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PERSPECTIVE

## Lessons from Delaware on noncompete best practices

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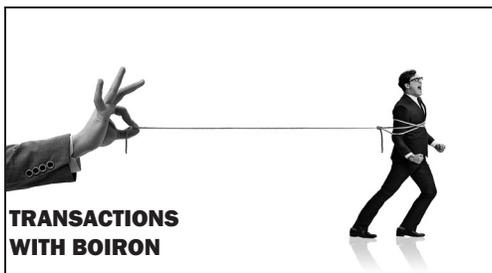
In *EBP Lifestyle Brands Holdings, Inc., v. Yann Boulbain*, the Delaware Court of Chancery granted a motion to dismiss on the grounds that the court lacked personal jurisdiction over the defendant, Boulbain, in a case involving the enforceability of non-competition and nonsolicitation provisions in a stockholders' agreement containing a Delaware choice-of-law provision but no Delaware forum-selection provision.

Boulbain was employed as a vice president of The Ergo Baby Carrier, Inc., a California-based company and subsidiary of EBP Lifestyle Brands Holdings, a Delaware corporation, until 2016, when the company terminated his employment.

EBP agreed to allow Boulbain to exercise his stock options after his termination, but required that Boulbain enter into a stockholders' agreement containing noncompetition and nonsolicitation restrictive covenants, as well as a Delaware choice-of-law provision. Stockholders are bound by the restrictive covenants for two years after final disposition of their shares of EBP stock, which is subject to the absolute discretionary approval of the majority stockholder. However, the stockholders' agreement did not contain a Delaware forum-selection provision or a Delaware consent to jurisdiction provision.

In 2017, Boulbain accepted employment as the chief executive officer of Petunia Pickle Bottom and Moby Wrap, California-based competitors of Ergo and, EBP alleged, Boulbain solicited employees of Ergo to join Boulbain at the new companies. EBP argued Boulbain's actions violated the terms of the noncompetition and nonsolicitation restrictive covenants in the stockholders' agreement and brought a claim for injunctive relief and specific performance.

In an opinion by Vice Chancellor Joseph R. Slight III, the court declined to enforce the restrictive covenants because the court lacked personal jurisdiction under both Delaware's long-arm personal jurisdiction



statute and the due process clause of the U.S. Constitution.

Under Delaware's long-arm statute, the plaintiff must demonstrate both that "(1) the nonresident transacted some sort of business in the state, and (2) the claim being asserted arose out of that specific transaction." The court concluded that although Boulbain entered into the stockholders' agreement with a Delaware choice of law provision and owned stock in a Delaware corporation, he did not have sufficient contact with Delaware to establish personal jurisdiction.

The court noted that Boulbain did not have any involvement in negotiating or drafting the stockholders' agreement. The court also emphasized Boulbain's lack of contact with Delaware, noting that he was a California resident, was employed in California, had never been to Delaware, and did not own any property in Delaware.

The court also rejected EBP's argument that Boulbain's actions as the vice president of EBP, or in his position with the competitor companies, namely transacting business in Delaware on behalf of the companies, could be imputed to Boulbain for the purpose of establishing personal jurisdiction due to the principles of the fiduciary shield doctrine.

The court also found personal jurisdiction lacking under the due process inquiry, which requires the defendant be "engaged in sufficient 'minimum contacts' with the State of Delaware," such that the defendant conducted deliberate and significant activities in Delaware. The court emphasized that Boulbain's actions involved the alleged conduct in California in violation of the

restrictive covenants and execution of a contract in California, and that Boulbain's only connection with Delaware was that EBP is a Delaware corporation and the stockholders' agreement contained a Delaware choice-of-law provision.

EBP also argued that finding personal jurisdiction would not violate the due process standard because Delaware has a strong interest in disputes involving corporate citizens seeking protection of Delaware's laws. However, the court rejected this argument citing *Ascension Ins. Hldgs. v. Underwood*, for the principle that "California's interest in preventing the enforcement of a covenant not to compete against a California resident employed and seeking to compete largely in California — and not in Delaware — is greater than Delaware's general, though profound, interest in vindicating freedom of contract."

Thus, the court concluded that exercising personal jurisdiction would violate due process because Boulbain lacked sufficient minimum contacts with Delaware, and due to California's greater interest in resolving the dispute.

The court noted in its conclusion that while its decision was limited to the issue of personal jurisdiction, Boulbain's motion to dismiss for failure to state a claim would likely be governed by *Ascension*, in which the court determined that, under the Restatement (Second) of Conflict of Laws Section 187, California had a "materially greater interest in the dispute than Delaware" in a case involving enforcement of a noncompete agreement executed and negotiated in California between a Delaware LLC with its principal place of business in California and a California resident.

Vice Chancellor Slight also noted that even if the Delaware choice-of-law provision was enforceable, he would still conclude that the noncompete provision was void under Delaware law as unreasonable in scope and duration. He emphasized that the noncompete provision restricted competition "anywhere in the world" for a period of two

years after the disposition of the stockholders' shares, and that the disposition was contingent upon the absolute discretionary approval of the majority stockholder.

*EBP Lifestyle* serves as a good reminder regarding best practices and current laws when California-based companies incorporated in Delaware are seeking to restrict the competitive activities of employees. A Delaware court will not exercise personal jurisdiction over a person with no connection to Delaware who is party to a stockholders' agreement that does not contain a Delaware forum-selection or consent to Delaware jurisdiction provision. More broadly, unless an agreement contains a Delaware forum-selection or consent to Delaware jurisdiction provision, a Delaware court likely will not exercise personal jurisdiction over a person with no connection to Delaware who is a party to an agreement that the person did not negotiate or draft but, instead, was required to sign to obtain a right to which he or she was entitled.

Second, as of Jan. 1, 2017, Section 925 of the California Labor Code prohibits a company from requiring an employee who primarily works and resides in California from signing, "as a condition of employment," an agreement containing

a forum-selection clause that requires a dispute to be brought in a court outside of California or from being governed by the laws of a state other than California. The only exception is where the employee is represented by counsel who is part of the negotiations regarding the forum-selection clause or the choice-of-law provision. Therefore, companies will have difficulty subjecting non-executive employees to noncompete agreements but may be able to subject executive employees, who often have their agreements reviewed and negotiated by counsel, to noncompetes governed by the laws of, or electing to have disputes brought in, a state other than California. Notwithstanding the dicta in *EBP Lifestyle* regarding the applicability of Delaware law to a California employee, working in California, for a California-based company, it is unclear whether, after the California legislature's implicit acceptance of non-compete agreements governed by the laws of, or electing to have disputes brought in, a state other than California for employees receiving advice from counsel, whether Delaware courts will reverse their existing position and no longer find that California has a greater interest in preventing the enforcement of noncompetes.

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