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California Court Strikes Down Overbroad Confidentiality Agreement as a de facto Non-Compete

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Trade secrets and other proprietary information can be among a business' most valuable assets and drive its competitive advantage. It is therefore ordinarily critical that employees be bound by an enforceable agreement that prohibits them from misusing or otherwise harming the value of the employer's confidential information. The recent California Court of Appeal decision, *Brown v. TGS Management Co., LLC* (2020) 57 Cal.App.5th 303, should be of concern to employers because it holds that an employee confidentiality agreement may be voided as a *de facto* unlawful non-compete agreement if it has the *effect* of preventing the employee from working in the industry.

In *Brown*, a securities trader sued TGS, his former employer, for unpaid bonuses. TGS counterclaimed for violation of the confidentiality provisions contained in Brown's employment agreement, contending no further payments were owed and that Brown was required to disgorge some of the compensation he had previously received. The arbitrator entered an award for TGS, the trial court confirmed, and Brown appealed.

On appeal, Brown contended his employment agreement defined "confidential information" so broad as to bar him from his chosen field of securities trading, in violation of California's public policy against non-compete. *See* Cal. Bus. & Prof. Code § 16600 ("section 16600"). The Court of Appeal agreed, holding the arbitrator acted in excess of its powers.

The *Brown* appellate court reasoned that TGS's definition of confidential information was "strikingly broad," and amounted to TGS claiming "for itself, without limitation, *all* information that is 'usable in' or that 'relates to' the securities industry." The definition encompassed all information used, or relating to "the Business" which was in turn defined to include virtually all subject matters pertaining to securities trading, with only two exceptions. The first was for information "generally known in the securities industry through legal means." The Court of Appeal agreed with Brown that this carve-out was essentially meaningless, because no such information would have value in his profession, which only creates value through the use of securities-related information that is not generally known.

The second carve-out from the definition of protected information was for information known to the employee before he joined TGS, "as evidenced by Employee's written records." The *Brown* court

took a particularly dim view of this exception, because it would mean that information which, by definition was not confidential before Brown began working at TSG, would become so unless Brown had written records proving he knew of it beforehand.

TGS did not defend the overbreadth of the definition of “confidential information,” but instead argued that the arbitrator had not exceeded his powers by declining to address its validity. But the Court of Appeal ruled the arbitrator was required to address the issue because Brown had mounted a facial challenge to the agreement.

The *Brown* court concluded that the confidentiality provisions in the employment agreement were void on their face as “patently” in violation of section 16600. “Collectively, these overly restrictive provisions operate as a de facto noncompete provision; they plainly bar Brown in perpetuity from doing any work in the securities field, much less in his chose profession of statistical arbitrage.”

The *Brown* decision is a reminder that companies with California employees should review their existing employee agreements to consider whether (i) they are tailored to protect actual confidential information, and (ii) the employee could try to nullify confidentiality obligations imposed therein by arguing that the agreement’s breadth unlawfully restrain the employee’s right to engage in the employee’s chosen profession or trade.

Trade secret misappropriation impacts businesses across a variety of industries, and the consequences can be severe. A potential victim of trade secret theft, or the accused, should swiftly consult experienced litigation counsel.

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