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In-House Non-Competes Put to the Test

Complaint by BASF staff lawyer prompts ethics investigation

By Henry Gottlieb

Lawyer regulators in New Jersey have begun the first known inquiry by a state into the ethical propriety of non-compete covenants that some corporations require of in-house counsel.

Agreements that restrict lawyers' practices upon termination of a relationship are unethical under Rule of Professional Conduct 5.6, effective

Florham Park corporate offices of BASF Corp., whose staff lawyers have been asked to sign a non-compete covenant.

in most states, including New Jersey.

But no state Supreme Court has ruled on the rule's applicability to in-house counsel, says David Stryker, general counsel of chemical giant BASF Corp.

Stryker should know. The New Jersey Supreme Court's Advisory Committee on Professional Ethics got into the issue two weeks ago, when an unidentified lawyer at BASF's Florham Park office asked for a ruling that RPC 5.6 barred the company from requiring staff lawyers to sign a new companywide non-compete covenant promulgated in November.

Stryker said in an interview on Thursday that his research, before the covenant was written, suggested there was no bar to making lawyers sign it. Now, pending the committee's review, the agreement as it applies to the 30-member legal department is on hold.

Stryker said that when committee

secretary Samuel Conti told him the issue would be on the panel's January agenda, "I told him great, I would love to participate in the process and in the meantime we won't be requiring lawyers to sign." A final decision could take months and require hearings.

While it came to a head at BASF, the issue affects thousands of companies around the country that require lawyers to sign non-compete contracts, or that are thinking of doing so.

Corporate lawyers are sure to argue that if the plain language of RPC 5.6 does indeed make such covenants for corporate counsel void, an exception should be tailored.

"It is actually a relatively new development that corporate counsel think about whether they can do restrictive covenants and, if so, how, for in-house lawyers," says Michael Lampert, of Princeton's Saul Ewing,

who advises corporations on non-compete clauses and lectures on the subject to members of the American Corporate Counsel Association.

The relevant section of RPC 5.6 says, "A lawyer shall not participate in offering or making: (a) a partnership or employment agreement that restricts the rights of a lawyer to practice after termination of the relationship, except an agreement concerning benefits upon retirement."

Lawyers and Other Professionals

RPC 5.6 is based on the public policy that restrictions on lawyers' ability to practice could deprive clients of choice of counsel. That policy was the rationale for *Jacob v. Norris, McLaughlin & Marcus*, 128 N.J. 10 (1992), a New Jersey Supreme Court decision that courts around the country have cited in finding non-compete

clauses for defecting lawyers unenforceable.

That's in stark contrast to the law on non-compete clauses for other professionals and workers, which says restrictions are permissible if they are fashioned narrowly.

"Generally, non-competes are restraints of trade and courts allow them only in limited circumstances when you can demonstrate a real need for them," Stryker says.

He says that after joining BASF from Siemens Corp. two years ago, he decided that the BASF covenants in effect for at least 10 years were too broad. Key employees, including lawyers, could not work for a competitor until two years after leaving BASF.

A lawyer could go into private practice and could go in-house to a non-chemical company, but could not, for example, join the in-house opera-



THE CORPORATE VIEW: General Counsel David Stryker of BASF says companies need non-compete clauses to protect their innermost secrets.

tion of Dow Chemical Co. or DuPont Corp.

The three-part document at BASF, "The Secrecy and Invention Agreement," has a secrecy restriction, an anti-solicitation agreement that pro-

hibits departing lawyers from recruiting colleagues to go with them, and a non-competition agreement. The stricture on working for competitors is now one year.

There is no difference between the pact for lawyers and non-lawyers at the company, he says.

He says Dow and DuPont have non-compete strictures for in-house lawyers, which could not be confirmed. The general counsel for Dow did not return a call seeking confirmation and a representative of the counsel's office at DuPont declined to comment.

Stryker says the new covenant also focuses on defections to competitors but reduces the time restraint to one year. He says he does not know why the demand for new covenant signings generated a protest among some lawyers. "Lawyers have signed them routinely and the issue never came up," he says.

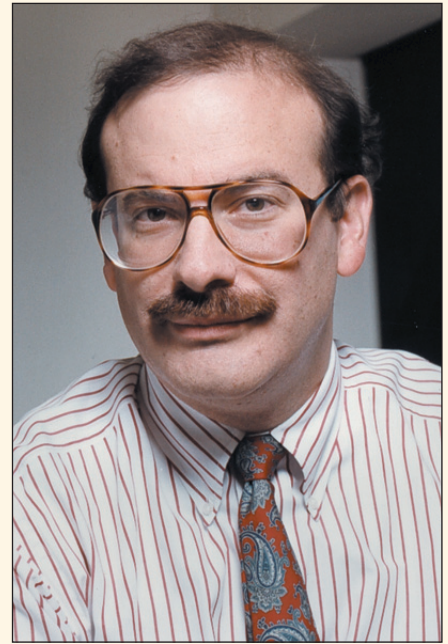
Lampert at Saul Ewing says a quick review of cases on the subject unearthed none about in-house lawyer covenants. In *The Hyman Companies, Inc. v. Brozost*, 964 F. Supp. 168 (1997), a federal court in Pennsylvania enjoined an in-house lawyer who handled store leasing for a retail jewelry company from doing the same work for a competitor. But that case isn't on point because there was no restrictive covenant.

Lampert says he reads RPC 5.6 to cover in-house counsel because corporations are in-house lawyers' clients and companies, like any other client, deserve an unfettered right to counsel of its choice. At the same time, he says, companies have a right to prevent the migration of secrets that in-house lawyers obtain when assuming non-legal titles or functions in a corporation, he says.

Would Macy's Tell Gimbels?

The issue is complicated by RPC 1.9, which covers conflicts of interest. RPC 1.9(b)(2), for instance, requires lawyers who acquired protected information in one firm to obtain consent before representing an adverse party.

Even without a non-compete agreement, an in-house lawyer at Macy's can't share Macy's secrets when she goes to any company, whether it's



EMPLOYEE-CLIENT DICHOTOMY: Medco Health Solutions general counsel David Machlowitz says non-compete rules for companies are different than those for law firms.

Gimbels or not.

"The bottom line is you can't have a covenant in a general sense in the same way you can't in a firm. I don't think there's a difference inside or outside in that way," Lampert says. "But if you have dual titles, you may be able to have a covenant. And it seems that with or without a covenant, RPC 1.9 prevents people from going to work for competitors if the competitor is actually adverse."

Stryker and two other general counsel for large corporations in the region say non-compete covenants for in-house counsel are common and are needed because the ethics rules alone aren't enough.

"It is my view that the confidentiality rules and the conflict of interest rules within the disciplinary rules do not cover every risk that is created when an in-house lawyer switches sides," Stryker says. "There is a gap that is unprotected without the non-compete."

In-house lawyers are far more integrated into decision-making than private lawyers called in for discreet matters, he says.

"It's not just data, it's the whole plan of the company, where we're going, what we're researching, what our targets are, our product information," he says.

"We can hurt a client much more than a guy from Kirkland & Ellis or Saul Ewing can if they try to switch sides," he says. "This short non-compete we use gives us that incremental protection for a one-year period."

"That's my view, there are views on the other side and the committee will decide which one prevails," he says.

Don Liu, general counsel at Toll Brothers Inc. in Horsham, Pa., says non-compete clauses for lawyers are common in corporations and that his company has them to prevent the flow

of secrets to competitors.

He says they are tailored narrowly and may be different for different lawyers, depending on the type of work they do for the corporation. When he was general counsel at Ikon Office Solutions Inc., attorneys were required to seek permission before taking a job at competitors like Xerox, he says.

David Machlowitz, general counsel of Medco Health Solutions Inc. in Franklin Lakes, suggests it is difficult drawing analogies between rules governing firms and rules governing corporations. A corporate non-compete rule is not like a law firm partnership non-compete rule because the corporation isn't just an employer, it's a client.

On the other hand, it also could be said that a corporation that can't hire a lawyer because of a non-compete clause is just losing out on an employ-

ee, he says.

Stewart Michaels, who heads Topaz Attorney Search in West Orange and is a former general counsel of Adidas United States, says he signed one there. No-compete and no-solicitation clauses for in-house lawyers are often included in the batches of documents lawyers sign when they take in-house positions, he says.

"AT&T gives a paper that says, before you join us I want to tell you that your choices are limited," he says. "They're enforceable."

Rees Morrison, a consultant at Hildebrandt Inc. in Somerville who advises corporate law departments, says that from a hiring perspective, non-compete clauses might not be a good idea below the general counsel level.

"It is already hard enough to recruit," he says. ■