own words to support the ruling: The executive had issued

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14. *See id.* at 263.

15. 18 U.S.C. § 1836(b)(3)(D) ("[A] court may[.] . . . if a claim of the misappropriation is made in bad faith, . . . award reasonable attorney's fees to the prevailing party."); *see also* Unif. Trade Secrets Act § 4 (amended 1985) (Unif. L. Comm'n 1985) (describing the same concept).

16. *FLIR Sys., Inc. v. Parrish*, 174 Cal. App. 4th 1270, 1276 (2009) (awarding over \$1.6 million in attorneys' fees and costs to defendants for trade secret case brought in bad faith).

17. *Cypress Semiconductor v. Maxim Integrated Prods.*, 186 Cal. Rptr. 3d 486, 508, 236 Cal. App. 4th 243, 269 (Cal. Ct. App. 2015).

a press release where he stated “[w]e will not tolerate unfair attempts to lure our employees away in order to gain access to our trade secrets.”<sup>18</sup>

And, again, in a 2012 case the court found “bad faith” where the CEO, again, offered dubious testimony that the departing employees bore the burden of proving that they did not take anything from the company.<sup>19</sup> The court noted that “[i]t was perfectly legitimate for [the new employer] to hire the individual defendants and for the individual defendants to leave the employ of [the plaintiff] in favor of a competitor, [defendant].”<sup>20</sup>

In each of these cases, these candid expressions of a top executive’s desire to stop employees from competing would be perfectly normal, and acceptable, in jurisdictions where noncompetition covenants are legal. Few would bat an eye, because raw aggression against departing employees is commonplace under the law of restrictive covenants. But under trade secret law, by contrast, such expressions of anticompetitive objectives can lead to sanctions where the employer must pay the departing employee’s legal fees.

For these reasons, we should not expect that the same number of lawsuits will be filed against departing employees—with only different labels on the causes of action—if the FTC succeeds in banning noncompetition covenants. There will almost certainly be a meaningful net decrease in lawsuits that employers file against departing employees. This is so because absent evidence of intellectual property-based wrongdoing, it will be more difficult for employer-side attorneys to draft a complaint, much less identify valid trade secrets and accusations of misappropriation. And the risk of punishment—through a finding of “bad faith” is real—where the objective of stymieing competition operates as evidence against the employer under trade secret law.

That’s not to say that we won’t see more trade secret lawsuits—just an overall net decrease in lawsuits against employees. To be sure, some employers will proceed with baseless trade secret lawsuits, wagering that fees recovery would require too much effort by an over-lawyered individual employee. Others will seek to revise the theory of “inevitable disclosure”—where a former employer tries to get the same result as a noncompetition covenant by arguing that the employee will ineluctably misuse trade secrets in the future. But that concept is in decline, in particular because the federal Defend Trade Secrets Act (DTSA) frowns on it.<sup>21</sup> Still others will seek to rewrite contractual confidentiality clauses so broadly that they could capture the exercise of general

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18. *Id.*

19. *See* SASCO v. Rosendin Elec., Inc., 207 Cal. App 4th 837, 843, 849 (Cal. Ct. App. 2012).

20. *Id.* at 848.

21. *See* 18 U.S.C. § 1836(b)(3)(A)(i)(I) (allowing injunctions for actual or threatened misappropriation if the order does not prohibit a person from entering into an employment relationship and the conditions placed on employment are based on evidence of threatened misappropriation, not merely on information the person knows). For a study of one hundred years of case law under this theory, see Charles Tait Graves, *Is There an Empirical Basis for Predictions of Inevitable Disclosure?*, 18 WAKE FOREST J. BUS. & INTELL. PROP. 193, 203–07 (2018).

employee skills and knowledge rather than only valid trade secrets.<sup>22</sup> Where executives pressure their attorneys to take action, and where attorneys fear an intrafirm status position decline if their area of practice is banned by the FTC, we will doubtless see many creative attempts to find new ways to sue people who change jobs.

Still, in the end, a trade secret lawsuit is something entirely different from a noncompetition covenant lawsuit. Should the FTC's April 2024 proposed ban become law—a result we should all support—the number of lawsuits filed against employees who choose to quit and join another company, or to form a new company, will almost certainly decrease.

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22. See generally Camilla A. Hrdy & Christopher B. Seaman, *Confidentiality Agreements that Act Like Noncompetes*, 133 YALE L.J. 669 (2024) (explaining the danger of overbroad confidentiality clauses). A California court rejected such practices, but it remains to be seen how courts elsewhere will react. See *Brown v. TGS Mgmt. Co.*, 271 Cal. Rptr. 3d 303, 315–19, 57 Cal. App. 5th 303, 316–17 (2020) (affirming that a “strikingly broad” confidentiality clause in employment agreement was overbroad and thus “operate[d] as a de facto noncompete provision”). To be sure, trade secret law permits employees to carry their general skills, knowledge, training, and experience from job to job. See *Retirement Grp. v. Galante*, 176 Cal. App. 4th 1226, 1237 (2009) (“a former employee may use general knowledge, skill, and experience acquired in his or her former employment . . .”); see also Camilla A. Hrdy, *The General Knowledge, Skill, and Experience Paradox*, 60 B.C. L. REV. 2409, 2419–20 (2019) (explaining this concept comprehensively).



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