

## New Massachusetts Noncompetition Law Will Impact PE Investors

### PENpoints

*Companies with employees in Massachusetts should review and update their form Noncompetition Agreements in light of the new law.*

On October 1, 2018, a new Massachusetts noncompetition statute went into effect that will impact PE investors with offices or portfolio companies located in Massachusetts. The key provisions of the new law are set forth below.

#### Definition Of “Noncompetition Agreement”

The new law broadly defines “Noncompetition Agreements” as any agreement in which an employee or independent contractor “agrees that he or she will not engage in certain specified activities competitive with his or her employer after the employment relationship has ended.”

The new law does not apply to:

- confidentiality and intellectual property protection provisions;
- employee nonsolicitation and no-hire provisions;
- covenants not to solicit or transact business with customers, clients or vendors;
- restrictions during the employment/contracting relationship;
- sale-of-business noncompetition provisions where the restricted party is a “significant owner of, or member or partner in, the business entity” and will receive “significant consideration or benefit” from the transaction;
- noncompetition provisions that are outside of an employment relationship, which seems to imply that partnership, limited liability company, stockholder and other similar agreements in which an individual is a partner, member or owner, rather than an employee, may be exempt from the new law under this exception (particularly where employees of one entity (e.g., a management company) are partners in, or members or owners of, a different entity (e.g., a limited partnership)); or
- covenants negotiated and entered into at the time of a separation from service, so long as the person is expressly given seven business days to rescind acceptance.

#### Forfeiture-For-Competition Clauses Are Covered Noncompetition Agreements

The new law covers any “agreement that by its terms or through the manner in which it is enforced imposes adverse financial consequences on a former employee as a result of the termination of an employment relationship if the employee engages in competitive activities.”<sup>1</sup>

#### Limits on Noncompetition Period

Noncompetition Agreements may not exceed one year, unless the individual breached his or her fiduciary duty or unlawfully obtained or retained property belonging to the company, in which case the duration may not exceed two years.

#### Must Be Consideration

Noncompetition Agreements entered into at the inception of the relationship must be supported by garden leave (which is simply severance) or “other mutually-agreed upon consideration,” which is not defined (but initial employment may satisfy this requirement).

Noncompetition Agreements entered into during the relationship must be supported by “fair and reasonable consideration independent of continuation of employment,” which is also not defined.

Until there is further clarity regarding what satisfies the alternative consideration requirements under the new law, consideration other than a provision for the payment of garden leave during the restricted period runs some risk of being deemed to be insufficient.

#### Garden Leave

Under the new law, a “garden leave” clause is sufficient consideration so long as it requires a company to pay

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the individual during the restricted period at least 50% of the individual's highest annualized base salary within the preceding two years.

If garden leave is provided as consideration, it should be paid for the length of the noncompetition period, up to one year.

### **Individuals Terminated Without Cause or Laid Off and Nonexempt Employees Cannot Be Bound to Noncompetition Agreements**

Any individual who is either (i) a nonexempt employee under the Fair Labor Standards Act or (ii) terminated "without cause" or "laid off" (with both terms being undefined in the law) cannot be subject to a Noncompetition Agreement. The new law is unclear regarding whether a company can still have noncompetition provisions with these individuals so long as the company is providing garden leave.

Alternatively, it may still be possible to secure noncompetition provisions from these employees either by structuring an employment agreement where an employee must give six months or a year of notice prior to terminating his or her employment or as negotiated at the end of the relationship, as both of these situations are not "Noncompetition Agreements" under the new law.

### **The Law Is Not Retroactive**

The new law only applies to agreements entered into on or after October 1, 2018. However, the new law does not address whether amended agreements or evergreen renewals on or after October 1, 2018, trigger the law.

### **Very Technical Requirements Must Be Satisfied To Have A Valid Noncompetition Agreement**

If entered into at the inception of the employment relationship, the employer must provide the candidate with the Noncompetition Agreement either at the time of a formal offer of employment or 10 business days prior to the commencement of employment, whichever is earlier.

If entered into during the employment relationship, the employee must have 10 business days to review the agreement before it becomes effective.

The Noncompetition Agreement must be in writing and signed by the employer and the individual.

The Noncompetition Agreement must explicitly state that the individual has the right to consult with counsel prior to signing.

### **The Law Covers Employees and Independent Contractors**

The new law covers employees and independent contractors who are employed or engaged in Massachusetts — but does not explicitly cover partners, members or owners.

### **Choice-of-Law Clauses**

The new law severely limits the parties' ability to circumvent its application by choosing another state's law to govern the agreement.<sup>2</sup>

\* \* \*

Companies with employees in Massachusetts should review and update their form Noncompetition Agreements in light of the new law.

1 In many states, such as New York, court will not scrutinize the reasonableness of a noncompetition provision so long as the only result of a breach is the loss of some benefit. Massachusetts appears to have foreclosed this legal construct by holding that such forfeiture clauses also need to conform to the parameters of the new law.

2 All civil actions relating to Noncompetition Agreements must be brought in the Massachusetts county where the individual resides (the new law does not specify that this must be in state court) or, if mutually agreed upon, in Suffolk County in Massachusetts (in the superior court or the business litigation session of the superior court).

If you have any questions about the matters addressed in this *KirklandPEN*, please contact the following Kirkland authors or your regular Kirkland contact.

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## PENbriefs

# U.S. Treasury Department Issues New Rule on Mandatory CFIUS Declarations

On October 11, 2018, the U.S. Department of the Treasury, as chair of the Committee on Foreign Investment in the United States (CFIUS), published an interim rule for a pilot program to implement certain provisions of the Foreign Investment Risk Review Modernization Act (FIRRMA). Under the Pilot Program, some investments by foreign persons in certain U.S. businesses will be subject to mandatory declaration requirements that obligate transaction parties to submit a short-form notice of the transaction to CFIUS in advance of closing. The Pilot Program represents a fundamental change to the CFIUS process — which has historically been voluntary — and is poised to have significant impacts on cross-border dealmaking. To learn more, see our recent [Alert](#).

## PENnotes

**Kirkland Registered Adviser Seminar & CCO Summit  
San Francisco, CA, October 18, 2018  
Los Angeles, CA, November 13, 2018**

Designed specifically for private fund manager CCOs, general counsel and other senior executives, this annual event enables firms to navigate the evolving regulatory landscape and get timely updates about SEC policy and enforcement developments affecting private fund managers. Click [here](#) for more information.

**Kirkland Direct Investing for the Family Office Seminar  
Chicago, IL, October 18, 2018**

Kirkland's Private Investment & Family Office Practice will host this networking lunch and learn, co-presented by Lazard Private Capital Advisory Group. The discussion will focus on the growing trend of direct investing and will aim to answer pertinent questions on the minds of family offices. Kirkland partners David Handler and Ryan Harris will present. Click [here](#) for more information or to register.

**IVCA CFO Summit for VC and PE Finance Professionals  
Chicago, IL, October 18, 2018**

Kirkland is a sponsor of this annual event, which is open to finance professionals and finance staff of venture capital and private equity professionals. Kirkland partner Bruce Ettelson will present the legal update at the event. Click [here](#) to register.

**NAIC Private Equity & Hedge Fund Conference  
Chicago, IL, October 24–25, 2018**

Kirkland sponsors this annual event, where institutional investors, CIOs, investment managers, consultants and others in the private equity and hedge fund industry discuss current investment strategies and research, and explore collaborative deals. The theme of this year's conference is "The Crossroads of Commerce and Capital." Click [here](#) for more information.

**Women's Alternative Investment Summit  
New York, NY, November 8–9, 2018**

Kirkland is a sponsor of this annual event, which will bring together more than 400 senior-level women across the broad spectrum of alternatives to network and discuss alternative investments in an emerging new world. Kirkland partners Jennifer Perkins, Stephanie Berdik, Erica Berthou and Linda Myers will participate in the event. Click [here](#) for more information.

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*The Lawyer* magazine has recognized Kirkland as one of its "Transatlantic Elite," having noted that the Firm is "leading the transatlantic market for the provision of top-end transactional services ... on the basis of a stellar client base, regular roles on top deals, market-leading finances and the cream of the legal market talent."

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