Massachusetts Non-Compete Legislation – A Walk Through the 'Garden' … Leave Provision

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December 27, 2017

With the approaching New Year bringing the possible passage of non-compete legislation in Massachusetts, we examine here the "Garden Leave" provision included in several proposed bills. The proposed "Garden Leave Bills" attempt to limit the frequency of enforcement of non-compete agreements and require compensation to employees for any financial hardship caused in the event their former employers pursue enforcement of the agreements.

Over the past eight years, the Massachusetts Legislature has made numerous attempts to enact laws regulating the use of employee restrictive covenants. (See our article, Down to the Wire for Proposed Non-Compete Reform Legislation in Massachusetts, for examples.) After falling just short of passing such legislation in 2016, the current legislative session introduced eight bills on the subject, including six that are focused specifically on non-compete agreements. While each bill has its own unique features, together, they share a common purpose of strengthening protections for the individuals who would be restrained in the ability to compete with their former employers.

In three of the six proposed non-compete bills, including House Bill 2371 (HB 2371), Senate Bill 840 (SB 840), and Senate Bill 1017 (SB 1017) (collectively, the "Garden Leave Bills"), a "garden leave" requirement is imposed on employers who would seek to prevent former employees from immediately jumping to a competitor. This provision requires an employer to continue paying a former employee while the former employee is restricted from engaging in competitive activity. Presumably, the primary purposes of these provisions are: (1) to support employee mobility by reducing the instances when employers seek enforcement of non-compete covenants; and (2) to reduce or eliminate any financial harm that a non-compete covenant might pose to the affected former employee.

Below, we examine how the "garden leave" requirement would be implemented under the Garden Leave Bills and consider the likely practical difficulties of implementing the proposed schemes.

A Brief History of "Garden Leave"

"Garden leave" typically is viewed as an English concept: following a separation from employment, the employee does not immediately commence a new job. Instead, the employee continues to be paid his or her salary for a period of time, while staying home and (figuratively or literally) tending to his or her garden. Certain U.S. employers have used a similar concept, by requiring some period of notice prior to resignation or termination. During this period, the employee continues to be paid but is not required to come to work or provide services (beyond, perhaps transition assistance). A primary function of garden leave payments is to neutralize any allegations of financial damage to a former employee caused by a non-compete covenant.

No Legislative Precedent

By mandating the attachment of garden leave to post-employment non-compete covenants, the Massachusetts Garden Leave Bills attempt to legislate what historically has been only a function of contract in the United States. That point was made to a member of the Legislature's Joint Committee on Labor and Workforce Development on October 31, 2017, during a hearing on the proposed bills. While the questioner might have assumed the Legislature would be reluctant to wade into uncharted waters, the committee members appeared untroubled by the prospect, remarking that this would not be the first time the Commonwealth has distinguished itself from the rest of the country.

This willingness to pursue first-of-its-kind legislation is undoubtedly helped by the fact that, for now, the Associated Industries of Massachusetts, a powerful industry association that represents large companies operating in the state, has thrown its support behind one of the Garden Leave Bills: HB 2371.

The Proposed Garden Leave Bills

Under SB 840 and SB 1017, an employer who chooses to enforce a post-employment non-compete

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covenant must continue paying the former employee at least 100 percent of the employee's earnings for the duration of the restricted period (excluding any extended periods that might result from employee violations). The employee's earnings would be measured according to the employee's highest annualized earnings for the two years immediately preceding separation of employment.

HB 2371 would require payments of at least 50 percent of earnings (using the same earnings calculation as in SB 840 and SB 1017).

All three Garden Leave Bills require the garden leave provision, including the specific terms mandated by the legislation, to be set forth in the applicable non-compete covenant.

Enforcement Trigger

Under all three Garden Leave Bills, the former employer may activate unilaterally the post-separation non-compete covenant without first seeking judicial endorsement.

SB 840 and SB 1017 require an employer to provide its departing employee written notice of the intent to enforce the non-compete covenant within 10 days after termination of the employment relationship. The employer then must commence garden leave payments no later than 30 days after termination of the employment relationship in order to effectuate the non-compete covenant's post-separation restrictions.

Although HB 2371 also requires garden leave payments as a condition for enforcement of a non-compete covenant, it does not require written notice of the intent to enforce such a covenant or set a deadline for garden leave payments to commence.

Significantly, while the proper commencement of garden leave payments gives an employer the right to seek judicial enforcement of a non-compete covenant in response to an alleged breach, it does not create any special presumption of enforceability of the actual non-compete covenant. This means a court may refuse to enforce a non-compete covenant on other grounds (*e.g.,* because it is broader than necessary to protect a legitimate business interest of the employer), regardless of the employer's diligent compliance with the garden leave provision.

Moreover, under the Garden Leave Bills, employers cannot recoup garden leave payments that have been made in furtherance of an otherwise invalid non-compete covenant. Nor do the bills allow an employer to stop garden leave payments once such payments have commenced, even if a court denies a request to enforce the non-compete provision.

Employer Ability to Opt Out

By requiring employers to *activate* a departing employee's post-separation non-compete covenant by giving written notice of intent and/or commencing garden leave payments, the Garden Leave Bills also enable the employer to forego making garden leave payments if it does not intend to enforce the covenant. The employer can do this by simply failing to give written notice of enforcement and/or failing to commence garden leave payments.

Importantly, none of the Garden Leave Bills requires the departing employee to communicate his or her plans or opportunities for future employment to the employer. Further, once an employer has opted out of paying garden leave to enforce a non-compete covenant, the Garden Leave Bills provide the employer no method to reverse its decision if the former employee's competitive activities significantly deviate from the employer's initial expectations.

Employer Ability to Discontinue Payments

Under each of the Garden Leave Bills, an employer that satisfies its initial notice and/or payment obligations under the applicable garden leave provision may not discontinue the garden leave payments unilaterally *except* where the employee has breached the non-compete covenant. The Bills do not state specifically whether such breach needs to be established in court.

The Bills also fail to state the consequences of garden leave payments following a determination of breach. For instance, it is unclear whether the former employee would remain subject to the non-compete covenant after the payments have been discontinued due to a breach. If a former employer successfully obtains an injunction after discontinuing garden leave payments, would it be required to reinstate payments for the remainder of the garden leave period? On the other hand, if a court determines that no breach occurred, would the initial discontinuation of payments render the non-compete covenant unenforceable, or would the employer be permitted to resuscitate the non-compete covenant by reinstating the garden leave payments? The current versions of the Garden Leave Bills do not address these questions.

Practical Challenges with Garden Leave Legislation

From a practical perspective, logistical issues with the implementation of the Garden Leave Bills may thwart the intent of the proposed legislation.

Employee Challenges

Including a garden leave provision in the legislation may not lead to greater employee mobility than the

status quo.

Currently, employees subject to non-competition agreements often disclose their contracts to prospective employers. Such employers must decide whether to go forward with the proposed employment without knowing how aggressively the former employer will pursue the non-compete. These communications usually take place while the employee is still employed by the former employer. Some prospective employers will refuse to go forward, not wanting to deal with potential litigation or invest in an employee who may be enjoined. Other employers will agree to go forward only if the employee convinces the prior employer to provide a written waiver of the non-compete. Still others may be willing to go forward, but with a "wait and see" approach, depending on how the former employer responds.

The Garden Leave Bills likely would not affect these analyses. The former employer need not indicate its enforcement intent until after the employee ends his or her employment. Therefore, the prospective employer would essentially be in the same position under a garden leave statute as it is today. Therefore, one primary goal of the proposed non-compete legislation — employee mobility — may not be adequately addressed.

In addition, it is unclear whether a former employee who is complying fully with a non-compete covenant may seek monetary damages in response to the employer's unilateral discontinuation of garden leave payments. While improper discontinuation of payments likely would impair the employer's right to continue enforcing the non-compete restrictions, most former employees would be unable immediately to exploit that opportunity after having already established a non-competitive posture. Should the Legislature push forward with the garden leave requirement, it should consider articulating the legal and judicial consequences of an employer's improper discontinuation of garden leave payments.

Employer Challenges

Ordinarily, an employer cannot make an informed decision as to whether to enforce a non-competition agreement against a specific employee without receiving details about the departing employee's future employment plans. Further, by forcing the employer to opt-in or opt-out of enforcement at the beginning of the restricted period, the Bills leave the employer with no recourse if the employee's competitive activities subsequently change materially during the restricted period. Not knowing where the employee will be working or what he or she will be doing, coupled with the specter of losing the ability to enforce the non-compete for the duration of the restricted period, may result in employers deciding to enforce in cases where, had they known of the employee's plans, they may have decided not to enforce.

Thus, the current version of the proposed garden leave provision may result in employers choosing to enforce non-competes more often than they otherwise would under the status quo, which is contrary to the rationale behind the legislation. In order to potentially address this issue, the Massachusetts Legislature might consider imposing requirements on both parties — not just employers — to engage in interactive dialogue at the start of the restricted time period to facilitate a reasoned, prudent judgment as to whether circumstances warrant enforcement.

Notwithstanding the above dilemma, the employer's difficulties do not end once it chooses whether to enforce the non-compete agreement. The proper payment of garden leave does not give the employer any additional assurance that the applicable non-compete covenant ultimately will be upheld in a court of law. A court can invalidate the covenant for other reasons and the employer would have no recourse to recoup the payments it had been making in furtherance of a losing cause. This problem could be corrected partially by attaching a presumption of validity to a non-compete covenant once the former employee has accepted garden leave payments without objection.

With respect to the lack of statutory guidance on the consequences of an employer's unilateral discontinuation of garden leave payments following an alleged employee breach, the Garden Leave Bills do not explain the consequences where a court disagrees with the employer's determination of a breach, even as they allow employers to discontinue payments in the event of a breach. If an employer discontinues garden leave based on a perceived breach, but the court subsequently holds that the breach did not occur, would the employer's decision itself constitute a breach that, thereby, renders the non-compete covenant unenforceable? The Bills also do not identify the circumstances under which an employer might be compelled to reinstate garden leave after initially discontinuing such payments. Without the Legislature's clarification on these issues, the existing uncertainty surrounding the consequences of discontinuation of garden leave benefits would pose significant burdens on both employers and employees.

Potential for Abuse

Finally, the Bills' current versions of the garden leave requirement could give rise to the potential for abuse. For instance, a departing employee who intends to engage in competition that violates his or her non-compete covenant would be motivated to hide those plans from the former employer until after the applicable opt-out period. Similarly, the employee's new employer might be motivated to initially place the employee in a non-competitive role, again, until the expiration of the opt-out period, only to switch the employee's position once the former employer decides not to enforce. A new employer also might be motivated to exploit the employee's diminished bargaining power — created by uncertainty over the

former employer's enforcement plans — by offering employment at a discounted wage, which would also thwart another stated purpose of the legislation: addressing wage suppression.

It would be virtually impossible to fully eliminate the potential for abuse of the proposed garden leave provisions, whether by employers or employees. However, some potential abuse could be avoided by granting the former employer greater flexibility to modify its enforcement position in response to a former employee's own modification of his or her competitive posture during the post-employment restrictive period. The Legislature could encourage the parties to "show their cards" upfront and avoid much of the uncertainty that threatens to frustrate the goals of the non-compete legislation.

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While some of the Legislature's concerns may be addressed by the Bills, the garden leave provisions, in their current form, may do more harm than good. Should it choose to move forward with a garden leave mandate, the Massachusetts Legislature may want to consider addressing the logistical and other issues raised here.

This is a general summary of the Bills. Given the complexities involved in the enforcement of non-compete agreements, employers would be well-served to address specific scenarios with the assistance of counsel.