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UNFAIR COMPETITION

No trade secret? No problem

by Michael Futterman and Jaime Touchstone

A large laundry company sued a former employee who, during his employment, set up a competing business and prepared to solicit the company's largest customers. The company didn't prevail on its claims for misappropriation under California's Uniform Trade Secrets Act (UTSA), but the California Court of Appeal found that the UTSA didn't bar the company's independent claims for breach of contract, breach of fiduciary duty/duty of loyalty, unfair competition, interference with business relationships, and conversion.

Employer sues disloyal corporate officer

Angelica Textile Services provides linens and laundry services to health-care facilities throughout the United States. As market vice president, Jaye Park operated Angelica's San Diego and Phoenix laundry plants and negotiated service contracts between the company and its San Diego-based customers.

Park signed a noncompetition agreement, in which he promised to "give his best endeavors, skill and attention to the discharge of his duties with [Angelica] in a manner consistent with his position." He also agreed that during his employment, he would not "become interested, directly or indirectly, as a partner, officer, director, stockholder, advisor, employee, independent

contractor or in any other form or capacity, in any other business similar to [Angelica's] business."

Nevertheless, while still employed by Angelica, Park prepared to open Emerald Textiles, LLC, a competing linen and laundry enterprise in San Diego. He crafted a business plan containing detailed financial projections. He negotiated contracts on behalf of Angelica that allowed customers to terminate its services without cause on 90 days' notice, which Angelica alleged was contrary to the industry standard of long-term contracts. In pursuit of financing for his new venture, Park allegedly told bank officers that Angelica had cut back on spending, which had caused customers to complain about the poor quality of linens and service. He also told the bank that Angelica's equipment was old and in need of repairs.

After obtaining financing, Emerald built a state-of-the-art laundry facility. Park resigned from his position at Angelica, took thousands of pages of company documents with him, and began work as Emerald's chief operating officer. Led by Park, Emerald successfully bid on laundry contracts for Angelica's customers, which then terminated their Angelica contracts on 90 days' notice. After winning the contracts, Park recruited more than 40 of Angelica's former employees.



Angelica sued Emerald and Park for misappropriation of trade secrets under the UTSA, unfair competition, interference with business relationships, conversion (an unauthorized act that deprives an owner of personal property without consent), breach of fiduciary duty, and breach of a non-competition contract. The trial court found that Angelica's non-UTSA claims were displaced by the UTSA. Displacement generally occurs when a statute fully occupies a field of litigation and is intended to preempt common-law claims based on a violation of the statute. Angelica appealed, and the court of appeal reversed the trial court's decision.

UTSA didn't displace Angelica's claims

The UTSA establishes a comprehensive statutory scheme that defines "trade secrets" and "misappropriation," and it provides an aggrieved party with various remedies intended to protect its trade secrets. The Act is designed to preempt common-law trade secret misappropriation claims. However, the law expressly does not displace breach of contract claims or other civil remedies, regardless of whether they are based on an alleged misappropriation of a trade secret. Moreover, the UTSA doesn't displace other claims that are independent and based on facts distinct from those supporting a misappropriation claim.

The trial court dismissed Angelica's non-UTSA claims, including its breach of contract claim, concluding that those claims were all based on the alleged misappropriation of trade secrets and therefore were displaced by the UTSA. On appeal, however, Angelica stressed that Park breached his employment agreement and his duty of loyalty because, while still an employee, he disparaged the company to a local bank and negotiated new linen contracts with its largest customers, inserting unusually lax cancellation rights that allowed them to take their business to Emerald on short notice. Angelica argued that those facts independently supported its non-UTSA claims.

The court of appeal agreed with Angelica. Its claim for breach of contract was independent because it was based on Park's breach of his non-competition agreement. Its claims for breach of fiduciary duty, unfair competition, and interference with business relations also were independent because they were based on the noncompetition agreement and on Park's alleged breach of his duty of loyalty owed to his employer.

Similarly, Angelica's conversion claim wasn't displaced because even if the documents Park took when he left the company didn't contain trade secrets, they were still tangible property Angelica could seek to recover in a conversion claim. Thus, the company's non-UTSA theories of liability were independent of any claim for misappropriation of trade secrets and should be pursued.

Business and Professions Code didn't restrict claims

Business and Professions Code Section 16600 prohibits restraints on trade. It embodies a strong California public policy that invalidates employment agreements that unreasonably interfere with an employee's ability to compete with a former employer. Emerald argued that any claims that Park violated his employment contract should be barred by Section 16600.

The statute, however, doesn't prevent an employer from imposing non-competition restrictions on an employee during his employment. Nor does it weaken the duty of loyalty the employee owes to his employer. Further,

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directors and corporate officers such as Park aren't permitted to use their position of trust and confidence to further their private interests or injure the corporation. While technically not trustees, corporate officers stand in a fiduciary relationship to the corporation and its stockholders.

Because Angelica's non-UTSA claims were based on Park's allegedly improper conduct during his employment with the company, they weren't barred by Section 16600. *Angelica Textile Services, Inc. v. Jaye Park, et al.* (California Court of Appeal, 4th Appellate District, 10/15/13).

Bottom line

This is an important decision. It demonstrates that even if an employer can't prove a claim for misappropriation of trade secrets, there may be alternative legal theories available to seek redress from former employees. You can make your strongest argument when the employee's wrongful conduct occurs during his employment potentially in violation of his duty of loyalty or contractual obligations owed to you.

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