

BATTLE OF THE TITANS: WHEN TRADE SECRET PROTECTION AND THE PROHIBITION ON NON-COMPETES HIT HEAD ON IN CALIFORNIA - ONE COURT GETS IT RIGHT

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We all know that non-competes are generally *verboden* in California. If you aren't sure, read [this brilliant blog](#) entry ([and this one](#)). California is very protective of its workers' rights to move from job to job, shopping his or her talents to the highest bidder (so to speak).

We also know that California is very protective of an employer's right to protect its intellectual property, including especially its trade secrets. This includes, of course, customer lists and client

information under proper circumstances.

So what happens when these two important and closely protected public policies *crash head on into one another*?

What happens when workers want to compete with their former employer by soliciting business from the employer's customers...and the customer contact information is both stored in the employer's database and (with a little digging) available from public sources? Who wins this one?

TRADE SECRETS V. NON-COMPETES

Intellectually, the answer is easy. Just ask fellow trade secret geek [Stuart Jasper](#). The courts (if they are paying attention) will say:

a) The employee can compete, solicit, plead and beg for business all he or she wants, even from the former employer's best and most valuable customers. [B&P 16600](#) is extremely clear in its prohibition of any contracts that restrain (even a little bit according to the Supreme Court in [Edwards](#)) a person's ability to engage in a trade or profession.

b) BUT, he (or she) can't use the former employer's trade secrets to jump start that competition. Assuming the employer properly protected its customer information as a trade secret, the employee cannot download the customer data onto a pen drive and use that to initiate solicitation.

("But the pen drive is so tiny, how wrong can it be?" "Very wrong.") (And don't try to email the information to yourself, thinking no one will figure that one out. Come on, those aren't hatracks on those IT guys and gals.)

But the intellectual answer - go ahead and compete, but don't use the employer's trade secrets to do so - is a lot easier to say than to implement. Even the trial courts run into trouble with this.

THE RETIREMENT GROUP V. GALANTE

Case in point: [The Retirement Group v. Galante](#) (July 30, 2009, 4th App. Dist., Cal. Court of Appeals) Case No. D054207, ___ Cal.App.4th ___ (Yeah, I know this citation is messed up, but I flunked Blue Book. Besides, isn't that what associates are for?) (By the way, Jasper promises me he had a hand in convincing the Court to publish this decision. O.K, whatever.)

This case is a great example of the tension between the competing interests of employees and employers in California, and some of the confusion that can be created when the two collide.

In *The Retirement Group*, the employer (TRG) was in the securities/investment business. Its customers were individuals willing to invest money (a rare commodity). The employer "spent substantial resources to develop its customer base" and protected its customer data as a trade secret. The employees (actually, they were independent contractors, but let's not get picky, it doesn't make a difference) provided investment advice to TRG's customers on behalf of the employer.

You can guess what happened next. The employees (contractors) left the employer and joined a competitor. You can also guess who these workers targeted for business!

Now, if you have been paying attention, you should be saying to yourself, "Hey, it's o.k. for these employees to target, solicit, and get business from TRG's customers. That's what B&P 16600 is all about." And you would be right.

But you should also be saying, "But they better not be using TRG's trade secrets to do it." Excellent.

So that leaves the most important practical question: "*What information did the employees use in order to contact those customers?*" (If you asked that question, give yourself an hour MCLE credit.)

In *TRG*, apparently there was enough evidence that the employees used (at least in part) the former employer's trade secret information to contact the customers that the trial court was willing to issue a preliminary injunction. The injunction prohibited four categories of conduct. Let's take a look at categories 3 and 4.

Injunction Category 3 prohibited the employees from "using in any manner TRG information found solely and exclusively on TRG databases. [However,] [s]imilar information found on servers, databases and other resources owned and operated by other entities or businesses is excluded from the injunction."

This is another way of saying "Don't use TRG's trade secrets, but it's ok to use the exact same data so long as you find it somewhere else."

Injunction Category 4 prohibited the employees from "directly or indirectly *soliciting any current TRG [customers]* to transfer any securities account or relationship from TRG to [the workers] or any broker-dealer or registered investment advisor other than TRG." (Emphasis added.)

Do you see the problem with Category 4 here? It's a prohibition not on the misuse of trade secrets *but on the solicitation of business*. (Emphasis added again.)

I am sure the attorneys for TRG drafted the injunction language and presented it to the trial court as a proposed preliminary injunction. Trial courts are busy, and probably not as well versed in the nuances of trade secret and restrictive covenant law as we trade secret geeks, and so once it determined that an injunction was appropriate, it probably just signed the proposal submitted by the employer. In any case, the trial court issued the preliminary injunction, including Category 4.

CATEGORY 4 - THE NON-COMPETE - GETS CHALLENGED

Not surprisingly, after the injunction issued, the parties continued to battle over the meaning and scope of the injunction language, with TRG saying the employees were still soliciting its clients, and the employees saying they

didn't know what "solicit" meant (not their best argument, in my humble opinion).

But the workers also said (a) they had obtained customer information from public sources; and (b) they had used only that public information in order to contact (and solicit) the customers, so that Category 4 was "invalid" as a restraint on their *lawful* competition. The dispute made its way to the appellate court by way of a writ.

Hat's off to Justice McDonald, writing for the appellate court, for doing a fine job summarizing the important public policies behind the competing employer/employee interests, and correctly distinguishing between the *prohibition on the use of trade secrets* (allowed) and the *prohibition on customer solicitation* (not allowed). While a little verbose (like I'm one to talk), the Court summarized:

"We distill from the foregoing cases that section 16600 bars a court from specifically enforcing (by way of injunctive relief) a contractual clause purporting to ban a former employee from soliciting former customers to transfer their business away from the former employer to the employee's new business,...

... but a court may enjoin tortious conduct (as violative of either the Uniform Trade Secrets Act and/or the Unfair Competition Law) by banning the former employee from using trade secret information to identify existing customers, to facilitate the solicitation of such customers, or to otherwise unfairly compete with the former employer."

In the end, the Court invalidated Category 4 of the injunction (which you should have anticipated by this point).

LESSONS LEARNED

Are there lessons here to be learned? Sure there are:

- 1) For attorneys representing employers in trade secrets cases - *don't overreach*, even if the trial court will give it to you. While the appellate work will make appellate specialist [Gerry Serlin](#) happy, does your client really want to pay for the losing battle?
- 2) Employers, *protect your trade secrets* - but understand that there's not much you can do if your former employees want to *fairly and lawfully* compete.
- 3) Employees who want to compete with a former employer, do so *fairly and lawfully*. This means developing your customer lists *after* your employment relationship is terminated, and base them on publicly available sources or your own hard work. Don't even think of downloading anything on your way out the door.
- 4) Read the Alston & Bird California Labor and Employment Blog regularly. We anticipated this issue (correctly, I might add) way back when. [Here's proof](#).

QUESTION - Did The TRG REALLY Get It Right?

Here's my question for those more smarter than I/me: The TRG court threw out Category 4, the non-compete portion of the injunction, because it violated the public policy reflected in B&P Section 16600. That section states that "**every contract** by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void." **Every contract!** The statute doesn't say "**every court injunction**" that restrains someone from practicing a trade is void, only **every contract!**

Don't the courts have some type of inherent equitable power to craft a remedy to fit the harm, so that if a trial court were to believe that *an injunction* forbidding competition was necessary to ameliorate a past bad act (to minimize the impact of prior trade secret misappropriation, for example), doesn't it have the power to issue such an injunction? If so, then maybe TRG wasn't analyzed quite properly. Email me your thoughts and I'll add them below.

I'm sure there's more to say, but I've got hours that need billing.

