

THE STATE BAR OF CALIFORNIA
STANDING COMMITTEE ON
PROFESSIONAL RESPONSIBILITY AND CONDUCT
FORMAL OPINION NO. 2022-208

ISSUE: What are a lawyer's ethical duties when advising a client regarding the use of a contract provision in a transaction with a third party that is a violation of the law applicable to the transaction?

DIGEST: A California lawyer has a duty not to counsel or assist a client in conduct that the lawyer knows is criminal, fraudulent, or a violation of any law, rule, or ruling of a tribunal. As such, a lawyer shall not counsel or assist a client in presenting as lawful a contract provision that the lawyer knows violates the law, or otherwise defend the legality of the provision to a third party. If the lawyer knows that the provision violates the law, the lawyer should advise the client accordingly, may not recommend the use of the provision, and must counsel the client not to use it. If the client insists on using a provision that violates the law against the lawyer's advice, the lawyer may not participate in presenting the provision as lawful or defending its legality to a third party. The lawyer is permitted to withdraw from the representation if the client insists on using the provision and, depending on the client's continued conduct and the scope of the representation, may be required to do so. If the lawyer concludes that the client's conduct is a violation of law reasonably imputable to an organization and likely to result in substantial injury to the organization, the lawyer must report the actions of the client constituent to a higher authority within the organization, unless the lawyer reasonably concludes that it is not in the best lawful interest of the organization to do so.

AUTHORITIES

INTERPRETED: Rules 1.0.1(f), 1.1, 1.2.1, 1.4, 1.13, 1.16, 4.1, and 8.4(c) of the Rules of Professional Conduct of the State Bar of California.^{1/}

Business and Professions Code section 6068, subdivision (d).

^{1/} Unless otherwise indicated, all references to "rules" in this opinion will be to the Rules of Professional Conduct of the State Bar of California.

INTRODUCTION

Certain types of contract provisions are illegal under California law.^{2/} For example, provisions in employment contracts that impair the ability of employees to compete against their employers following termination of employment have been found to be illegal and unenforceable, and the use of these provisions violates California law, subject to specific, limited exceptions. See *Edwards v. Arthur Andersen LLP* (2008) 44 Cal.4th 937, 945 [81 Cal.Rptr.3d 282]; *Robinson v. U-Haul Co. of California* (2016) 4 Cal.App.5th 304, 309 [209 Cal.Rptr.3d 81]; *Brown v. TGS Management Co., LLC* (2020) 57 Cal.App.5th 303, 315 [271 Cal.Rptr.3d 303]; and Business and Professions Code sections 16600 and 17200.^{3/}

For purposes of this opinion, the committee does not opine on whether a particular clause in a contract violates the law as this raises an issue of law; instead, the committee confines its discussion to the ethical issues presented by the factual scenarios below and assumes that the contract provision in the hypothetical scenario violates the law at the time the agreement is made and not potentially subject to an exception that would make the provision legal. The opinion is not intended to address provisions that are legal, but against public policy, unenforceable, voidable, or subject to some other prohibition. Nor is it intended to address situations where the lawyer knows a court has held a provision to be unlawful, but nonetheless has a good faith belief that the ruling was incorrect, another court in the controlling jurisdiction has ruled or would rule otherwise, or the provision might be enforceable against the person who is being asked to sign it under reasonably foreseeable circumstances. See rule 1.2.1, Comment [3]; see also Cal. State Bar Formal Opn. 2020-202 (“Under the California Rules of Professional Conduct, a California-licensed lawyer is permitted to advise and assist a client in interpreting and complying with California law, including laws permitting and regulating commerce in cannabis, even if the client’s conduct violates federal law, provided that the lawyer informs the client of the conflict between state and federal law and does not advise or assist the client in concealing or evading prosecution for that conduct.”); Bar Association of San Francisco Legal Ethics Opn. 2015-1. **STATEMENT OF FACTS**

Lawyer works for a large California corporation (“Company”) providing employment law advice to the Human Resources department (“HR”) responsible for all nonexecutive hiring. Employees hired through HR are presented with a standard form written employment agreement (“Agreement”). This Agreement is presented by HR to all nonexecutive new hires in California as a nonnegotiable agreement that must be signed as a condition of employment. Lawyer is tasked with reviewing and updating the Agreement, which contains a material provision that violates California law.

FACTUAL SCENARIOS

Scenario 1

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69 Lawyer knows that the provision violates California law but advises HR to use the Agreement
70 anyway, without informing HR that the provision violates California law.

71 **Scenario 2**

72 Lawyer does not know that the provision violates California law, and Lawyer performs no
73 research or analysis to determine the legality of the provision but advises HR to use the
74 Agreement anyway.

75 **Scenario 3**

76 Lawyer advises HR that the provision violates California law but does not recommend against
77 including the provision.

78 **Scenario 4**

79 Lawyer advises HR that the provision violates California law and recommends against including
80 the provision. HR advises Lawyer that it understands the provision violates California law but
81 would still like to include it in the Agreement for its chilling effect. HR then instructs Lawyer to
82 include the provision in the Agreement as is and to assist HR in presenting the Agreement to its

^{2/} The use of the term “illegal” in this opinion refers to a provision that violates the law. ^{3/} In *Arthur Anderson*, the Supreme Court concluded that “section 16600 prohibits employee noncompetition agreements unless the agreement falls within a statutory exception” *Edwards v. Arthur Andersen LLP* (2008) 44 Cal.4th 937, 946 [81 Cal.Rptr.3d 282, 289] (“Under the statute’s plain meaning, therefore, an employer cannot by contract restrain a former employee from engaging in his or her profession, trade, or business unless the agreement falls within one of the exceptions to the rule.”). The Court also stated that “following the Legislature, this court generally condemns noncompetition agreements. (See, e.g., *Armendariz v. Foundation Health Psychcare Services, Inc.* (2000) 24 Cal.4th 83, 123, fn. 12 [99 Cal.Rptr.2d 745] [such restraints on trade are ‘largely illegal’].)” *Ibid.* See also, *Brown v. TGS Management Co., LLC* (2020) 57 Cal.App.5th 303, 315 [271 Cal.Rptr.3d 303] (“An employer’s use of an illegal noncompete agreement also violates the UCL (§ 17200 [‘unfair competition shall mean and include any unlawful, unfair or fraudulent business act or practice and unfair, deceptive, untrue or misleading advertising’].) [Citations.]”).

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83 employees as a condition of their employment. HR also asks Lawyer to defend the legality of
84 the provision if asked about it by any Company employees.

85 DISCUSSION

86 A. Duty to Advise of an Illegal Contract Provision

87 Rule 1.2.1(a) states that a “lawyer shall not counsel a client to engage, or assist a client in
88 conduct that the lawyer *knows* is criminal, fraudulent, *or a violation of any law, rule, or ruling of*
89 *a tribunal.*” (Emphasis added.) Rule 1.2.1 is modeled in substance after former rule 3-210 but
90 adds clarifying language derived from ABA Model Rule 1.2(d). The California rule is broader
91 than ABA Model Rule 1.2(d)^{4/} Both the California rule^{5/} and the ABA Model Rule allow a lawyer
92 to discuss the legal consequences of any proposed course of action and counsel or assist the
93 client in interpreting the application of any law, rule, or ruling to that course of action.^{6/}

94 The California rule on its terms applies to every type of legal representation, including
95 transactional work and negotiation. In the transactional context, a lawyer is “counsel[ing] a
96 client to engage” or “assist[ing] a client in conduct” when the lawyer recommends the inclusion
97 of a provision in a contract that the lawyer knows violates the law, or agrees to present or
98 defend the legality of that provision to a third party. See ABA Model Rule 1.2, Comment [10]
99 (“The lawyer is required to avoid assisting the client, for example, by drafting or delivering
100 documents that the lawyer knows are fraudulent or by suggesting how the wrongdoing might
101 be concealed.”); ABA Section of Litigation, *Ethical Guidelines For Settlement Negotiations*
102 (August 2002), at pp. 46-47 (“A lawyer should not negotiate a settlement provision that the
103 lawyer knows to be illegal.”).^{7/}

104 In Scenario 1, Lawyer recommends the inclusion of a provision that Lawyer knows is illegal
105 under California law in violation of rule 1.2.1(a) and potentially not subject to an exception that

^{4/} ABA Model Rule 1.2(d): “A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law.”

^{5/} Rule 1.2.1(b): “Notwithstanding paragraph (a), a lawyer may: (1) discuss the legal consequences of any proposed course of conduct with a client; and (2) counsel or assist a client to make a good faith effort to determine the validity, scope, meaning, or application of a law, rule, or ruling of a tribunal.”

^{6/} See generally Cal. State Bar Formal Opn. 2020-202 for discussion on the scope of permitted advice and assistance a lawyer may provide to clients related to conduct described in rule 1.2.1(a).

^{7/} The ABA Model Rules may be looked to for guidance on proper professional conduct, particularly in areas where there is no contrary California authority or conflicting public policy. See rule 1.0, Comment [4] (“Ethics opinions and rules and standards promulgated by other jurisdictions and bar associations may also be considered” for guidance on proper professional conduct.).

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would make the provision legal.^{8/} Rule 1.0.1(f) defines knows: “‘Knowingly,’ ‘known,’ or ‘knows’ means actual knowledge of the fact in question. A person’s knowledge may be inferred from circumstances.” Here, knows means Lawyer has actual knowledge that including the provision in question violates California law.

Conversely, in Scenario 2, Lawyer does not know that the specific type of contract provision is illegal under California law. Therefore, Lawyer does not violate rule 1.2.1.

However, in Scenario 2, Lawyer likely violated the duty of competence under rule 1.1(a) because Lawyer’s conduct reflects a deliberate or reckless disregard for the lawfulness of the specific provision. Knowing that the specific provision is illegal is likely to be reasonably necessary to provide competent legal advice to HR on employment law matters consistent with rule 1.1(b), particularly to the extent it is well-established that this type of provision is illegal and that including an illegal provision in an employment contract violates California law.^{9/} Rule 1.1(c) allows a lawyer to fulfill the duty of competence by associating or consulting a lawyer the lawyer reasonably believes to be competent or acquiring sufficient learning and skill to become competent before advising the client on a material legal provision. A lawyer’s failure to do so might be reckless or grossly negligent under rule 1.1(a). See *In the Matter of Morse* (Review Dept. 1994) 3 Cal. State Bar Ct. Rptr. 24 (Respondent’s mass advertising without thoroughly researching relevant statute to evaluate exemption was “grossly negligent and could be characterized as reckless or intentional after he disregarded the later request from the Attorney General’s Office that he stop mailing unlawful advertisements.”); see also rule 1.1(b).

B. Duty Not to Assist in the Use of an Illegal Contract Provision or Misrepresent the Legality of Provision

While the ABA frames this issue in terms of fraud or crime, the duty is broader in California because our variation of ABA Model Rule 1.2(d), rule 1.2.1, also adds violation of any law, rule, or ruling of a tribunal, even if those violations do not amount to a crime or fraud.

In Scenario 3, Lawyer has a duty under rule 1.2.1 not only to advise the client or client constituent, HR, on the applicable law and the possible consequences of using the provision in question, but also to recommend against its use. See also rule 1.4(b) (“A lawyer shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation.”).

In Scenario 4, because HR insists on including the illegal provision for its chilling effect contrary to Lawyer’s advice, Lawyer must advise Company regarding the limitations on Lawyer’s conduct, including that Lawyer will not represent Company in presenting the Agreement to

^{8/} The committee would reach the same conclusion in all four scenarios if Lawyer was the original drafter of the agreement.

^{9/} Under the Labor Code, it is illegal for an employer to “require any employee or applicant for employment to agree, in writing, to any term or condition which is known by such employer, or agent, manager, superintendent, or officer thereof to be prohibited by law.” (Lab. Code, § 432.5.)

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139 Company employees or otherwise defend the legality of the provision. Rule 1.2.1, Comment [5];
140 rule 1.4(a)(4).

141 If Lawyer ultimately decides to assist Company by including the provision for its chilling effect
142 and presenting it to Company employees as a condition of their employment, or otherwise
143 vouching for the legality of the provision to those employees, Lawyer's conduct is a
144 misrepresentation by omission or an affirmative misrepresentation that the provision is legal.
145 See rule 4.1(a), Comment [1].^{10/}

146 Rule 8.4(c) also states that it is professional misconduct for a lawyer to "engage in conduct
147 involving dishonesty, fraud, deceit, or reckless or intentional misrepresentation." Presenting a
148 third party with a knowingly illegal provision in an employment agreement for its chilling
149 effect^{11/} would violate rule 4.1(a), rule 8.4(c), and Business and Professions Code section 6068,
150 subdivision (d). See also California State Bar Formal Opinion 2015-194, where this committee
151 opined that a lawyer may not knowingly make false statements of fact or implicit
152 misrepresentations of material fact during negotiations.^{12/}

153 Traditionally, in representing a client in arm's-length business negotiations, a lawyer owes a
154 limited duty to the other side that does not include a duty to inform that party of relevant facts.
155 "[I]n drafting an agreement or other document on behalf of a client, a lawyer does not
156 necessarily affirm or vouch for the truthfulness of representations made by the client in the
157 agreement or document." Rule 4.1, Comment [1]. Nonetheless, a "nondisclosure can be the
158 equivalent of a false statement of material fact or law under paragraph (a) where a lawyer
159 makes a partially true but misleading material statement or material omission." *Id.*; see also Cal.
160 State Bar Formal Opn. 2015-194. In Scenario 4, if Lawyer presents employees with the
161 employment contract containing a knowingly illegal provision for its chilling effect or otherwise
162 defends the legality of a knowingly illegal provision, Lawyer's conduct goes beyond mere
163 drafting of the agreement. In presenting the agreement with the knowingly illegal provision for
164 its chilling effect, Lawyer would be making an implicit misrepresentation that the provision is
165 legal. Moreover, in defending the legality of the illegal provision, Lawyer would be engaging in
166 explicit misrepresentation of fact and dishonest or misleading conduct.

167 In addition, a lawyer may not make or ratify a false statement of law or fact made by the client
168 that the lawyer knows is false. See rule 4.1(a); see also S.C. Bar Ethics Opn. 05-03 (2005) (lawyer

^{10/} The committee is not addressing the potential application of rule 4.1(b), which is fact-specific and involves an interpretation of legal issues concerning what constitutes a "fraudulent act" under applicable law.

^{11/} The chilling effect includes situations where a client wants to include a term not just to frighten employees, but to obtain the client's desired result by inducing employees to comply with an illegal provision out of a mistaken fear of liability or fear of the risks and costs of litigation..

^{12/} Cal. State Bar Formal Opn. 2015-194 was issued prior to the time that rule 4.1 was enacted; the committee principally relied on existing statutory law (Bus. & Prof. Code, §§ 6106, 6128, subd. (a), and 6068, subd. (d)), and related California case law, but it also relied on ABA Model Rule 4.1 in support of its argument.

for ex-wife sent letter to ex-husband falsely claiming that ex-husband was required under divorce decree to undergo drug testing; this conduct violated South Carolina Rules of Professional Conduct 4.1 and 8.4(c)); *In re Discipline of Attorney* (2008) 451 Mass. 131 [884 N.E.2d 450] (lawyer disciplined under Massachusetts Rules of Professional Conduct, rule 8.4(c) alone for sending letters to insurers of opposing parties falsely claiming entitlement to lien on insurance payments payable to his clients). Here, Lawyer's defense of the legality of the provision would ratify the false statement of law made by the client in violation of rule 4.1(a).

C. Lawyer May Have a Duty to Withdraw from the Representation

In Scenario 4, if HR insists on including the illegal provision in Company's employment agreements, Lawyer may withdraw but is not compelled to withdraw merely because HR chooses to use the illegal provision despite Lawyer's admonition. Even where the use of that contract provision is deemed fraudulent or criminal, withdrawal from representation is permissive, not mandatory. Rule 1.2.1, Comment [1]; rule 1.16(b)(1)–(3).^{13/}

If, however, HR not only ignores Lawyer's advice but insists that Lawyer be involved with presenting and defending the illegal contract provision to its employees, Lawyer would likely be required to terminate the representation of Company with respect to this requested matter.^{14/} Rule 1.16(a)(2) provides that withdrawal is mandatory if "the lawyer knows or reasonably should know that the representation will result in violation of these rules or of the State Bar Act." Lawyer's continued, active participation in presenting and defending the illegal contract provision would likely violate rules 1.2.1, 4.1, 8.4, and Business and Professions Code section 6068, subdivision (d).¹⁵

^{13/} See rule 1.16(b) ("Except as stated in paragraph (c), a lawyer *may* withdraw from representing a client if: (1) the client insists upon presenting a claim or defense in litigation, or *asserting a position or making a demand in a non-litigation matter, that is not warranted under existing law and cannot be supported by good faith argument for an extension, modification, or reversal of existing law*; (2) the client either seeks to pursue a criminal or fraudulent course of conduct or has used the lawyer's services to advance a course of conduct that the lawyer reasonably believes was a crime or fraud; (3) the client insists that the lawyer pursue a course of conduct that is criminal or fraudulent . . ."). (Emphasis added.)

^{14/} In the case of an in-house lawyer, we assume that Lawyer would be permitted to ethically limit the scope of the representation to exclude any negotiation, defense, or enforcement regarding the illegal provision. See rules 1.2(b); 1.16(a)(2). Whether Lawyer would need to withdraw from other matters or whether Lawyer would be required to terminate Lawyer's employment at Company is beyond the scope of this opinion and depends on specific facts, including HR's instructions or continued demands, and whether the withdrawal from representation relating to the illegal provision would impact Lawyer's representation of Company on other matters.

^{15/} If this matter was before a tribunal, Lawyer may not reveal confidential advice or information regarding the use of the illegal provision in seeking withdrawal, except as required by rule 1.13. See rule 1.6 and Bus. & Prof. Code, § 6068, subd. (e)(1). See also, Cal. State Bar Formal Opn. 2015-192, generally,

D. Duty to Report Up in an Organization

Lawyer in Scenario 4 has a duty to report the conduct of the corporate constituent (e.g., HR) to a higher authority within Company because Lawyer knows that HR's conduct is illegal and the use and defense of a knowingly illegal contract provision for all nonexecutive new hires for its chilling effect is "likely to result in substantial injury to the organization." See rule 1.13(b).^{16/} Rule 1.13(b) provides for an exception to reporting up if the facts indicate that "it is not necessary in the best lawful interest of the organization to do so." *Id.* While the duty to report up is fact-specific, in Scenario 4, if HR insists on using the illegal provision or that Lawyer participate in presenting and defending the legality of the provision, reporting up would likely be in the best lawful interest of Company.

Moreover, because Lawyer has a duty not to withdraw without taking reasonable steps to avoid reasonably foreseeable prejudice to the organization client under rule 1.16(d), this disclosure must be made even if Lawyer opts to withdraw under the permissive withdrawal provisions in rule 1.16(b)(1)–(3). Beyond this scenario, a lawyer should evaluate carefully whether disclosure to a higher authority within the organization is reasonably necessary, which will depend on the relevant circumstances.

CONCLUSION

A California lawyer has a duty not to counsel or assist a client in conduct that the lawyer knows is criminal, fraudulent, or a violation of any law, rule, or ruling of a tribunal. As such, a lawyer shall not counsel or assist a client in presenting as lawful a contract provision that the lawyer knows violates the law, or otherwise defend the legality of the provision to a third party. If the lawyer knows that the provision is illegal, the lawyer: (1) should advise the client accordingly; (2) may not recommend the use of the provision; and (3) must counsel the client not to use it.

If the client insists on using the illegal provision against the lawyer's advice, the lawyer shall not participate in presenting the illegal provision to the third party and shall not assist the client in defending the legality of the provision against a third party. The lawyer is permitted to withdraw from the representation if the client insists on using the illegal provision and, depending on the client's continued conduct and the scope of the representation, may be required to do so.

for discussion on a lawyer's duty to maintain confidential information when withdrawing from a client representation.

^{16/} Company's use of an illegal provision is likely to result in substantial injury to the organization. See, e.g., Lab. Code, § 432.5 ("No employer, or agent, manager, superintendent, or officer thereof, shall require any employee or applicant for employment to agree, in writing, to any term or condition which is known by such employer, or agent, manager, superintendent, or officer thereof to be prohibited by law.").

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220 If the lawyer concludes that the conduct is a violation of law reasonably imputable to the
221 organization and likely to result in substantial injury to the organization, the lawyer for an
222 organization must report the actions of the client constituent to a higher authority within the
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 36 following termination of employment have been found to be illegal and unenforceable, and the
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The opinion is not intended to address provisions that are legal, but against public policy, unenforceable, voidable, or subject to some other prohibition. Nor is it intended to address situations where the lawyer knows a court has held a provision to be unlawful, but nonetheless has a good faith belief that the ruling was incorrect, another court in the controlling jurisdiction has ruled or would rule otherwise, or the provision might be enforceable against the person who is being asked to sign it under reasonably foreseeable circumstances. See rule 1.2.1, Comment [3]; see also Cal. State Bar Formal Opn. 2020-202 (“Under the California Rules of Professional Conduct, a California-licensed lawyer is permitted to advise and assist a client in interpreting and complying with California law, including laws permitting and regulating commerce in cannabis, even if the client’s conduct violates federal law, provided that the lawyer informs the client of the conflict between state and federal law and does not advise or assist the client in concealing or evading prosecution for that conduct.”); Bar Association of San Francisco Legal Ethics Opn. 2015-1. **STATEMENT OF FACTS**

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FACTUAL SCENARIOS

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Lawyer knows that the provision violates California law but advises HR to use the Agreement anyway, without informing HR that the provision violates California law.

Scenario 2

Lawyer does not know that the provision violates California law, and Lawyer performs no research or analysis to determine the legality of the provision but advises HR to use the Agreement anyway.

Scenario 3

Lawyer advises HR that the provision violates California law but does not recommend against including the provision.

Scenario 4

Lawyer advises HR that the provision violates California law and recommends against including the provision. HR advises Lawyer that it understands the provision violates California law but would still like to include it in the Agreement for its chilling effect. HR then instructs Lawyer to include the provision in the Agreement as is and to assist HR in presenting the Agreement to its

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employees as a condition of their employment. HR also asks Lawyer to defend the legality of the provision if asked about it by any Company employees.

DISCUSSION

A. Duty to Advise of an Illegal Contract Provision

Rule 1.2.1(a) states that a “lawyer shall not counsel a client to engage, or assist a client in conduct that the lawyer *knows* is criminal, fraudulent, *or a violation of any law, rule, or ruling of a tribunal.*” (Emphasis added.) Rule 1.2.1 is modeled in substance after former rule 3-210 but adds clarifying language derived from ABA Model Rule 1.2(d). The California rule is broader than ABA Model Rule 1.2(d)^{4/} Both the California rule^{5/} and the ABA Model Rule allow a lawyer to discuss the legal consequences of any proposed course of action and counsel or assist the client in interpreting the application of any law, rule, or ruling to that course of action.^{6/}

The California rule on its terms applies to every type of legal representation, including transactional work and negotiation. In the transactional context, a lawyer is “counsel[ing] a client to engage” or “assist[ing] a client in conduct” when the lawyer recommends the inclusion of a provision in a contract that the lawyer knows violates the law, or agrees to present or defend the legality of that provision to a third party. See ABA Model Rule 1.2, Comment [10] (“The lawyer is required to avoid assisting the client, for example, by drafting or delivering documents that the lawyer knows are fraudulent or by suggesting how the wrongdoing might be concealed.”); ABA Section of Litigation, *Ethical Guidelines For Settlement Negotiations* (August 2002), at pp. 46-47 (“A lawyer should not negotiate a settlement provision that the lawyer knows to be illegal.”).^{7/}

In Scenario 1, Lawyer recommends the inclusion of a provision that Lawyer knows is illegal under California law in violation of rule 1.2.1(a) and potentially not subject to an exception that

^{4/} ABA Model Rule 1.2(d): “A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent, but a lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law.”

^{5/} Rule 1.2.1(b): “Notwithstanding paragraph (a), a lawyer may: (1) discuss the legal consequences of any proposed course of conduct with a client; and (2) counsel or assist a client to make a good faith effort to determine the validity, scope, meaning, or application of a law, rule, or ruling of a tribunal.”

^{6/} See generally Cal. State Bar Formal Opn. 2020-202 for discussion on the scope of permitted advice and assistance a lawyer may provide to clients related to conduct described in rule 1.2.1(a).

^{7/} The ABA Model Rules may be looked to for guidance on proper professional conduct, particularly in areas where there is no contrary California authority or conflicting public policy. See rule 1.0, Comment [4] (“Ethics opinions and rules and standards promulgated by other jurisdictions and bar associations may also be considered” for guidance on proper professional conduct.).

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would make the provision legal.^{8/} Rule 1.0.1(f) defines knows: “‘Knowingly,’ ‘known,’ or ‘knows’ means actual knowledge of the fact in question. A person’s knowledge may be inferred from circumstances.” Here, knows means Lawyer has actual knowledge that including the provision in question violates California law.

Conversely, in Scenario 2, Lawyer does not know that the specific type of contract provision is illegal under California law. Therefore, Lawyer does not violate rule 1.2.1.

However, in Scenario 2, Lawyer likely violated the duty of competence under rule 1.1(a) because Lawyer’s conduct reflects a deliberate or reckless disregard for the lawfulness of the specific provision. Knowing that the specific provision is illegal is likely to be reasonably necessary to provide competent legal advice to HR on employment law matters consistent with rule 1.1(b), particularly to the extent it is well-established that this type of provision is illegal and that including an illegal provision in an employment contract violates California law.^{9/} Rule 1.1(c) allows a lawyer to fulfill the duty of competence by associating or consulting a lawyer the lawyer reasonably believes to be competent or acquiring sufficient learning and skill to become competent before advising the client on a material legal provision. A lawyer’s failure to do so might be reckless or grossly negligent under rule 1.1(a). See *In the Matter of Morse* (Review Dept. 1994) 3 Cal. State Bar Ct. Rptr. 24 (Respondent’s mass advertising without thoroughly researching relevant statute to evaluate exemption was “grossly negligent and could be characterized as reckless or intentional after he disregarded the later request from the Attorney General’s Office that he stop mailing unlawful advertisements.”); see also rule 1.1(b).

B. Duty Not to Assist in the Use of an Illegal Contract Provision or Misrepresent the Legality of Provision

While the ABA frames this issue in terms of fraud or crime, the duty is broader in California because our variation of ABA Model Rule 1.2(d), rule 1.2.1, also adds violation of any law, rule, or ruling of a tribunal, even if those violations do not amount to a crime or fraud.

In Scenario 3, Lawyer has a duty under rule 1.2.1 not only to advise the client or client constituent, HR, on the applicable law and the possible consequences of using the provision in question, but also to recommend against its use. See also rule 1.4(b) (“A lawyer shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions regarding the representation.”).

In Scenario 4, because HR insists on including the illegal provision for its chilling effect contrary to Lawyer’s advice, Lawyer must advise Company regarding the limitations on Lawyer’s conduct, including that Lawyer will not represent Company in presenting the Agreement to

^{8/} The committee would reach the same conclusion in all four scenarios if Lawyer was the original drafter of the agreement.

^{9/} Under the Labor Code, it is illegal for an employer to “require any employee or applicant for employment to agree, in writing, to any term or condition which is known by such employer, or agent, manager, superintendent, or officer thereof to be prohibited by law.” (Lab. Code, § 432.5.)

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139 Company employees or otherwise defend the legality of the provision. Rule 1.2.1, Comment [5];
140 rule 1.4(a)(4).

141 If Lawyer ultimately decides to assist Company by including the provision for its chilling effect
142 and presenting it to Company employees as a condition of their employment, or otherwise
143 ~~defending~~vouching for the legality of the provision to those employees, Lawyer's conduct is a
144 misrepresentation by omission or an affirmative misrepresentation that the provision is legal.
145 See rule 4.1(a), Comment [1].^{10/}

146 Rule 8.4(c) also states that it is professional misconduct for a lawyer to "engage in conduct
147 involving dishonesty, fraud, deceit, or reckless or intentional misrepresentation." Presenting a
148 third party with a knowingly illegal provision in an employment agreement for its chilling
149 effect^{11/} would violate rule 4.1(a), rule 8.4(c), and Business and Professions Code section 6068,
150 subdivision (d). See also California State Bar Formal Opinion 2015-194, where this committee
151 opined that a lawyer may not knowingly make false statements of fact or implicit
152 misrepresentations of material fact during negotiations.^{12/}

153 Traditionally, in representing a client in arm's-length business negotiations, a lawyer owes a
154 limited duty to the other side that does not include a duty to inform that party of relevant facts.
155 "[I]n drafting an agreement or other document on behalf of a client, a lawyer does not
156 necessarily affirm or vouch for the truthfulness of representations made by the client in the
157 agreement or document." Rule 4.1, Comment [1]. Nonetheless, a "nondisclosure can be the
158 equivalent of a false statement of material fact or law under paragraph (a) where a lawyer
159 makes a partially true but misleading material statement or material omission." *Id.*; see also Cal.
160 State Bar Formal Opn. 2015-194. In Scenario 4, if Lawyer presents employees with the
161 employment contract containing a knowingly illegal provision for its chilling effect or otherwise
162 defends the legality of a knowingly illegal provision, Lawyer's conduct goes beyond mere
163 drafting of the agreement. In presenting the agreement with the knowingly illegal provision for
164 its chilling effect, Lawyer would be making an implicit misrepresentation that the provision is
165 legal. Moreover, in defending the legality of the illegal provision, Lawyer would be engaging in
166 explicit misrepresentation of fact and dishonest or misleading conduct.

^{10/} The committee is not addressing the potential application of rule 4.1(b), which is fact-specific and involves an interpretation of legal issues concerning what constitutes a "fraudulent act" under applicable law.

^{11/} The chilling effect includes situations where a client wants to include a term not just to frighten employees, but to obtain the client's desired result by inducing employees to comply with an illegal provision out of a mistaken fear of liability or fear of the risks and costs of litigation. ~~Such a practice would also likely be considered to be an unfair business practice under California law in violation of Business and Professions Code section 17200 and related cases.~~

^{12/} Cal. State Bar Formal Opn. 2015-194 was issued prior to the time that rule 4.1 was enacted; the committee principally relied on existing statutory law (Bus. & Prof. Code, §§ 6106, 6128, subd. (a), and 6068, subd. (d)), and related California case law, but it also relied on ABA Model Rule 4.1 in support of its argument.

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In addition, a lawyer may not make or ratify a false statement of law or fact made by the client that the lawyer knows is false. See rule 4.1(a); see also S.C. Bar Ethics Opn. 05-03 (2005) (lawyer for ex-wife sent letter to ex-husband falsely claiming that ex-husband was required under divorce decree to undergo drug testing; this conduct violated South Carolina Rules of Professional Conduct 4.1 and 8.4(c)); *In re Discipline of Attorney* (2008) 451 Mass. 131 [884 N.E.2d 450] (lawyer disciplined under Massachusetts Rules of Professional Conduct, rule 8.4(c) alone for sending letters to insurers of opposing parties falsely claiming entitlement to lien on insurance payments payable to his clients). [Here, Lawyer's defense of the legality of the provision would ratify the false statement of law made by the client in violation of rule 4.1\(a\).](#)

C. Lawyer May Have a Duty to Withdraw from the Representation

In Scenario 4, if HR insists on including the illegal provision in Company's employment agreements, Lawyer may withdraw but is not compelled to withdraw merely because HR chooses to use the illegal provision despite Lawyer's admonition. Even where the use of that contract provision is deemed fraudulent or criminal, withdrawal from representation is permissive, not mandatory. Rule 1.2.1, Comment [1]; rule 1.16(b)(1)–(3).^{13/}

If, however, HR not only ignores Lawyer's advice but insists that Lawyer be involved with presenting and defending the illegal contract provision to its employees, Lawyer would likely be required to terminate the representation of Company with respect to this [requested](#) matter.^{14/} Rule 1.16(a)(2) provides that withdrawal is mandatory if "the lawyer knows or reasonably should know that the representation will result in violation of these rules or of the State Bar Act." Lawyer's continued, active participation in presenting and defending the illegal contract

^{13/} See rule 1.16(b) ("Except as stated in paragraph (c), a lawyer *may* withdraw from representing a client if: (1) the client insists upon presenting a claim or defense in litigation, or *asserting a position or making a demand in a non-litigation matter, that is not warranted under existing law and cannot be supported by good faith argument for an extension, modification, or reversal of existing law*; (2) the client either seeks to pursue a criminal or fraudulent course of conduct or has used the lawyer's services to advance a course of conduct that the lawyer reasonably believes was a crime or fraud; (3) the client insists that the lawyer pursue a course of conduct that is criminal or fraudulent . . ."). (Emphasis added.)

^{14/} In the case of an in-house lawyer, we assume that Lawyer would be permitted to ethically limit the scope of the representation to exclude ~~this matter~~[any negotiation, defense, or decline the representation if HR sought to have Lawyer negotiate, defend, advocate, or litigate enforcement regarding](#) the illegal provision. See rules 1.2(b); 1.16(a)(2). Whether Lawyer would need to withdraw from other matters or whether Lawyer would be required to terminate Lawyer's employment at Company is beyond the scope of this opinion and depends on specific facts, including HR's instructions or continued demands, and whether the withdrawal from representation relating to the illegal provision would impact Lawyer's representation of Company on other matters.

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provision would likely violate rules 1.2.1, 4.1, 8.4, and Business and Professions Code section 6068, subdivision (d).¹⁵

D. Duty to Report Up in an Organization

Lawyer in Scenario 4 has a duty to report the conduct of the corporate constituent (e.g., HR) to a higher authority within Company because Lawyer knows that HR's conduct is illegal and [the use and defense of a knowingly illegal contract provision for all nonexecutive new hires for its chilling effect](#) is "likely to result in substantial injury to the organization." See rule 1.13(b).^{16/} Rule 1.13(b) provides for an exception to reporting up if the facts indicate that "it is not necessary in the best lawful interest of the organization to do so." *Id.* While the duty to report up is fact-specific, in Scenario 4, if HR insists on using the illegal provision or that Lawyer participate in presenting and defending the legality of the provision, reporting up would likely be in the best lawful interest of Company.

Moreover, because Lawyer has a duty not to withdraw without taking reasonable steps to avoid reasonably foreseeable prejudice to the organization client under rule 1.16(d), this disclosure must be made even if Lawyer opts to withdraw under the permissive withdrawal provisions in rule 1.16(b)(1)–(3). Beyond this scenario, a lawyer should evaluate carefully whether disclosure to a higher authority within the organization is reasonably necessary, which will depend on the relevant circumstances.

CONCLUSION

A California lawyer has a duty not to counsel or assist a client in conduct that the lawyer knows is criminal, fraudulent, or a violation of any law, rule, or ruling of a tribunal. As such, a lawyer shall not counsel or assist a client in presenting as lawful a contract provision that the lawyer knows violates the law, or otherwise defend the legality of the provision to a third party. If the lawyer knows that the provision is illegal, the lawyer: (1) should advise the client accordingly; (2) may not recommend the use of the provision; and (3) must counsel the client not to use it.

If the client insists on using the illegal provision against the lawyer's advice, the lawyer shall not participate in presenting the illegal provision to the third party and shall not assist the client in

^{15/} If this matter was before a tribunal, Lawyer may not reveal confidential advice or information regarding the use of the illegal provision in seeking withdrawal, except as required by rule 1.13. See rule 1.6 and Bus. & Prof. Code, § 6068, subd. (e)(1). See also, Cal. State Bar Formal Opn. 2015-192, generally, for discussion on a lawyer's duty to maintain confidential information when withdrawing from a client representation.

^{16/} Company's use of an illegal provision is likely to result in substantial injury to the organization. See, e.g., Lab. Code, § 432.5 ("No employer, or agent, manager, superintendent, or officer thereof, shall require any employee or applicant for employment to agree, in writing, to any term or condition which is known by such employer, or agent, manager, superintendent, or officer thereof to be prohibited by law.").

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216 defending the legality of the provision against a third party. The lawyer is permitted to
217 withdraw from the representation if the client insists on using the illegal provision and,
218 depending on the client's continued conduct and the scope of the representation, may be
219 required to do so.

220 If the lawyer concludes that the conduct is a violation of law reasonably imputable to the
221 organization and likely to result in substantial injury to the organization, the lawyer for an
222 organization must report the actions of the client constituent to a higher authority within the
223 organization, unless the lawyer reasonably concludes that it is not in the best lawful interest of
224 the organization to do so.

**AB-747 Business: unlawful employee contracts and requirements.** (2023-2024)

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CALIFORNIA LEGISLATURE— 2023–2024 REGULAR SESSION

ASSEMBLY BILL**NO. 747****Introduced by Assembly Member McCarty****February 13, 2023**

An act to amend Section 16601 of, and to add Sections 6090.5.5 and 16608 to, the Business and Professions Code, and to amend Section 925 of, and to add Chapter 4.1 (commencing with Section 1058) to Part 3 of Division 2 of, the Labor Code, relating to business.

LEGISLATIVE COUNSEL'S DIGEST

AB 747, as introduced, McCarty. Business: unlawful employee contracts and requirements.

(1) Existing law provides that every contract that restrains anyone from engaging in a lawful profession, trade, or business of any kind is, to that extent, void, except as provided. Existing law authorizes any person who sells the goodwill of a business, any owner of a business entity selling or otherwise disposing of all of their ownership interest in the business entity, or any owner of a business entity that sells specified assets or ownership interests to agree with the buyer to refrain from carrying on a similar business within a specified geographic area in which the business so sold, or that of the business entity, division, or subsidiary has been carried on, if the buyer, or any person deriving title to the goodwill or ownership interest from the buyer, carries on a like business therein. Existing law defines "ownership interest" as a partnership interest, membership interest, or a capital stockholder, as described.

This bill would modify the definition of "ownership interest" to require the partnership interest, membership interest, or capital stock to be more than a 10% interest of the total partnership interest, more than a 10% interest of the total membership interest, or more than 10% of the total shares of ownership of the entity, respectively.

This bill would prohibit an employer, as defined, from entering into, presenting an employee, as defined, or prospective employee as a term of employment, or attempting to enforce any covenant not to compete, as defined, that is void, as described. The bill would provide that an employer that violates that provision is liable for actual damages and an additional penalty of \$5,000 per employee or prospective employee who is harmed by the violation. The bill would authorize an employee or prospective employee to bring an action for injunctive relief and for the recovery of actual damages and penalties and would provide that a prevailing employee or prospective employee is entitled to recover reasonable costs and attorney's fees.

(2) Existing law, the State Bar Act, provides for the licensure and regulation of attorneys by the State Bar of California, a public corporation. Existing law provides that it is cause for suspension, disbarment, or other discipline for any licensee, whether acting on their own behalf or on behalf of someone else, whether or not in the context of litigation, to solicit, agree, or seek agreement that, among other things, misconduct or the terms of a settlement of a claim for misconduct shall not be reported to the State Bar.

This bill would provide that it is cause for suspension, disbarment, or other discipline for any licensee to enter into with an employee or prospective employee, present an employee or prospective employee as a term of employment, or attempt to enforce any employee contract or other agreement that violates the above-described prohibition on covenants not to compete.

(3) Existing law regulates various aspects of employment, including the payment of wages to specified provisions in employment contracts. Existing law creates the Division of Labor Standards Enforcement, which is under the direction of the Labor Commissioner, and generally commits to the commissioner the authority and responsibility for the enforcement of employment laws.

Existing law prohibits an employer from requiring an employee who primarily resides and works in the state to agree, as a condition of employment, to a provision that would require the employee to adjudicate outside of the state a claim arising in the state or would deprive the employee of the substantive protection of state law with respect to a controversy arising in the state. Existing law provides that this prohibition does not apply to a contract with an employee who is in fact individually represented by legal counsel in negotiating the terms of an agreement to designate either the venue or forum in which a controversy arising from the employment contract may be adjudicated or the choice of law to be applied.

This bill would provide that, for a contract entered into, modified, or extended on or after January 1, 2024, an employee is not considered individually represented by legal counsel if the counsel is paid for by, or was selected based upon the suggestion of, the employee's employer.

This bill would prohibit an employer, as defined, from requiring an employee, as defined, to reimburse, pay, or repay, including upon termination of employment, costs for trainings, as defined, related to the employee's responsibilities and duties related to their employment.

Vote: majority Appropriation: no Fiscal Committee: yes Local Program: no

THE PEOPLE OF THE STATE OF CALIFORNIA DO ENACT AS FOLLOWS:

SECTION 1. Section 6090.5.5 is added to the Business and Professions Code, to read:

6090.5.5. (a) It is cause for suspension, disbarment, or other discipline for any licensee to enter into with an employee or prospective employee, present an employee or prospective employee as a term of employment, or attempt to enforce any employee contract or other agreement that violates Section 16608.

(b) For purposes of this section, "employee" includes, but is not limited to, a full-time or part-time employee and independent contractor.

SEC. 2. Section 16601 of the Business and Professions Code is amended to read:

16601. (a) Any person who sells the goodwill of a business, ~~or~~ any owner of a business entity selling or otherwise disposing of all of ~~his or her~~ *their* ownership interest in the business entity, or any owner of a business entity that sells (a) all or substantially all of its operating assets together with the goodwill of the business entity, (b) all or substantially all of the operating assets of a division or a subsidiary of the business entity together with the goodwill of that division or subsidiary, or (c) all of the ownership interest of any subsidiary, may agree with the buyer to refrain from carrying on a similar business within a specified geographic area in which the business so sold, or that of the business entity, division, or subsidiary has been carried on, ~~so long as~~ *if* the buyer, or any person deriving title to the goodwill or ownership interest from the buyer, carries on a like business therein.

~~For~~

(b) *For* the purposes of this section, ~~"business~~ *the following definitions apply:*

(1) *"Business* entity" means any partnership (including a limited partnership or a limited liability partnership), limited liability company (including a series of a limited liability company formed under the laws of a jurisdiction that recognizes such a series), or corporation.

For the purposes of this section, "owner

(2) "Owner of a business entity" means any partner, in the case of a business entity that is a partnership (including a limited partnership or a limited liability partnership), or any member, in the case of a business entity that is a limited liability company (including a series of a limited liability company formed under the laws of a jurisdiction that recognizes such a series), or any owner of capital stock, in the case of a business entity that is a corporation.

For the purposes of this section, "ownership

(3) "Ownership interest" means ~~a~~ any of the following:

(A) A partnership interest, in the case of a business entity that is a ~~partnership (including partnership, including a limited partnership a limited liability partnership), a partnership, that is more than a 10-percent interest of the total partnership interest of the entity.~~

(B) A membership interest, in the case of a business entity that is a limited liability ~~company (including company, including a series of a limited liability company formed under the laws of a jurisdiction that recognizes such a series), or a series, that is more than a 10-percent interest of the total membership interest of the entity.~~

(C) A capital ~~stockholder, stock,~~ in the case of a business entity that is a ~~corporation. corporation, that is more than 10-percent of the total shares of ownership of the corporation.~~

For the purposes of this section, "subsidiary"

(4) "Subsidiary" means any business entity over which the selling business entity has voting control or from which the selling business entity has a right to receive a majority share of distributions upon dissolution or other liquidation of the business entity (or has both voting control and a right to receive these distributions.)

SEC. 3. Section 16608 is added to the Business and Professions Code, immediately following Section 16607, to read:

16608. (a) An employer shall not enter into, present an employee or prospective employee as a term of employment, or attempt to enforce any covenant not to compete that is void under this chapter.

(b) (1) An employer that violates this section is liable for actual damages and an additional penalty of five thousand dollars (\$5,000) per employee or prospective employee who is harmed by the violation.

(2) An employee or prospective employee may bring an action for injunctive relief and for the recovery of actual damages and additional penalties pursuant to this section. In addition to these remedies, a prevailing employee or prospective employee in any action based on a violation of this section is entitled to recover reasonable costs and attorney's fees.

(c) For purposes of this section, the following definitions apply:

(1) "Covenant not to compete" means any provision of any contract or other agreement that restrains anyone from engaging in a lawful profession, trade, or business of any kind.

(2) "Employee" includes, but is not limited to, a full-time or part-time employee and independent contractor.

(3) "Employer" means any person or entity that employs employees.

SEC. 4. Section 925 of the Labor Code is amended to read:

925. (a) An employer shall not require an employee who primarily resides and works in California, as a condition of employment, to agree to a provision that would do either of the following:

(1) Require the employee to adjudicate outside of California a claim arising in California.

(2) Deprive the employee of the substantive protection of California law with respect to a controversy arising in California.

(b) Any provision of a contract that violates subdivision (a) is voidable by the employee, and if a provision is rendered void at the request of the employee, the matter shall be adjudicated in California and California law shall govern the dispute.

(c) In addition to injunctive relief and any other remedies available, a court may award an employee who is enforcing ~~his or her~~ *their* rights under this section reasonable attorney's fees.

(d) For purposes of this section, ~~adjudication~~ *"adjudication"* includes litigation and arbitration.

(e) *(1) This section shall not apply to a contract with an employee who is in fact individually represented by legal counsel in negotiating the terms of an agreement to designate either the venue or forum in which a controversy arising from the employment contract may be adjudicated or the choice of law to be applied. For purposes of this subdivision, an employee is not considered individually represented by legal counsel if the counsel is paid for by, or was selected based upon the suggestion of, the employee's employer.*

(2) The amendments made by the act adding this paragraph shall apply to a contract entered into, modified, or extended on or after January 1, 2024.

(f) This section shall apply to a contract entered into, modified, or extended on or after January 1, 2017.

SEC. 5. Chapter 4.1 (commencing with Section 1058) is added to Part 3 of Division 2 of the Labor Code, to read:

CHAPTER 4.1. Training Costs and Debt

1058. (a) An employer shall not require an employee to reimburse, pay, or repay, including upon termination of employment, costs for any training related to the employee's responsibilities and duties related to their employment.

(b) For purposes of this section, the following definitions apply:

(1) "Employee" includes, but is not limited to, a full-time or part-time employee and independent contractor.

(2) "Employer" means any person or entity that employs employees.

(3) (A) "Training" means any instruction or course the employer requires the employee to complete as a prerequisite to the employee fulfilling their responsibilities and duties related to their employment.

(B) "Training" does not mean or include any required training to obtain or maintain necessary professional licenses and excludes required coursework, apprenticeship programs, work experience education programs, or other similar coursework and programs required before employment of the employee.