

HOUSE BILL REPORT

ESSB 5478

As Reported by House Committee On: Labor & Workplace Standards

Title: An act relating to restraints, including noncompetition covenants, on persons engaging in lawful professions, trades, or businesses.

Brief Description: Concerning restraints on persons engaging in lawful professions, trades, or businesses.

Sponsors: Senate Committee on Labor & Commerce (originally sponsored by Senators Liias, Keiser, Conway, Hunt, Pedersen, Kuderer and McCoy).

Brief History:

Committee Activity:

Labor & Workplace Standards: 3/19/19, 3/25/19 [DP].

Brief Summary of Engrossed Substitute Bill

- Makes noncompetition covenants unenforceable unless an employee earns more than \$100,000 per year.
- Creates a presumption that a noncompetition covenant longer than 18 months is unreasonable and unenforceable.
- Establishes other provisions relating to competition and creates remedies.

HOUSE COMMITTEE ON LABOR & WORKPLACE STANDARDS

Majority Report: Do pass. Signed by 4 members: Representatives Sells, Chair; Chapman, Vice Chair; Gregerson and Ormsby.

Minority Report: Do not pass. Signed by 2 members: Representatives Mosbrucker, Ranking Minority Member; Hoff.

Staff: Joan Elgee (786-7106).

Background:

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Washington disfavors restraints on trade. However, restraints are permitted in some circumstances. A noncompetition agreement, one type of restraint, is an agreement between parties where one party promises not to compete with the other party for a specific period of time, and sometimes within a specified geographic area. Statutory law addresses noncompetition agreements only in the broadcasting industry.

Under the common law, Washington courts will enforce a noncompetition agreement if the agreement is reasonable. Reasonableness involves consideration of three factors, which are whether the:

1. restraint is necessary for the protection of the business or goodwill of the employer;
2. restraint imposes on the employee any greater restraint than is reasonably necessary to secure the employer's business or goodwill; and
3. degree of injury to the public is such loss of the service and skill of the employee as to warrant nonenforcement of the agreement.

In evaluating the reasonableness of an agreement, the courts examine the time and geographic scope of the restraint. If a court finds that an agreement is unreasonable, the court may reform the terms of the agreement.

In general, if a noncompetition agreement is agreed to after an employee is hired, the agreement is enforceable only if the employer gives the employee independent consideration, such as a raise or a promotion.

Summary of Bill:

Restrictions on Noncompetition Covenants.

Certain restrictions apply to noncompetition covenants (covenant) with employees. A covenant is void and unenforceable unless the employer discloses the terms in writing to a prospective employee. If the covenant becomes enforceable only at a later date due to changes in the employee's compensation, the employer must specifically disclose that the covenant may be enforceable in the future. If the covenant is entered into after employment commences, the employer must provide independent consideration for the covenant.

A covenant is unenforceable unless the earnings from the party seeking enforcement exceed \$100,000. In addition, if an employee is terminated as the result of a layoff, the covenant is void unless enforcement includes compensation equivalent to the employee's base salary at the time of termination for the period of enforcement minus compensation earned through subsequent employment, a so-called "garden leave" clause.

A presumption is created that any covenant with a duration longer than 18 months is unreasonable and unenforceable. To rebut the presumption, a party must prove to a court or arbitrator by clear and convincing evidence that a longer duration is necessary to protect the party's business or goodwill.

Covenants with persons other than employees are also addressed. A covenant with an independent contractor is unenforceable unless the contractor's earnings from the party

seeking enforcement exceed \$250,000 per year. The dollar thresholds for enforceable covenants with employees and with independent contractors are adjusted annually by the Consumer Price Index. A covenant between a performer and a performance space, or a third party scheduling the performer for a performance space, may not exceed three calendar days.

A provision in a covenant signed by an employee or an independent contractor who is Washington-based is unenforceable if it requires the employee to adjudicate a noncompetition agreement outside the state and to the extent it deprives the employee of the substantive protection of Washington law.

Other Limits on Employment.

A franchisor may not restrict, restrain, or prohibit a franchisee from soliciting or hiring an employee of a franchisee of the same franchisor or any employee of the franchisor.

An employer may not restrict, restrain, or prohibit an employee earning less than twice the state minimum wage from having an additional job, supplementing their income by working for another employer, working as an independent contractor, or being self-employed. This provision does not apply in specified circumstances, including if the additional services raise safety issues. In addition, the obligations of an employee to an employer under existing law are not altered.

Remedies.

If a court or arbitrator determines that a covenant violates the provisions, or if the court reforms or only partially enforces a covenant, the party seeking enforcement must pay the aggrieved person the greater of the actual damages or \$5,000, plus reasonable attorneys' fees, expenses, and costs. An aggrieved person who is a party to the covenant may bring a cause of action for these remedies, and the Attorney General (AG), on behalf of a person or persons, may pursue any and all relief.

Definitions.

A "noncompetition covenant" includes every written or oral agreement by which an employee or independent contractor is prohibited or restrained from engaging in a lawful profession, trade, or business of any kind. Certain agreements are declared not to be noncompetition agreements, including nonsolicitation and confidentiality agreements. A "nonsolicitation agreement" is an agreement that prohibits solicitation by an employee of any employee of the employer to leave the employer or of any customer to cease or reduce the extent to which it is doing business with the employer.

"Earnings" is the compensation reflected on box one of the Internal Revenue Service Form W-2 for employees and Form 1099 for independent contractors.

Other.

Except as provided, the provisions do not revoke, modify, or impede the development of the common law. The provisions displace conflicting tort, restitutionary, contract, and any other laws relating to liability for competition by employees or independent contractors with their employers or principals.

The act takes effect January 1, 2020, and applies to all proceedings commenced on or after the effective date, regardless of when the cause of action arose. Otherwise, the law applies prospectively.

The provisions must be construed liberally.

Appropriation: None.

Fiscal Note: Not requested.

Effective Date: The bill takes effect on January 1, 2020.

Staff Summary of Public Testimony:

(In support) This bill is the result of years of work. While negotiators did not get everything they wanted, the bill reflects good policy. The bill will help reduce and eliminate the use of noncompete agreements for low wage workers so they are not restrained in earning a livelihood. Many blue collar workers, including grocery store workers and electricians, have been subject to noncompete agreements. The bill will also put common sense restrictions on noncompete agreements for higher wage earners such as technology workers; which restrictions will also help startup businesses. The bill reflects a carefully negotiated balance between business and labor.

(Opposed) None.

(Other) The bill is a compromise. One problem is Section 9, which mandates penalties if the judge even slightly modifies the agreement. Amendatory language will be provided.

Persons Testifying: (In support) Senator Liias, prime sponsor; Joe Kendo, Washington State Labor Council; and Debbie Gath, Teamsters Union Local 38.

(Other) Bob Battles, Association of Washington Business; and Tim O'Connell, Stoel Rives.

Persons Signed In To Testify But Not Testifying: None.