

New Legislation in New York Bars Non-Competes

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Update: On December 23, 2023, New York Governor Hochul vetoed the legislation described in this client advisory. Our short update on this development can be found [here](#).

The New York state legislature passed an amendment to the state's Labor Law that essentially bars the use of non-competes. The bill will go to Governor Hochul and will become law if she signs it. Here are the answers to some key questions about the substance of the legislation:

What does the legislation do? The bill provides that no employer or officer or agent of a corporation, partnership, LLC, or other entity may seek, require, demand or accept a "non-compete agreement" from any covered individual. A "non-compete agreement" is defined as any agreement between "an employer and a covered individual that prohibits or restricts" the individual from obtaining employment after the conclusion of the individual's "employment with the employer."

What individuals are covered by the legislation? The bill covers any person who "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." This language should encompass all employees. The definition of covered individuals could, in some cases, include independent contractors.

Does the legislation apply to highly compensated employees? Yes. Unlike recent statutes in a number of other states barring non-competes for lower compensated employees, the New York legislation does not have a carve out or exception for highly compensated individuals. The legislation applies to covered individuals regardless of compensation level.

Does the legislation apply to garden leave agreements? The bill provides that it does not impact employers' ability to enter into contracts for a fixed term of service provided that the agreement does not otherwise restrict competition in violation of the statute. Since a garden leave provision typically restricts or prohibits an employee from working for a competitor for a period of time, it appears that garden leave provisions could be void under this new legislation.

Does the legislation cover agreements not to solicit clients? The bill states that it does not impact agreements prohibiting an employee from soliciting "clients of the employer that the covered individual learned about during employment, provided that such agreement does not otherwise restrict competition in violation" of the statute. Thus, non-solicits of clients should continue to be enforceable if they meet New York's existing common law test for enforceability and if (a) they apply only to clients about whom the employee learned during their employment and (b) the provision is not so broad that it effectively prohibits or restricts the employee from working for a competitor. It is not clear whether the phrase "learned about during employment" will be interpreted expansively or narrowly, so employers should carefully examine the language they use in non-solicitation agreements.

Does the legislation cover agreements not to solicit employees? The bill does not mention solicitation of employees. An agreement by an individual not to solicit other employees of a former employer is unlikely to “prohibit or restrict” that individual from obtaining new employment, so there are strong arguments that carefully tailored agreements not to solicit employees will not be impacted by this legislation.

Does the legislation cover confidentiality agreements? The bill does not prohibit agreements preventing an employee from disclosing trade secrets or confidential and proprietary client information, as long as those agreements do not otherwise restrict competition in violation of the statute.

Does the legislation cover non-competes in long term incentive compensation arrangements that are subject to the employee choice doctrine? Some employers provide employees with stock options or restricted stock units that can be forfeited or clawed back if the employee competes with the employer. The employee thus has the choice of whether to (a) compete and lose the incentive compensation or (b) not compete and keep the incentive compensation. In this scenario, the employer’s sole remedy if the employee competes is the loss of the compensation, and the employer cannot prevent competition or specifically enforce the non-compete. Arguably, this type of provision would not prohibit or restrict an employee from obtaining subsequent employment. It remains to be seen, however, whether courts will interpret the legislation expansively so that it applies to these types of “employee choice” compensation provisions.

When does the ban on non-competes take effect? The new legislation will take effect 30 days after it is signed by the governor.

Does the legislation apply retroactively? The statute provides that it applies to contracts “entered into or modified on or after” the effective date of the statute. Despite this, the Sponsor’s Memo submitted to the Senate with the bill states that Section 3 of the bill “[v]oids current non-compete agreements” Section 3 of the bill provides:

Every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void. For all covered individuals, 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.

An interpretation of this section that applies it retroactively as suggested in the Sponsor’s Memo seems contrary to the explicit provision of the statute that it applies only to contracts entered into or modified on or after the effective date. An interpretation that the statute voids existing contracts is likely to be met with legal challenges.

Does the legislation provide penalties for violations? Yes. Covered individuals can bring civil actions in any court of competent jurisdiction within two years of the later of (a) signing a prohibited non-compete, (a) learning of a prohibited non-compete, (c) termination of employment, or (d) when the employer takes steps to enforce a prohibited non-compete. Courts are empowered to void a prohibited non-compete, to enjoin enforcement of the non-compete, and to award lost compensation, other damages, and reasonable attorneys’ fees. In addition to those remedies, the statute provides that courts may award liquidated damages of up to \$10,000 to every covered individual affected by the statute.

What should employers in New York do? Employers with employees in New York should carefully review their existing post-employment restrictions in preparation for the effective date of the legislation. This includes the following potential considerations:

- using choice of law provisions applying the law of another state where feasible;
- increasing reliance on carefully tailored non-solicitation of clients and employees provisions and confidentiality agreements;
- identifying contracts that automatically renew upon expiration and considering whether those contracts will be impacted if they renew after the effective date of the new legislation; and

- exploring the feasibility of moving employees with whom non-compete agreements are critical out of New York.

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