APPLICATION GROUP, INC. V. HUNTER GROUP, INC.

By Mark A. Kahn

Each state has its own laws reflecting different policy interests with respect to protection of trade secrets. Frequently, the laws of one state directly oppose the laws of another state. When a court must determine which state law to apply, inevitably, the court will issue a judgment that contravenes the policies of one of the states. In *Application Group, Inc. v. Hunter Group, Inc.*,[1] a California court was faced with a dispute arising out of a non-compete agreement. Contrary to the choice of law provision specifying that Maryland law would govern, the court chose to invalidate the non-compete agreement under California law rather than to uphold it as would be required under the laws of Maryland.[2]

Although the court analyzed the dispute under the proper framework, the court erred in invalidating the non-compete agreement. California and Maryland have very different laws that reflect different policy considerations with respect to non-compete agreements. When a California court must decide what state law to apply, the court ultimately must determine which state's policies would be impaired more by having the other state's law applied.[3] Here, the California court erred by failing to properly weigh the interests of Maryland in having its state law applied.

As technology continues to evolve and phenomena such as cross-country telecommuting become increasingly commonplace, courts will be faced with the question of what state law to apply in deciding whether a non-compete agreement is valid. Unfortunately, as is the case here, courts may not adequately consider the interests of the other state, and, as a result, state courts may make decisions that significantly affect other states.

I. BACKGROUND

Hunter Group, Inc. ("Hunter") is headquartered in Maryland with offices in various states including California.[4] In 1991, Hunter hired Dianne Pike, a Maryland resident, as a consultant in computerized human re-

1. 61 Cal. App. 4th 881 (1998).
2. *See id.* at 885.
3. *See* Nedlloyd Lines B.V. v. Superior Court, 3 Cal. 4th 459, 466 (1992).
4. *See Hunter*, 61 Cal. App. 4th at 885.

sources management systems.[5] While employed by Hunter, Pike worked at several customer sites, none of which were in California.[6]

When Hunter hired Pike, Pike signed an employment agreement that prohibited her from working for a competing company during her term of employment and for one year following the termination of her employment.[7] The agreement further specified that it was to be construed under Maryland law.[8] Despite signing the employment agreement, Pike resigned in 1992 to take a position with The Application Group, Inc. ("AGI"), a California corporation that directly competes with Hunter in the niche industry of human resources software consulting.[9] In her new position, Pike was hired for employment in California, although she continued to reside in Maryland.[10] Hunter demanded that Pike cease working for AGI and return to Hunter but Pike refused.[11]

A. Procedural History

In 1992, Hunter sued Pike in a Maryland circuit court for breach of contract.[12] In the same action, Hunter sued AGI for unlawful interference with Hunter's contractual relationship with Pike.[13]

Meanwhile, in April 1993, AGI and Pike filed a complaint in San Francisco Superior Court seeking a declaratory judgment stating that California Business & Professional Code section 16600 rather than Maryland law applied to Pike's covenant not to compete.[14] The California court, however, stayed that action pending the completion of the Maryland action.[15]

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5. *See id.* at 887.
6. *See id.*
7. The contract specifically stated that:
   During the term of [her] employment, and for a period of [one year] after the date of its termination, [Pike] agrees that [she] will not render, directly or indirectly, any services of an advisory or consulting nature, whether as an employee or otherwise, to any business which is a competitor of [Hunter].

Id.

8. The choice of law provision of the agreement provided that it was to be "governed by and construed in accordance with the laws of the State of Maryland." *Id.*
9. *See id.*
10. *See* Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881, 892 (1998).
11. *See id.* at 887.
12. *See id.*
13. *See id.*
14. *See id.* at 888.
15. *See id.*

In May 1994, the Maryland court issued judgments in favor of both Pike and AGI because Hunter failed to present evidence of damages.[16] The judgment of the Maryland court allowed the San Francisco Superior Court to move forward on AGI's and Pike's requests for declaratory relief. In December 1994, the law and motion department of the San Francisco Superior Court partially granted a summary judgment motion filed by AGI.[17] Specifically, the court held that "California law applied to Pike's covenant not to compete, which was 'invalid and unenforceable in California' as to her."[18]

In January 1995, the California court held a trial on the claims that survived the summary judgment motion.[19] Initially, the court denied AGI's claims for declaratory relief.[20] However, the court revised its findings in response to objections by AGI.[21] Specifically, in addition to reinforcing the findings of the court's law and motion department, the court held that California law applied to AGI's hiring of Hunter employees to engage in business in California because of California's strong public policy interests in invalidating non-compete agreements.[22]

B. The Court of Appeal Decision

The Court of Appeal affirmed the trial court's decision to apply California law rather than Maryland law to the non-compete clause of the employment agreement.[23] The Court of Appeal did not consider the merits of Pike's claims because the trailer clause in her contract had already expired and her claims had become moot.[24] However, AGI's claims were justiciable because AGI was seeking declaratory relief with respect to potential litigation regarding interference by AGI.[25]

To determine whether California or Maryland law should apply, the Court of Appeal engaged in a "governmental interest analysis" that the

16. *See* Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881, 887 (1998).
17. *See id.* at 889.
18. *See id.*
19. *See id.*
20. *See id.*
21. *See id.* at 890.
22. *See* Application Group, Inc. v. Hunter Group, Inc. 61 Cal. App. 4th 881, 890 (1998).
23. *See id.* at 909.
24. *See id.* at 894.
25. *See id.*

Ninth Circuit had previously applied.[26] Under this analysis, when state laws conflict, a California court must apply California law unless the competing state has significant interests in having its law applied.[27] When the competing state does have significant interests, the court must analyze the costs and benefits to each state.[28]

However, the court noted that in contractual disputes, the California court should apply the contractually specified substantive law unless:

> (1) the chosen state has no substantial relationship to the parties or the transaction, or
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> (2) application of the law of the chosen state would be contrary to a fundamental policy of the state.[29]

Here, because both Pike and Hunter had a relationship with the contractually specified state, the court focused on the second exception. The court cited *Nedlloyd Lines B.V. v. Superior Court*[30] in support of its decision to engage in a public policy analysis to determine whether the contractually specified substantive state law should be ignored.[31] Specifically, the Court of Appeal quoted the *Nedlloyd* court, which stated that the court must decide whether California has a "materially greater interest than the chosen state in the determination of the particular issue."[32]

The court then briefly examined the question of how the "governmental interest analysis," as explained in *S.A. Empresa de Viacao Aerea Rio Grandense v. Boeing Co.*,[33] relates to the "materially greater interest analysis," as explained in *Nedlloyd*.[34] The court noted that no court had explicitly undertaken such an analysis.[35] However, the Court of Appeal held that the Ninth Circuit, in *Empresa*, first analyzed the governmental interests of the states with conflicting laws and then determined "the extent to which those interests would be impaired by application of the other state's laws."[36] The Court of Appeal then held that a court must enforce

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26. *See id.* at 896 (construing S.A. Empresa de Viacao Aerea Rio Grandense v. Boeing Co., 641 F.2d 746 (9th Cir. 1981)).

27. *See id.*

28. *See* Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881, 896 (1998).

29. *Id.*

30. 3 Cal. 4th 459, 464-66 (1992).

31. *See Hunter*, 61 Cal. App. 4th at 897.

32. *Id.* at 897 (quoting *Nedlloyd*, 3 Cal. 4th at 466).

33. 641 F.2d 746 (9th Cir. 1981).

34. *See id.* at 898.

35. *See id.*

36. *Id.*

the contractual choice of law unless the interests of the other state are materially greater and the other state's interests would be more seriously impaired if the court followed the contractually specified substantive state law.[37]

While the Court of Appeal affirmed the trial court's decision, the court noted that the trial court did not analyze which state's law should be applied under the above framework.[38] Consequently, the Court of Appeal performed a thorough analysis to determine whether Maryland or California law should apply.

The court first noted that Maryland and California each have significant interests in having its own laws applied.[39] Consequently, the court had to determine which state had a "materially greater interest" in having its laws applied and which state's interests would be impaired more seriously if the other state's laws were applied.

In analyzing California's interests, the court explained that California has strong public policy interests in prohibiting non-compete agreements.[40] Specifically, the court noted that in California, employee mobility is more precious than competitive business interests of employers as long as trade secrets are not imperiled.[41] In addition, California prohibits non-compete agreements because they prevent California corporations from hiring the most talented and skilled workers in their industries.[42] According to the court, non-compete agreements promote anti-competitive behavior.[43] Finally, the court stated that because of the rapid developments in technology, California corporations need to be able to hire employees outside of California.[44]

With respect to Maryland's interests, the court noted Hunter's argument that Maryland allows non-compete agreements because employers should be allowed to prevent recruitment of employees who provide unique services.[45] In addition, non-compete agreements allow Maryland employers to prevent "the misuse of trade secrets, routes, or lists of cli-

37. *See id.*

38. *See* Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881, 899 (1998).

39. *See id.*

40. *See id.* at 900.

41. *See id.*

42. *See id.* at 901.

43. *See id.*

44. *See* Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881, 901 (1998).

45. *See id.*

ents, or solicitation of customers."[46] However, the court concluded that Hunter did not demonstrate that human resources consultants such as Pike either provide unique services or pose a threat to information protected by trade secret law.[47] Consequently, the court determined that California had a materially greater interest in having its laws applied.[48]

Finally, the court evaluated Hunter's claims that California's interests were irrelevant because of the "relevant contacts" of the parties with the states.[49] Specifically, Hunter argued that because Pike had contacts with only Maryland at the time the non-compete agreement was entered into, the court should follow the state law of Maryland.[50] The court held that Hunter's analysis of relevant contacts was strained and that relevant contacts include the following:

> (a) the place of contracting,
> (b) the place of negotiation of the contract,
> (c) the place of performance,
> (d) the location of the subject matter of the contract, and
> (e) the domicile, residence, nationality, place of incorporation and place of business of the parties.[51]

While the court acknowledged that Maryland would arguably be the appropriate choice in an analysis of the overall contract between Hunter and Pike, the court held that the covenant not to compete clause was performed in areas outside of Maryland, specifically in California.[52] In addition, because AGI, a California corporation, was involved, California had relevant contacts in the matter.[53] Finally, Hunter had significant contacts with California because it did business in California. Thus, according to the court, the "relevant contacts" requirement did not preclude the application of California law.[54]

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46. *Id.*
47. *See id.* at 901-02.
48. *See id.* at 902.
49. *See id.* at 903.
50. *See* Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881, 903 (1998).
51. *Id.*
52. *See id.* at 904.
53. *See id.* at 904-05.
54. *See id.* at 905.

II. DISCUSSION

In invalidating the non-compete agreement entered into between Hunter Group and its employee Pike, the court determined that California's public policy interests outweighed Maryland's public policy interests.[55] Specifically, the court cited California's historically strong public policy bias against non-compete agreements.[56] The court reasoned that Maryland's public policy interests in allowing companies to enter into non-compete agreements with their employees were not as strong as California's interests.[57] Here, the court made a fundamental error.

A. Non-Compete Agreements in California and Maryland

Before examining why the court erred, it is helpful to explore further the laws relating to non-compete agreements in each state. California and Maryland have very different attitudes toward non-compete agreements. In general, California has a strong policy against non-compete agreements, primarily because they severely limit employee mobility.[58] Meanwhile, Maryland permits non-compete agreements under trade secret protection theories.

1. California

California strongly favors employee mobility and, consequently, California laws explicitly forbid non-compete agreements.[59] The relevant statute provides in pertinent part that:

> Except as provided in this chapter, every contract by which anyone is restrained from engaging in a lawful profession, trade or business of any kind is to that extent void.[60]

The statutory exceptions are not relevant to this case.[61]

When applying the section, courts have detailed California's strong underlying public policy concerns.[62] Specifically, with respect to the em-

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55. *See* Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881, 902 (1998).

56. *See id.* at 900-01.

57. *See id.* at 901-02.

58. *See* Diodes, Inc. v. Franzen, 260 Cal. App. 2d 244, 255 (1968) (explaining the high premium courts place on employee mobility).

59. *See* Frame v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 20 Cal. App. 3d 668, 673 (1971).

60. CAL. BUS. & PROF. § 16600 (WEST 1997).

61. The statutory exceptions are detailed in CAL. BUS. & PROF. §§ 16601-16602. In general, the exceptions relate to agreements not to compete as conditions following the sale of a business or the dissolution of a partnership.

ployer-employee relationship, the law exists because of California's belief that an employee should be free to switch jobs whenever he or she desires.[63] From the employee perspective, the statute exists to protect a citizen's right to pursue any career or livelihood that he or she chooses.[64] In fact, California views this right as more important than the competitive business interests of employers.[65]

If non-compete agreements were valid in California, a citizen employed by Company A often would have to stay employed with Company A if he or she wanted to continue to work in the industries with which Company A is affiliated. Although an employee who is bound by a non-compete agreement usually could still work for countless companies in other industries, California's laws operate under the philosophy that an employee should be able to work for *any* company in any position. Moreover, an employee of Company A may have a strong desire to continue his or her career within Company A's industry. In addition, although some skill sets translate easily across industries, many do not, and an employee who is bound by a non-compete agreement may not be as employable in other industries.

In addition, under California law, as the court points out, employee mobility benefits employers as well as employees because it allows employers to have access to the best employees without restrictions.[66] Because of the prohibition on non-compete agreements, California companies are free to recruit employees from competitors. In her book, *Regional Advantage,* AnnaLee Saxenian analyzes why Silicon Valley has grown so rapidly, and she partially attributes the rapid growth to the high degree of employee mobility.[67] In Silicon Valley, professional networking occurs just as it does in other parts of the country.[68] However, in Silicon Valley, job opportunities arise frequently out of both informal and formal networking situations.[69] Naturally, with a substantial amount of networking taking place, employees in Silicon Valley are able to switch jobs relatively easily, and, in fact, Silicon Valley companies typically have abnormally

62. *See, e.g.,* Robinson v. Jardine Ins. Brokers Intern. Ltd., 856 F. Supp. 554, 558 (N.D. Cal. 1994); Diodes, Inc. v. Franzen, 260 Cal. App. 2d 244, 255 (1968).

63. *See Robinson,* 856 F. Supp. at 558.

64. *See id.*

65. *See Diodes,* 260 Cal.App.2d 244, 255 (1968).

66. *See* Application Group v. Hunter Group, 61 Cal. App. 4th 881, 901 (1998).

67. ANNALEE SAXENIAN, REGIONAL ADVANTAGE 34 (1996). The author is an Associate Professor in the Department of City and Regional Planning at the University of California, Berkeley.

68. *See id.*

69. *See id.*

high levels of turnover as compared to the rest of the country.[70] "This decentralized and fluid environment accelerated the diffusion of technological capabilities and know-how within the region."[71] Obviously, Silicon Valley companies benefit from access to employees with higher levels of knowledge. The effect manifests itself in two ways: 1) employers can seek to employ anyone and directly derive benefits from the new employees; and 2) more senior employees learn from their recently hired colleagues and become more efficient and productive. Thus, by not allowing non-compete agreements, California has created certain advantages for its employers.

Notably, in applying Section 16600, courts have recognized that trade secrets must still be protected.[72] Consequently, the strong bias towards employee mobility in California does not imply a lesser obligation on the part of employees with respect to trade secrets.[73] Thus, as the court in *Diodes, Inc. v. Franzen*[74] noted, although employee rights are more important than an employer's interest in preventing an employee from working for a competitor in general, the employee's rights do not permit the employee to misappropriate trade secrets after leaving a company.[75]

2. *Maryland*

Unlike California law, Maryland law permits employment contracts to contain post-employment non-compete provisions.[76] Specifically, Maryland statutes do not contain any explicit restrictions on the scope of non-compete agreements. Thus, the legality of non-compete agreements is determined entirely by common law.

Under Maryland common law, non-compete agreements are generally held to be valid. However, there are restrictions on the limitations that an employer can put on an employee through non-compete clauses. Specifically, for any restrictive covenant to be valid, there must be adequate consideration.[77] However, consideration need not be in the form of monetary

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70. *See id.* at 34-35.

71. *Id.* at 37.

72. *See e.g.,* Scott v. Snelling and Snelling, Inc., 732 F. Supp. 1034, 1043 (N.D. Cal. 1990).

73. *See* Loral Corp. v. Moyes, 174 Cal. App. 3d 268, 274-75 (1985).

74. 260 Cal. App. 2d 244 (1968).

75. *Id.* at 255.

76. For a thorough discussion of non-compete agreements in Maryland, see Barry F. Rosen & Steven A. Loewy, *Restrictive Covenants in Maryland Employment Agreements: A Guide for Drafting*, 11 U. BALT. L. REV. 379 (1982).

77. *See* Becker v. Bailey, 268 Md. 93, 96 (1973).

payments. In *Hekiman Laboratories, Inc. v. Domain Systems, Inc.*,[78] the court noted that "its research had revealed no case in Maryland in which the employer had agreed to additionally compensate the employee during the non-compete period."[79] Thus, although there must be consideration for the non-compete restriction, that consideration does not necessarily have to be additional payments explicitly made for the non-compete period.

Further, according to the court in *Becker v. Bailey*,[80] the non-compete agreement must be "confined within limits which are no wider as to area or duration than are reasonably necessary for the protection of the business."[81] The geographical and time limit tests are not static ones.[82] Instead, what is geographically reasonable or temporally reasonable will depend on the specific facts of the employer-employee relationship in question.[83]

The final limitation on non-compete agreements in Maryland is that they cannot "impose undue hardship on the employee or disregard the interests of the public."[84] In applying the reasonableness standard, Maryland courts will only enforce non-compete agreements to prevent the revelation of trade secrets or to restrict employees who provide unique services.[85]

Thus, while Maryland statutes do not prohibit non-compete agreements, the evolution of the common law in Maryland has imposed significant restrictions on how an employer can limit the mobility of ex-employees through non-compete agreements. As a result, although Maryland law allows non-compete agreements, Maryland law still permits a significant degree of employee mobility.

Maryland public policy allows non-compete agreements between employers and employees as part of its body of trade secret law. Non-compete agreements assist in the deterrence of trade secret misappropriation. An employee who considers working for a competitor or starting his or her own competing company might be tempted to use the information acquired during the course of performing his or her job. In addition, the employee could even seek out information specifically to use to compete with his or her employer. However, if the employee is bound by a non-compete agreement, the employee will likely realize that if he obtains trade secret protected information, he or she will be barred from using the

78. 664 F. Supp. 493 (1987).
79. *Id.* at 498.
80. 268 Md. 93 (1973).
81. *Id.* at 96.
82. *See id.* at 97.
83. *See id.*
84. *Hekiman*, 664 F. Supp. at 497.
85. *See id.*

information in competition. If the non-compete agreement were not in place, even if the employee knew that trade secret theft was illegal, the employee might be willing to take the risk, either consciously or subconsciously, of using the information while working for a competitor. Thus, because non-compete agreements prevent employees from obtaining jobs with competitors, employees who might be inclined to misappropriate trade secret information are deterred from doing so because they will have no means for using the misappropriated information.

Because non-compete agreements reduce the chances of trade secret misappropriation, they provide an incentive for employers to create.[86] When a company cannot be assured that it will be able to reap the benefits of whatever it creates, the company has less incentive to create.[87] On the other hand, when a company thinks that it will be able to exploit whatever it creates either directly or indirectly, the company has more incentive to create.[88] Thus, because non-compete agreements allow a company to ensure that its employees will be unable to compete with the company if the employee leaves, the company's incentives to create remain high. Even without non-compete agreements, a former employee would still be barred from misappropriating trade secrets.[89] However, with non-compete agreements, by definition, the company has a higher level of certainty that trade secrets will not be misused.

Moreover, non-compete agreements reduce indirect and transaction costs that companies would otherwise incur.[90] For example, if a company can be assured that a valuable employee will not leave for a competitor, the company does not need to expend resources ensuring that the valuable employee does not know too much. Although the company may still be vulnerable if the employee leaves for an entirely different career, it does not have to be concerned that the employee will leave for a new company in which the employee's knowledge directly affects the original company. Thus, the employer can operate more efficiently because each employee can be given as much information as is needed for the employee to do his or her job at an optimal level.

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86. For a detailed discussion and critique of the underlying rationales of trade secret law, see Robert G. Bone, *A New Look at Trade Secret Law: Doctrine in Search of Justification*, 86 CALIF. L. REV. 241 (Mar. 1998).

87. *See* ROBERT P. MERGES ET AL., INTELLECTUAL PROPERTY IN THE NEW TECHNOLOGICAL AGE 34-35 (1997).

88. *See id.*

89. *See* Barry F. Rosen & Steven A. Loewy, *Restrictive Covenants in Maryland Employment Agreements: A Guide for Drafting*, 11 U. BALT. L. REV. 379, 402 (1982).

90. *See* MERGES ET. AL., *supra* note 87, at 89.

Trade secret disputes involve significant costs to all parties involved.[91] Specifically, trade secret cases are extremely fact-intensive and thus frequently involve extensive discovery.[92] Moreover, attempting to prove trade secret violations may require the resources of critical employees whose time would otherwise be spent on more productive projects.[93] Finally, a plaintiff may incur numerous other direct and indirect costs over the course of investigating and litigating a trade secret dispute.[94]

Thus, non-compete agreements reduce the costs of trade secret litigation.[95] If an employee leaves for a competitor in potential violation of a non-compete agreement, the potential litigation can be narrowly focused on whether or not the employee's actions violated the clause. Admittedly, the employer still may not prevail if the non-compete agreement is not reasonable or if the new company is not actually a competitor, for example. However, the costs will be significantly less than if the employer has to engage in extensive discovery to determine whether or not the former employee misused information protected by trade secret laws. Moreover, without non-compete agreements, employees are free to work for competitors. In those situations, the former employers must consider whether or not it is worth investigating and/or litigating against the former employees for potential trade secret violations.

B. Why the Court Erred

In California, when a court is faced with a decision as to which of two conflicting laws to apply, the court may consider several factors. Among the major factors to be considered are the contractual choice-of-law provision, if it exists, and the relative interests of each state in having its law applied.[96]

Here, the court was justified in disregarding the choice-of-law provision that was present in the employment agreement between Hunter and Pike. Since both Hunter and Pike had substantial relationships with Maryland, the court focused on whether application of the law of Mary-

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91. *See* JAMES POOLEY, TRADE SECRETS §10.02[4] (1997).

92. *See id.*

93. *See id.*

94. Among the other costs are both intangible ones, such as a decline in employee morale or an increase in customer irritation, as well as tangible ones such as exposure to counterclaims and risk of loss of secrecy during litigation of the precise trade secret subject matter that is in dispute. *See id.*

95. *See* MERGES ET AL., *supra* note 87, at 89.

96. *See* S.A. Empresa de Viacao Aerea Rio Grandense. v. Boeing Co., 641 F.2d 746, 749 (9th Cir. 1981).

land conflicted with the fundamental policy of California.[97] Enforcing the choice-of-law provision would have meant upholding the validity of the non-compete agreement, and California has fundamental public policy interests against non-compete agreements.

However, as the court acknowledged, the inquiry does not end just because enforcement of Maryland's law would contravene California's public policy interests.[98] Instead, when a court must decide which state law to apply, the court must perform the "governmental interest analysis."[99] If each state has significant interests, the court will then compare the relative impairment to each state's policies if the other state's law is applied.[100] "[T]he 'comparative impairment' approach to the resolution of such conflict seeks to determine which state's interest would be more impaired if its policy were subordinated to the policy of the other state."[101] Under the comparative impairment analysis, the court does not compare the relative merits of the underlying policies of the two state's laws.[102] Rather, the court only considers whether applying each state's law would hamper the goals of the other state.[103] Here, the court determined that California's policies would be impaired more, and thus, the court invalidated the non-compete agreement.[104]

Although the court correctly laid out the test to be applied in determining which of two conflicting state laws to apply, the court did not apply the test correctly. Specifically, while the court accurately outlined California's interests in having the non-compete agreement invalidated, the court failed to adequately consider Maryland's interests in having the non-compete agreement upheld.

With respect to the California common law, the court did consider the policy interests underlying Section 16600.[105] The court took a global approach and determined that California has a strong policy against non-compete agreements.[106]

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97. *See* Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881, 897 (1998).

98. *See* Nedlloyd Lines B.V. v. Superior Court, 3 Cal. 4th 459, 466 (1992).

99. *See S.A. Empresa,* 641 F.2d at 749.

100. *See id.*

101. Bernhard v. Harrah's Club, 16 Cal. 3d 313, 320 (1976).

102. *See id.*

103. *See S.A. Empresa*, 641 F.2d at 749.

104. *See* Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881, 902 (1998).

105. *See id.* at 900-01.

106. *See id.*

While the court performed a cursory evaluation of the uniqueness of Pike's services as required under Maryland common law regarding non-compete agreements, the court did not consider the underpinnings of Maryland's acceptance of non-compete agreements.[107] With respect to Maryland, the court took a fact-specific approach and determined that Maryland did not have significant interests in having a non-compete agreement enforced in this particular situation.[108] Thus, the court did not make a fair comparison. Instead, the court should have compared the relative interests of each state using the same standard for each state.

Consequently, the court ignored Maryland's interests in having the non-compete agreement upheld. Because the court struck down the non-compete agreement, companies in Maryland will be unable to know in advance whether their non-compete agreements will truly protect them. As a result, companies could be forced to expend more resources protecting trade secrets. This decision reduces the benefits to Maryland and its companies derived from Maryland's laws that permit non-compete agreements without providing Maryland with the counterbalancing benefits found in a jurisdiction that prohibits non-compete agreements.[109]

In addition, the court ignored the intentions of the parties. Specifically, the parties knowingly entered into an employment agreement that contained a non-compete clause. Both employers and employees have a right to expect that courts generally will enforce contract provisions. This decision undermines those expectations. As a result, employers will be unable to rely as extensively on the validity of non-compete provisions even though their employees have agreed to them. Businesses include provisions such as non-compete clauses in employment contracts to provide them with a degree of certainty. Consequently, this decision reduces that degree of certainty.

Further, California companies will have a competitive advantage over Maryland companies. For example, suppose that Employee J works for Company X in Baltimore. The employment contract between Employee J and Company X includes a reasonable non-compete clause. Employee J decides to leave Company X but wants to remain in the same industry. In Company X's industry, there are two other companies that Employee J wants to work for: Company Y, another Maryland company and Company Z, a California company that will permit Employee J to telecommute from

107. *See id.* at 901-02.

108. *See id.*

109. *See supra,* Part II(A)(2) for a discussion of the benefits of non-compete agreements.

his home in Baltimore. Because of the non-compete clause, Employee J is prohibited from seeking immediate employment in a similar position with Company Y. However, according to the court in *Application Group v. Hunter Group*, Employee J would be free to work for Company Z. Thus, under this decision, Maryland can either force its companies to operate at a competitive disadvantage or change its laws to conform to California's laws.

In addition, the court over-emphasized the point that non-compete agreements limit access to the best employees by California employers. Trade secret law already limits such access to a certain degree. Specifically, a California company cannot hire away a competitor's employees if doing so would result in the misappropriation of trade secrets. For example, a manager at Yahoo! would be prevented from hiring a key programmer from Excite to reprogram Yahoo!'s search engine if doing so would result in the divulgence of Excite's trade secrets.[110] Consequently, California companies do not have access to the entire labor pool when the companies seek to fill positions.

Moreover, as the Yahoo!-Excite example illustrates, trade secret laws frequently will prevent California companies from hiring the potential employees who are most knowledgeable in the specific company's industry. Specifically, if Yahoo! could specify a skill set for its new programmers, the Excite employee would likely possess many of the key skills. Thus, although California places a high premium on employee mobility and on employers being able to recruit whomever they want, the realities of the market place and of trade secret laws significantly hinder these goals. While non-compete agreements undoubtedly further restrict who employers can and cannot hire, the court failed to acknowledge that some limitations already exist regardless of whether or not non-compete agreements are enforceable.

The court made a valid point in stating that the technological advances that have resulted in such phenomena as telecommuting mean that California companies are now more apt to employ people who live in other parts of the country in jobs that previously required physical presence at the office in California.[111] However, the court went too far when it stated that these advances justify invalidating non-compete agreements made between a Maryland company and a Maryland resident who is continuing

110. Yahoo! and Excite are two Silicon Valley companies specializing in Internet search engines.

111. *See* Application Group, Inc. v. Hunter Group, Inc., 61 Cal. App. 4th 881, 901 (1998).

to live in Maryland. The fact that Pike was telecommuting does not justify the court's refusal to respect or even consider the underlying reasons that Maryland has chosen to allow non-compete agreements.

In *Roll Systems, Inc. v. Shupe*,[112] a Massachusetts district court also invalidated a non-compete agreement under California law even though the contract specified that Massachusetts law was governing.[113] While the court did not explicitly state that the residency of the employee was determinative, in explaining that California had a materially greater interest than Massachusetts, the court specifically noted that the employee was continuing to work and live in California.[114] Moreover, "the fact that [the defendant's] contract was not performed in Massachusetts substantially decreases the Commonwealth's interest in having its laws govern this dispute."[115] In contrast, Hunter was continuing to live in Maryland, and the court did not accurately consider Maryland's interests in having its laws applied.

However, a bright-line test based on residency and physical location of employment does not solve the telecommuting problems suggested by the court in *Hunter*. Determining which state has a materially greater interest inevitably will continue to be a fact-intensive dilemma. Perhaps courts should focus on the business relationships that a given company has with the other state. For instance, it may be reasonable to invalidate non-compete agreements entered into by Microsoft or AT&T with employees who are now leaving to seek work in Silicon Valley. Both Microsoft and AT&T have significant business contacts in California. Moreover, both of those companies have broad contacts in California that touch upon many different areas of business. In contrast, a company such as Hunter Group has very limited business contacts with California. Of course, courts will not necessarily be able to easily apply this test.

Ultimately, the problem may require a federal trade secret solution. As the United States workforce becomes more and more fluid, the need for federal trade secret laws to govern these types of situations will only increase. Otherwise, we will likely continue to be faced with state courts making decisions that have significant impacts on other states.

112. 1998 U.S. Dist. LEXIS 3142 (D. Mass. Jan. 22, 1998).
113. *Id.*
114. *Id.* at *7.
115. *Id.* at *7 n.2.

III. CONCLUSION

In *Application Group, Inc. v. Hunter Group, Inc.,* the court erred in failing to properly consider the interests of Maryland in having the non-compete agreement upheld. As a result, companies in Maryland and other states will have to act with the understanding that a non-compete agreement will be ineffective if an employee becomes affiliated with a California company and has requisite contacts with California, even if the employee continues to work and live outside of California. Although the decision underscores the need for clear laws regarding employment situations that have only become significant with recent advances in technology, a California court is not the place for such laws to be made. Rather, the proper mechanism for determining the validity of non-compete agreements as they relate to employees telecommuting across state lines is probably federal legislation.

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