SENATE BILL REPORT
SSB 5935

As Passed Senate, February 6, 2024

Title: An act relating to noncompetition covenants.

Brief Description: Concerning noncompetition covenants.

Sponsors: Senate Committee on Labor & Commerce (originally sponsored by Senators Stanford, Keiser, Conway, Dhingra, Frame, Kuderer, Liias, Nobles and Saldaña).

Brief History:
Committee Activity: Labor & Commerce: 1/18/24, 1/23/24 [DPS, DNP, w/oRec].
Floor Activity: Passed Senate: 2/6/24, 29-20.

Brief Summary of First Substitute Bill

- Provides that the term noncompetition covenant also includes an agreement that directly or indirectly prohibits the acceptance or transaction of business with a customer.
- Modifies the exclusions related to the sale or purchase of goodwill or a business interest to apply if the person signing the covenant purchases or sells a 1 percent or more interest.
- Limits nonsolicitation agreement to current customers.
- Modifies the timeline for one of the exceptions to making covenants void, related to acceptance of an offer of work, to an initial oral or written acceptance.
- Makes a covenant void if the covenant allows or requires the application of choice or substance of law of a jurisdiction other than Washington State.
- Removes a requirement that an aggrieved person be a party to a covenant to bring an action for relief.

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

SENATE COMMITTEE ON LABOR & COMMERCE

Majority Report: That Substitute Senate Bill No. 5935 be substituted therefor, and the substitute bill do pass.

Signed by Senators Keiser, Chair; Conway, Vice Chair; Saldaña, Vice Chair; Hansen and Stanford.

Minority Report: Do not pass.

Signed by Senators Braun, MacEwen and Schoesler.

Minority Report: That it be referred without recommendation.

Signed by Senator King, Ranking Member.

Staff: Susan Jones (786-7404)

Background: In 2019 the Legislature passed laws making certain noncompetition covenants void and unenforceable.

Definitions. Noncompetition covenant includes every written or oral covenant, agreement, or contract by which an employee or independent contractor is prohibited or restrained from engaging in a lawful profession, trade, or business of any kind. It excludes a nonsolicitation agreement, a confidentiality agreement, a covenant prohibiting use or disclosure of trade secrets or inventions; a covenant related to a purchase or sale of the goodwill or an ownership of a business or related to franchises.

Nonsolicitation agreement is an agreement between an employer and employee that prohibits solicitation by an employee, upon termination of employment, of any coworkers or the employer's customers if it would cause them to cease or reduce doing business with the employer.

Void Noncompetes. A noncompetition covenant is void and unenforceable against an employee:

- unless the employer discloses the terms in writing no later than the time of the acceptance of the offer of employment and, if the agreement becomes enforceable only at a later date due to changes in the employee's compensation, the employer specifically discloses the agreement may be enforceable against the employee in the future; or if the covenant is entered into after the commencement of employment, unless the employer provides independent consideration for the covenant;
- unless the employee's earnings from the party seeking enforcement, when annualized, exceed a certain amount adjusted each year for inflation, currently $120,559.99; or
- if the employee is terminated as the result of a layoff, unless enforcement of the noncompetition covenant includes certain compensation.

A noncompetition covenant is void and unenforceable against an independent contractor

unless the independent contractor's earnings from the party seeking enforcement exceed a certain amount adjusted each year for inflation, currently $301,399.98.

Certain Covenant Provisions. There is a rebuttable presumption that any noncompetition covenant exceeding 18 months after termination of employment is unreasonable and unenforceable. A party seeking enforcement may rebut the presumption by proving by clear and convincing evidence a duration is necessary to protect the party's business or goodwill.

A provision in a noncompetition covenant signed by a Washington-based employee or independent contractor is void and unenforceable if the covenant requires the individual to adjudicate a noncompetition covenant outside of Washington; and to the extent it deprives the individual of the protections or benefits of this chapter.

Remedies. The attorney general or a party to the noncompetition covenant may bring a private right of action to pursue relief for violations. If a court or arbitrator finds a violation or if a court or arbitrator reforms, rewrites, or only partially enforces any noncompetition covenant, the violator or person seeking enforcement of the covenant must pay the aggrieved person the greater of the actual damages or a statutory penalty of $5,000, plus reasonable attorneys' fees, and costs. An action may not be brought for a covenant signed prior to January 1, 2020, if the noncompetition covenant is not being enforced.

Construction. The noncompetition covenant laws are an exercise of the state's police power and must be construed liberally for the accomplishment of its purposes.

Summary of First Substitute Bill: Definitions. Noncompetition covenant also includes an agreement that directly or indirectly prohibits the acceptance or transaction of business with a customer. The exclusions related to the sale or purchase or goodwill or a business interest to apply if the person signing the covenant purchases or sells a 1 percent or more interest. Nonsolicitation agreements apply only to current customers.

Void Noncompetes. The bill removes the language that the covenant is void against an employee. The timeline for one of the exceptions to making covenants void related to acceptance of an offer of work is modified to include an initial oral or written acceptance. A covenant for an employee or independent contractor is void if the covenant allows or requires the application of choice of law or substantive law of a jurisdiction other than Washington.

Remedies. The requirement that an aggrieved person be a party to a covenant to bring an action for relief is removed. The bill does not prohibit a cause of action if a covenant signed before January 1, 2020, is being explicitly leveraged. The bill adds to the laws displaced by the noncompete provisions to include contract principles related to discharge by assent or alteration.

Construction. The legislative findings are modified to provide that the noncompetition covenants laws to need to be liberally construed and exceptions narrowly construed.

Appropriation: None.

Fiscal Note: Available.

Creates Committee/Commission/Task Force that includes Legislative members: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony on Original Bill: *The committee recommended a different version of the bill than what was heard.* PRO: Noncompete clauses in contracts interfere with a person's ability to seek or accept a new job. We have to be very careful about restricting those choices. The original bill was a bipartisan bill that employees should be able to take their skills to the open market. There are many reasons that a person may need or want a new job like finding a new job that better utilizes their skills and abilities or the need to relocate. Noncompetes suppress wages and allows large companies to control workers. This is a follow up to the previous bill and updates the law based on experiences that have come up since the bill was enacted. The word changes are short and concise and reinforce the 2019 legislative intent. These reforms are sweeping the country and would provide clarity.

Some courts have not interpreted the intent of the Legislature. It does not impact the employers ability to protect their interests. It is necessary to clarify provisions that courts have misinterpreted or where employers argue certain provisions don't mean what they say. This has undermined the legislative purpose of worker mobility. The courts have also failed to embrace that the statute should be liberally construed. Some courts have required out of state litigation and application of non-Washington law because the statute uses the word or instead of the word and. One court ruled that the provisions, requiring the employee get the noncompete upon accepting, didn't apply because the employee accepted the job offer orally. Some employers threaten employees that they are subject to an invalid noncompete and include it in a severance agreement. A court in Washington held that this was not a violation of the statute.

The courts have misconstrued nonacceptance of business clauses as nonsolicitiation covenants. The employer can prevent a former employee from seeking out customers but not from accepting the business. Employers have been able to prevent former employees from taking the business. The 25 percent requirement for the sale of a business would generally not apply to many employees because of the income threshold. Now employers can offer a small percentage and have the employees sign a noncompete. This allows enforcement of a noncompete because of the sale of the small percentage of the company.

CON: There are concerns with the bill. Business was part of the negotiations in 2019 and

carefully negotiated a number of parts. Some of the language in the bill is redundant. For example, the requirements to construe the bill.

The two biggest concerns are related to nonsolicitions and the 25 percent in sales of businesses. The nonsolicitation language was specifically carved out in the negotiations. It looks like they are trying to address where the customer is trying track down the former employee. The bill eliminates the exception for nonsolicitation. The 25 percent issue for sales of businesses sounds like a reasonable number. However, for many big companies, 5 percent can be a controlling interest. This would apply for all companies except a small business.

Persons Testifying: PRO: Senator Derek Stanford, Prime Sponsor; Jesse Wing, Washington State Association for Justice; Sybill Hyppolite, Washington State Labor Council, AFL-CIO; Lawrence Cock, WA Employment Lawyers Association (WELA); Sung Shin; Elizabeth Sowa.

CON: Robert (Bob) Battles, Association of Washington Business (AWB).

Persons Signed In To Testify But Not Testifying: No one.