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California Employee Required to Challenge Non-Compete Clause in Indiana

Article By:

Anthony J Oncidi

Pietro A Deserio

Despite California's prohibition against non-compete agreements, a federal court in the Eastern District of California recently ruled that a California resident may be subject to the non-compete covenant in his employment agreement due to a provision in the agreement identifying Indiana as the parties' choice of forum and that state's law as the parties' choice of law. The lawsuit, *Scales v. Badger Daylighting Corp.* (Case No. 1:17-cv-00222-DAD-JLT), was (prior to removal to federal court) filed in California state court by the employee, Daniel Scales, after his employer, Badger Daylighting Corp., first filed a breach of contract action against Scales in Indiana state court.

Badger's Indiana lawsuit claims that Scales violated the non-compete clause in his employment agreement when he quit his employment with Badger in California and began working for one of the hydrovac excavation company's California competitors. Scales' employment agreement contains Indiana choice of law and choice-of-forum clauses. Trial for the Indiana action is set for January 23, 2018.

In Scales' later-filed California action, he seeks a declaratory judgment "that [his] respective Non-Competition Agreement [is] an unlawful and unenforceable restraint of trade, in violation of section 16600 of the California Business and Professions Code." Badger removed the case to federal court in the Eastern District of California based on diversity of citizenship and immediately filed a motion to dismiss based on the agreement's Indiana forum-selection clause.

U.S. District Judge Dale A. Drozd *granted* Badger's motion to dismiss on June 1, 2017, holding that the forum-selection clause was valid because it did not deprive Scales of his day in court and it did not contravene public policy. Judge Drozd reasoned that Scales has the financial means and opportunity to challenge the non-compete provisions of the employment agreement in the matter pending in Indiana state court – thus consigning Scales to the Indiana court for a determination of the enforceability of the non-compete.

Judge Drozd also rejected Scales' argument that enforcing the forum-selection clause would violate recently enacted California Labor Code § 925. The new law (which became effective this year) provides that an employer shall not require an employee who primarily resides and works in

California to agree to a provision that would either: (1) require the employee to adjudicate a claim outside of California that arose in California; or (2) deprive the employee of the substantive protection of California law with respect to a controversy arising in California. The statute also requires that a provision of a contract that violates § 925 is "voidable by the employee" and "the matter shall be adjudicated in California." The recently enacted law also awards attorneys' fees to employees seeking its protection. However, Judge Drozd correctly noted that § 925 applies only to contracts "entered into, modified, or extended on or after January 1, 2017." Scales signed his employment agreement in August 2014, and, therefore, is not covered by the protections of § 925.

Although non-California forum-selection clauses may sometimes save a non-compete from near-certain-death before a California court, Judge Drozd recognized that going forward, § 925 will generally preclude the enforcement of forum-selection clauses contained in agreements entered into on or after January 1, 2017, thus defeating out-of-state employers' attempts to evade California's non-compete restrictions.

Employers should review their employment agreements going forward to ensure compliance with § 925 and can begin by visiting the helpful FAQ we published earlier this year regarding the new law.

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