No-poach employment provisions – are they still acceptable?

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For years, the oil and gas industry, along with other sectors of the economy, has experienced a chronic shortage of qualified labor. In this era of low unemployment and lack of skilled workers with adequate training, employers are understandably protective of their workforce investments.

So when it's time to add new talent, you will advertise for positions, maybe pay a recruiter, invest in employee training and have ramp-up time before new hires are fully functional—all at significant effort and cost. In order to protect your investment in these employees, you may ask customers to agree to contract provisions prohibiting them from hiring your workers without your consent.

These types of restrictions have become commonplace and are a safe and standard practice, right? Well... maybe not anymore. A recent Pennsylvania court decision, which follows a series of federal litigation and policy actions, should cause employers to consider no-poach employment provisions in a new light. Such matters can be tricky and involve employment and/or antitrust issues, so business leaders should work closely with legal counsel.

Phase I–legal actions impacting competing businesses

In 2016, the U.S. Department of Justice (DOJ) and the Federal Trade Commission—the enforcers of antitrust laws—issued official guidance proclaiming that agreements amongst "competitors" to limit or fix terms of employment may violate antitrust laws if the agreements constrain individual decision-making regarding wages, salaries or benefits. According to the regulators, free competition leads to innovation, lower prices, better products, higher wages and better terms of employment. Arrangements between competitors not to hire each other's employees may constitute a "per se" violation of antitrust laws. Bad from the get-go.

The genesis of this guidance was the High-Tech Employee Antitrust Litigation, which involved Adobe Systems, Inc., Apple, Inc., Google, Inc., Intel Corp., Intuit, Inc., Lucasfilm, Ltd., Microsoft Corporation and Pixar. This massive case, which eventually settled, alleged that these various organizations each had agreements with one or more of the other parties containing restrictive provisions that essentially prohibited the organization from cold calling on the other's employees to recruit or solicit them directly for employment.

In a similar high-profile class action case against the University of North Carolina and Duke University, the plaintiff, an individual, brought a lawsuit when she was denied a position by UNC, allegedly due to an agreement between the universities not to hire each other's faculty. This case settled as well.

Since the issuance of the federal guidance, the antitrust agencies have taken additional enforcement action against competitive employers who had agreed not to poach each other's employees. However, the guidance is clear that it does not address the legality of specific restrictive terms contained in employer/employee agreements, including non-competes.

In 2018, the antitrust division of the DOJ filed suit against Knorr-Bremse AG and Westinghouse Air Brake Technologies Corp. (Wabtec). DOJ asserted these two large rail equipment suppliers, and eventually a third company purchased by Wabtec, conspired to "not poach" each other's employees. The suit was settled by the issuance of an injunction in which the companies agreed not to continue such behavior.

These various settlements did little to compensate the aggrieved employees. Class actions soon followed to correct these alleged wrongs as well.

Phase II–legal actions impacting franchise businesses

State governments have instituted investigations and class action litigation involving franchisors and restrictions contained in their franchise agreements prohibiting the poaching of employees between franchisees. Such provisions were added to these agreements so that all franchisees bear the costs and risks of training, and so that a franchisee could not simply set up shop and hire another organization's staff. In 2018, the Attorneys General in eleven states,

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including Pennsylvania, launched investigations into these issues. As of July last year, seven franchise organizations agreed to drop no-poaching clauses from their franchise agreements. A number of franchisors and franchisees have settled class action suits involving these claims.

In contrast, federal policy under the DOJ appears to make a distinction between the franchise no-poach agreements and no-poach agreements between competitors. According to DOJ policy, in the franchise context these arrangements are more akin to what is known as vertical restraints, which include arrangements between supply side organizations. DOJ does not see these arrangements as "per se" violations of the law, but they are reviewed under a standard of "rule of reason". This standard considers whether there is justification for the anti-competitive restriction that outweighs the alleged harm done by such restrictions, in other words whether the restraint is "unreasonable."

The ultimate outcome of these franchise issues has not been determined, including what justifications will be acceptable for such no-poach restrictions.

Phase III–recent court decisions in Pennsylvania

Pennsylvania businesses should take special note that courts in the Commonwealth recently have decided no-poaching issues for the first time. In *Pittsburgh Logistics Systems Inc. v. BeeMac Trucking LLC et al.*, the Superior Court of Pennsylvania upheld the lower court decision of the Beaver County Court of Common Pleas and invalidated a no-poaching agreement between the companies. Further appeals could occur.

The *Pittsburgh Logistics Systems* case involves a logistics company (arranging shipping) and a trucking company it utilized to ship its customers' goods. The agreement between the companies was non-exclusive and contained a non-solicitation as to customers and a non-solicitation as to employees. The lawsuit occurred because four logistics company employees left to work for the trucking company. The logistics company sought an injunction against the trucking company and the former employees to stop the prohibited behavior. The lower court and the appellate court both upheld the customer non-solicit, but determined the no-hire provision violated public policy by "preventing persons from seeking employment with certain companies without receiving additional consideration for the prohibition or even having any input regarding or knowledge of the restrictive provision."

The decisions of both courts did not discuss issues involving the protection of the investment in employees or the use of no-poach agreements in other kinds of commercial contracts. The courts summarily dismissed any rationale for having an employee no-poach agreement between companies, instead finding that avoiding the loss of clients was the ultimate purpose of the relevant restrictions and was addressed by the customer non-solicitation.

The Superior Court concluded that such no-hire provision "exceeds the necessary protection [the logistic company] needs to secure its business, and is void as a matter of public policy." In the court's view, these types of restrictions should be dealt with between the employer and employee, not between competing businesses. In Pennsylvania, it appears as though agreements between businesses not to steal customers may be enforceable, but agreements not to steal employees may no longer hold up.

Takeaways

Businesses using no-poaching agreements have a lot to consider in light of these various developments. In fact, in the two latest Pennsylvania legislative sessions, bills have been introduced to restrict non-compete provisions in the employment context both for low-income workers and also for all workers except for owners in the sale of a business.

Organizations with agreements governed by Pennsylvania law should review the terms of these types of restrictions in commercial contracts and take appropriate steps to protect their interests. If the *Pittsburgh Logistics Systems* decision holds up, companies may need to consider options for protecting investment in employees within the context of employer/employee agreements rather than in commercial agreements with customers. For example, employers could ask employees to acknowledge upon hiring that subsequent employment with a customer or competitor is prohibited, similar to a non-compete, whether or not the customer is a direct or indirect competitor. Employers that invest in employee training may want to consider having workers agree to a pay-back plan if they leave employment before there is a return on that investment. At a minimum, the parties to restrictive no-poach agreements should clearly spell out in their contracts that the interest they seek to protect is the significant investment in employees, along with the other interests of the client or customer.

In short, don't rely solely on your customer arrangements to protect your employee talent. ■

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