THE COMPETITIVE WORLD OF NON-COMPETES

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I. INTRODUCTION

"Litigation over agreements not to compete after the termination of employment has long been a staple of business litigation"[1] The same remains true regarding alleged misappropriations of trade secrets. Whether one represents employers or employees, understanding the ever-shifting ground upon which these cases are fought is essential.

In addition to the evolving legal rules, competent counsel should also discuss with their clients the legitimate business justification for their proposed noncompetition agreements and the wisdom of limiting their scope to only that necessary to protect such legitimate interests. For example, the Jimmy John's sandwich chain has recently received much adverse publicity for imposing noncompetition agreements on their $9/hour sandwich makers. It boggles the imagination why someone thought that was a good idea, or likely to be enforceable. Moreover, as first reported in the *Huffington Post*, Congressional Democrats are requesting the Federal Trade Commission and the Department of Labor to investigate this practice.

This article will begin by discussing the current status of the law of noncompetition agreements.[2] It will then address the related issues concerning nondisclosure and nonsolicitation agreements and trade secrets disputes. Finally, the article will discuss what has been called the doctrine of inevitable or probable disclosure. The latter is a concept by which some litigants have sought, with some success, to obtain results similar to those achieved through more traditional restrictive agreement and trade secret misappropriation claims, without necessarily meeting the demanding elements of the latter claims.

II. OVERVIEW OF TEXAS NONCOMPETITION AGREEMENT DEVELOPMENTS

Texas law pertaining to noncompetition agreements has been circuitous at best. One commentator earlier identified three distinct phases in the history of noncompetition agreements in Texas.[3] The first phase was typified by a flexible "rule of reason" analysis enunciated in cases such as *Weatherford Oil Tool Co. v. Campbell.*[4] In that phase, Texas courts recognized that noncompetition agreements were restraints of trade, but that they may nevertheless be enforced if they were sufficiently reasonable with respect to the interests to be protected and the scope of the time, geography, and activity restricted.[5]

The second phase lasted between 1987-89. During this brief phase, the Texas Supreme Court drastically cut back on the enforcement of noncompetition agreements. In cases such as *Hill v. Mobile Auto*

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[1] Michael Quinn & Andrea Levin, *Post Employment Agreements Not to Compete: a Texas Odyssey*, 33 Tex. J. of Bus. L. 7, 9 (Spring 1996) *(hereinafter "Texas Odyssey").*

[2] For uniformity, this article will generally refer to covenants not to compete or noncompetition agreements simply as "noncompetition agreements."

[3] *Id.* at 15.

[4] 340 S.W.2d 950 (Tex. 1960).

[5] This analysis was supported in a seminal law review, Harlan M. Blake, *Employee Agreements Not to Compete*, 73 Harv. L. Rev. 625 (1960), which has been cited in over 100 opinions around the country. *See Texas Odyssey*, 33 Tex. J. of Bus. L. at 17 n.20.

Trim,[6] the Supreme Court generally prohibited the enforcement of noncompetition agreements in employment cases involving a "common calling." This tended to eviscerate noncompetition agreements in most employment settings.

The third phase resulted from the Texas Legislature's rejection of the Supreme Court's growing hostility to noncompetition agreements. In 1989 and, more forcefully again in 1993, the Texas Legislature adopted and amended the Covenant Not to Compete Act (the “Act”).[7]This Act was intended to sweep aside many of the judicially-imposed obstacles that had previously barred the enforcement of noncompetition agreements. The legislature's efforts in this regard were dramatically affected, if not supplanted by the Texas Supreme Court decision in *Light v. Centel Cellular Co.*[8] Much of the third phase was devoted to efforts to interpret and apply the *Light* decision, especially with respect to the type of contract language and consideration necessary to support a noncompetition agreement.

2006 witnessed the beginning of a sea change in the Texas Supreme Court's interpretation of noncompetition agreements under the Act. At that time, the Court issued its long awaited decision in *Alex Sheshunoff Management Services, L.P. v. Johnson.*[9] *Sheshunoff* could be construed as the Court’s final capitulation to the legislative mandate for courts to more vigorously enforce noncompetition agreements. In any event, *Sheshunoff* dramatically altered the analysis set forth in *Light* by dispensing with some of the technical requirements created by *Light.*

Subsequently, the Court continued and expanded the changes initiated by *Sheshunoff* in *Mann Frankfort Stein & Lipp Advisors, Inc. v. Fielding,*[10] and *Marsh USA Inc. v. Cook.*[11] Most recently, the Court issued its decision in *Exxon Mobile Corp. v. Drennen*,[12] which further limits the scope of the Covenant Not to Compete Act.

III. COVENANT NOT TO COMPETE ACT

Since noncompetition agreements are now governed by the Covenant Not to Compete Act, the starting point for any discussion of such agreements must be the Act itself. As currently written, Section 15.50 states, in relevant part, as follows:

> . . . [A] covenant not to compete is enforceable if it **is ancillary to or part of an otherwise enforceable agreement at the time the agreement is made** to the extent that it contains **limitations as to time, geographical area, and scope of activity** to be restrained **that are reasonable** and do not impose a greater restraint than is **necessary to protect the goodwill or other business interest** of the promisee.[13]

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[6] 72 S.W.2d 168 (Tex. 1987).

[7] Tex. Bus. & Com. Code Ann. § 15.50 – 52.

[8] 883 S.W.2d 642 (Tex. 1994).

[9] 209 S.W.3d 644 (Tex. 2006).

[10] 289 S.W.3d 844 (Tex. 2009),

[11] 354 S.W.3d 764 (Tex. 2011).

[12] No. 12-0621 (August 29, 2014).

[13] Tex. Bus. & Com. Code § 15.50 (emphasis added).

Section 15.51 sets forth the procedures and remedies relating to alleged violations of noncompetition agreements.[14] One of Section 15.51's key provisions is as follows:

> If the covenant is found to be ancillary to or part of an otherwise enforceable agreement but contains limitations as to time, geographical area, or scope of activity to be restrained that are not reasonable and impose a greater restraint than is necessary to protect the goodwill or other business interest of the promisee, **the court shall reform the covenant to the extent necessary to cause the limitations contained in the covenant as to time, geographical area, and scope of activity to be restrained to be reasonable and to impose a restraint that is not greater than necessary to protect the goodwill or other business interest** of the promisee and enforce the covenant as reformed, except that **the court may not award the promisee damages for a breach of the covenant before its reformation** and the relief granted to the promisee shall be limited to injunctive relief. **If** the primary purpose of the agreement to which the covenant is ancillary is to obligate the promisor to render personal services, the promisor establishes that **the promisee knew at the time of the execution of the agreement that the covenant did not contain limitations as to time, geographical area, and scope of activity to be restrained that were reasonable** and the limitations imposed a greater restraint than necessary to protect the goodwill or other business interest of the promisee, and the promisee sought to enforce the covenant to a greater extent than was necessary to protect the goodwill or other business interest of the promisee, **the court may award the promisor the costs, including reasonable attorney's fees, actually and reasonably incurred** by the promisor in defending the action to enforce the covenant.[15]

Finally, Section 15.52, states that Sections 15.50 and 15.51 preempt any other common law rules relating to criteria for enforcement, procedures, or remedies for violations of noncompetition agreements.[16]

IV. THE *LIGHT* ERA

A. The *Light* Decision

The Texas Supreme Court squarely addressed the Covenant Not to Compete Act for the first time in *Light v. Centel Cellular Co. of Texas.*[17] In *Light*, the Court explicitly recognized the broad preemptive effect of that Act. The Court then addressed the application of the Act in the at-will employment context.

First, the Court affirmed that at-will employment alone will not support a noncompetition agreement. Nor will any consideration that is dependent upon the continuation of at-will employment. The Court, however, further held that at-will employment did not *necessarily* defeat a noncompetition agreement. Instead, even in the at- will employment context, a noncompetition agreement may be enforceable if it is supported by sufficient consideration that is independent of continued employment.[18]

Drawing directly on the language of Section 15.50, the Court set forth two requirements for the

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[14] *Id.* at § 15.51.

[15] *Id.* at § 15.51(c) (emphasis added).

[16] *Id.* at § 15.52.

[17] 883 S.W.2d 642 (Tex. 1994).

[18] *Id.* at 644-45.

enforcement of a noncompetition provision:

(1) The provision must be "ancillary to or part of an otherwise enforceable agreement at the time the agreement is made;" and

(2) The provision must "contain limitations as to time, geographical area, and scope of activity to be restrained that are reasonable and do not impose a greater restraint than is necessary to protect the goodwill or other business interest of the promisee."[19]

Whether these standards are met is a question of law for the court.[20]

Having studiously tracked the specific language of the Act to this point, the Supreme Court then added a gloss to the first requirement above. To meet the "ancillary" standard, the following two additional factors must be satisfied:

(1) [T]he consideration given by the employer in the otherwise enforceable agreement must give rise to the employer's interest in restraining the employee from competing; and

(2) [T]he covenant must be designed to enforce the employee's consideration or return promise in the otherwise enforceable agreement.[21]

To illustrate the foregoing, the Supreme Court, in dicta, discussed two hypothetical situations. In the first situation, an employee enters an agreement to maintain the confidentiality of any confidential information the employee may subsequently receive in the course of employment. Although the court recognized that a binding unilateral contract could be formed by the employer's subsequent provision of confidential information to the employee, the Court held such subsequent transfer of information could not sustain a noncompetition provision [had one been placed in the original agreement] because there was no *binding* commitment on the part of the employer to provide confidential information to the employee at the time the noncompetition provision would have been adopted.[22]

In the second situation, the employer actually does give an employee confidential information in exchange for the employees agreement not to disclose the information and not to compete. In that case, the Court opined that the noncompete would be enforceable.[23]

Between 1994 and 2006, there was an abundance of litigation as to exactly how to apply the Act to noncompetition agreements in the wake of *Light.* Much, but not all, of that precedent has been overtaken by subsequent Texas Supreme Court decisions.

V. ***SHESHUNOFF* AND ITS PROGENY**

A **The *Sheshunoff* Decision**

The Texas Supreme Court revisited *Light* and the Covenants Not to Compete Act for the first

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19 *Id.* at 644.

20 *Id.*

21 *Id.* at 647.
22 *Id.* at 645 n.6.

23 *Id.* at 647 n.14.

time since *Light* in *Alex Sheshunoff Management Services, L.P. v. Johnson.*[24] In that case, the employee executed an employment agreement with a noncompetition provision shortly after receiving a promotion to a senior management position. The agreement provided for the employee to receive training and further access to confidential information. It also provided the employee with the right to at least two weeks advance notice of termination. In exchange, the agreement included a covenant for the employee not (a) to provide consulting services to the employer's clients for whom the employee had provided more than 40 hours of service within his last year of employment, or (b) to solicit the employer's customers or specifically identified potential customers, for a period of one year after his termination.

The Austin Court of Appeals found that a promise of future access to confidential information constituted illusory consideration insufficient to support the covenant. In addition, the court held that the two weeks' notice of termination was not sufficiently ancillary to support the covenant. Following the then majority rule, the Austin Court of Appeals found the noncompetition agreement unenforceable due to the lack of a promise to exchange confidential information contemporaneously with the execution of the agreement.[25] The Supreme Court accepted a petition to review this case and, for the first time, revisit *Light.* The court finally issued its decision on October 20, 2006.

In *Sheshunoff,* the Supreme Court majority purported not to modify the "holding" in *Light.*[23] Nevertheless, the Court clearly modified the *Light* analysis to a significant degree. The majority opinion first reaffirms *Light's* test regarding whether a noncompetition provision is "ancillary to or part of an otherwise enforceable agreement (the "ancillary" test). Thus, as stated in the last part of *Light*, for a noncompetition provision to be enforceable, it must at a minimum meet the following two conditions: "(1) the consideration given by the employer in the otherwise enforceable agreement must give rise to the employer's interest in restraining the employee from competing; and (2) the covenant must be designed to enforce the employee's consideration or return promise in the otherwise enforceable agreement."[26]

The Court then addressed the requirement of an "otherwise enforceable agreement." It was this requirement that had so deeply divided the lower courts and confused practitioners after *Light*. The Court rejected *Light* to the extent it could be read to require the simultaneous exchange of confidential information or the creation of a mutually binding bilateral contract at the time the noncompetition agreement was executed. The Court acknowledged that it was departing from *Light* with respect to the timing of the exchange of confidential information for a noncompetition restriction. Asserting that Section 15.50's requirement that a noncompetition agreement be "ancillary to or part of an otherwise enforceable agreement at the time the agreement is made" is ambiguous, the Court concluded that the term "at the time the agreement is made" modifies "ancillary to or part of rather than "an otherwise enforceable agreement." The clarification of the "ambiguity" was purportedly based on a review of the legislative and judicial history leading up to the Covenant Not to Compete Act.[27] Based on this reinterpretation of the Act, the Court found that there is no requirement that the employer provide a binding promise or consideration at the same time as the agreement is entered into. Instead, it is sufficient if the employer provide such consideration

[24] 209 S.W.3d 644 (Tex. 2006).

[25] 123 S.W.3d 678 (Tex. App. — Austin 2003), *rev'd* 209 S.W.3d 644 (Tex. 2006).
[26] 209 S.W.3d at 649.

[27] 209 S.W.3d *at* 650-55.

pursuant to a conditional or illusory initial promise at some point after the agreement was formed. In the Court's analysis, the *employee's* binding promise not to disclose confidential information and not to compete constitutes an offer to enter into a unilateral contract that is accepted when the employer fulfills a reciprocal, but nonbinding, promise to provide confidential information or similar consideration. In reaching this result, the Court rejected the "dicta" set forth in the famous footnote 6 of *Light.*[28] Thus, an agreement in which an employer promises to provide an employee with access to confidential information and/or training in the course of at-will employment may, if fulfilled, constitute sufficient consideration to support the employee's reciprocal nondisclosure and noncompetition commitments.

In justifying its conclusion, the majority stressed that the *Light* line of cases had diverted the courts from the most important issue, i.e. whether the noncompetition provision was reasonable in terms of duration, geographic area, scope of activities, and underlying business interest. Based on this observation, Texas courts are supposed to have a renewed focus on these scope/business justification considerations.

Finally, the Court affirmed the denial of a temporary injunction on the grounds that it was moot. Since the one-year noncompetition period had already passed, the Court remanded solely on the issue of damages.

Justice Jefferson, joined by two colleagues, filed a concurring opinion arguing for a limitation on the majority holding. Justice Jefferson felt that the majority opinion left too much room for manipulation, e.g. by an employer who had no intent to provide confidential information to the employee at the outset and only does so on the eve of an employee's termination to trigger enforceability of the noncompetition agreement. Justice Jefferson would require that the employer's consideration, e.g. the delivery of confidential information, should begin to occur at or relatively soon after the original agreement is executed.

Justice Jefferson's concurring opinion also sheds light on the issue of at least his own views of the type of confidential information that can support a noncompetition provision executed after an employee has already started working for an employer. Justice Jefferson noted that the defendant/employee had received much of the same <u>kind</u> of confidential information both before and after the noncompetition agreement was executed. The fact that he <u>continued</u> to receive such information after the execution date appeared to have been viewed as sufficient to satisfy the "new consideration" requirement.

Finally, Justice Wainwright delivered his own concurrence that questioned the majority's reinforcement of *Light's* two-part test for whether the noncompete is part of or ancillary to the enforceable agreement. As Justice Wainwright notes, there is no support in the language of the statute for this two part test.

B. The *Mann Frankfort Decision*

In *Mann Frankfort Stein & Lipp Advisors, Inc. v. Fielding,*[29] the noncompetition agreement in question failed to *explicitly* promise that the employer would provide confidential information to the employee in exchange for a noncompetition agreement. The Texas Supreme Court, however, found that it was *implicit* in the agreement that both parties contemplated the transmission of confidential information due to the very nature of the accounting position at issue. That plus the

[28] 209 S.W.3d at 655-56.
[29] 289 S.W.3d 844 (Tex. 2009),

employee's reciprocal express promise to keep such information confidential was deemed sufficient to support the agreement that the employee would not provide accounting services to the employer's customers for one year post employment without paying a substantial price to "purchase" such customer accounts.

C. The Marsh Decision

In *Marsh USA Inc. v. Cook*, 354 S.W.3d 764 (Tex. 2011), the manager of Marsh & McClennan Companies Dallas office entered into a *stock option* agreement that included a provision that the manager would not solicit or do business with Marsh customers whom he had serviced or for which he had supervised the provision of service for two years after the termination of employment. The agreement also included an employee nonsolicitation provision.

Consistent with his concurrence in *Sheshumoff*, Justice Wainwright substantially modified, if not virtually abandoned, *Light* altogether and affirmed the noncompete on pure contract principals. In doing so, Justice Wainwright stated, in passing, that an *employee nonsolicitation* and a *customer nonsolicitation* agreement should be judged by the same standards.

First, a court must determine whether the noncompete is part of an "otherwise enforceable agreement." Here, the stock option agreement easily met that test. The *Marsh* opinion, however, said that there is no requirement that the "consideration for the otherwise enforceable agreement gives rise to the interest in restraining the employee from competing."[30]

Second, a court must determine whether the noncompete is "ancillary to or part of" the otherwise enforceable agreement.[31] Following the lead of the *Sheshumoff* and *Mann Frankford* decisions, the court substantially relaxed the requirements of this test. All a party seeking to enforce must show is that the noncompete is not a naked restraint of trade and that there is a "nexus" between the otherwise valid transaction and an "interest worth of protection." **"Consideration for a noncompete that is reasonably related to an interest worth of protection, such as trade secrets, confidential information or goodwill satisfies the statutory nexus; and there is no textual basis for excluding the protection of good will from the business interests that a noncompete may protect."[32]**. Here, Marsh's sharing of the business' "good will" was deemed sufficient.

[30] 354 S.W.3d at 773.

[31] *Cf.* Tex. Bus. & Comm. Code § 15.50.

[32] *354 S. W.3d at773*

VI. EXXON MOBILE CORP. v. DRENNEN

The Texas Supreme Court's most recent decision relating to noncompetition agreements is *Exxon Mobil Corporation v. Drennen.*[33] In *Drennen*, a high level executive of Exxon Mobil participated in an executive incentive pay program under which he was eligible for restricted stock that would vest over a 7 year period. The agreement included a provision that unvested stock would be forfeited if the executive engaged in "detrimental activity" before vesting. The defendant resigned under the pretense that he was retiring. He, however, took a job with a competitor thereafter and Exxon Mobil declared his unvested stock forfeited.

In addition to the detrimental activity/forfeiture provision, the incentive agreement had a New York choice of law provision. In *DeSantis v. Wackenhut Corp.*, the Texas Supreme Court had previously held that Texas courts would not honor a choice of law for a foreign jurisdiction in noncompetition agreements.[34] The Supreme Court first analyzed whether, under *DeSantis*, the New York choice of law provision should be followed. The Court determined that it should.

In reaching this choice of law determination, the Court first analyzed whether the incentive agreement was a noncompetition agreement governed by *DeSantis*. The Court recognized, that in *Marsh*, the Court had applied the Covenant Not to Compete Act provisions to a stock option agreement that included a forfeiture of stock options in the event an employee subsequently solicited the first employer's customers or employees. The Court, however, concluded that this executive incentive agreement was somehow different. The Court held the stock option provisions in *Marsh* were designed to protect the first employer's investment in good will. The award of stock options was designed to incentivize the employee to build up that good will to enhance the value of the stock.

In contrast, the Court found that the restricted stock plan in *Drennen* was not designed to enhance the employer's investment in good will. Instead, the Court said the incentive plan was designed to reward "continued employment and loyalty." This supposedly made all the difference.

The *Drennen* decision, written by Justice Green without dissent, is somewhat puzzling. There does not seem to be a clear dividing line between the stock-related incentive programs in *Marsh* and in *Drennen*. Both involved the loss of valuable stock rights for, among other things, joining a competitor or soliciting customers. The Court, however, did note that the defendant in *Drennen* did not directly contribute to the incentive plan. In contrast, since *Marsh* involved stock options, the employee at least had to pay the initial strike price of the stock and would be rewarded only to the extent the stock increased in value, thereby directly tying the employee's interest to the success of the company.

Finally, the *Drennen* decision left some major questions unanswered. First, the Court stated that it was not setting forth a test to determine what makes an agreement a "noncompetition" agreement governed by the Act. The Court, however, did say that "forfeiture clauses in non-contributory profit-sharing plans . . . clearly are not covenants not to compete" sufficient to trigger *DeSantis* choice of law restrictions. In reaching this conclusion, the Court seemed to call into *DeSantis* itself, at least in the case of multistate corporation. *Drennen* indicated that times have changed since the former decision and that Texas may have a greater public policy interest in protecting the interests of Texas-based multistate corporations seeking uniformity in the interpretation of its agreements.

Second, the Court stated that, since it purportedly was merely applying New York law, it was not deciding whether a forfeiture clause such as this would be void as an unreasonable restraint of trade under Texas law.

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[33] No. 12-0621 (August 29, 2014).

[34] 793 S.W.2d 670 (Tex. 1990)

VII. NONCOMPETITION AGREEMENT ISSUES

As set forth in the Act, in addition to be ancillary to or part of an otherwise enforceable agreement that justifies a restriction on competition, a noncompetition agreement must also be reasonable with respect to time, geography, and scope. In addition, a number of related issues have arisen. Some of these key issues will be discussed in this section.

A. Duration

Neither *Sheshunoff,* nor *Light* substantially altered the law with respect to the requirement that a noncompetition agreement contain reasonable time limits. In *John R. Ray*, for example, the court struck down a noncompetition provision that had no time limit. The court refused to reform the agreement because the plaintiff had made no showing as to what lesser time limit would be reasonable.[35]

In *Gallagher Healthcare Insurance Services v. Vogelsang,*[36] the court upheld a noncompetition agreement for two years post-employment.

In *Stone*, the agreement imposed a five-year post-employment noncompetition requirement. Noting that courts had previously upheld restrictions of between two and five years, the court found a five year restriction not to be unreasonable.[37]

In the sale of a business context, courts have upheld even longer noncompetition periods. For example, in *Heritage Operating, L.P. v. Rhine Bros., LLC*, the Fort Worth Court of Appeals upheld a 10 year post-sale noncompete for a former owner of the business sold. In doing so, the court reversed the trial court that had reformed the agreement to last only 5 years.[38]

B. Geographic Area

Courts also require that the geographic area of a post-employment noncompetition agreement be reasonable. Once again, the total failure to provide limit the geographic scope of an agreement is typically fatal.[39]

A number of cases have recognized that the geographic territory in which an employee worked for the former employer is presumed to be reasonable.[40]

In a recent case, *Daily Instruments Corp. v. Heidt*, a federal judge upheld a worldwide

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[35] 923 S.W.2d at 85-85.

[36] 312 S.W.3d 640, 655 (Tex. App. – Houston [1st Dist.] 2009) .

[37] 53 S.W.3d at 696.

[38] 2012 Tex. App. LEXIS 4939, No. 02-10-00474-CV (Tex. App. – Fort Worth, 2012, no pet.).

[39] *Zep Manufacturing Co. v. Harthcock*, 824 S.W.2d 654 (Tex. App. -- Dallas 1992, no writ).

[40] *Stone*, 53 S.W.3d at 695; *Evans World Travel, Inc. v. Adams*, 978 S.W.2d 225, 232-33 (Tex. App. -- Tyler 2001, no pet h.).

noncompetition provision for a former high level employee who had an assigned sales territory covering much of the world, and had been engaged in work in areas outside his assigned sales territory.[41] This decision may have been influenced by the court's multiple findings of fact demonstrating a pervasive theft of confidential information and discovery abuse, as well as the very narrow scope of the industry at issue.

In the context of a customer nonsolicitation provision, courts have held that no geographic restriction is necessary in light of the restriction to specific customers, which serves as an alternative limitation.[42]

If requested and supported by appropriate evidence, courts may reform an overbroad geographic restriction and enforce as reformed.[43] For example, in *Republic Services, Inc. v. Rodriquez*, the Houston Court of Appeals reversed the trial court's decision to grant summary judgment rejecting a potentially geographically overbroad noncompetition agreement and remanded with instructions to reform the agreement to a reasonable geographic area.[44]

C. <u>Attorneys' Fees</u>

In *Butler v. Arrow Mirror & Glass, Inc.*, the court awarded the plaintiff attorney's fees, even though the overbroad geographic scope of the noncompetition agreement had been reformed.[45] In contrast, in *Perez v. Texas Disposal Systems, Inc.*, the court held that attorneys' fees may not be awarded if the covenant had to be reformed.[46]

In *Contemporary Contractors,*[47] an employer sued a former employee for breach of a noncompetition agreement contained in a confidentiality agreement. The employee counter-claimed with a request for a declaratory judgment as to *all* of his obligations under the confidentiality agreement. The employer then nonsuited its claim. Nevertheless, the trial court entered judgment declaring the noncompetition agreement invalid for lack of consideration and awarded attorney's fees. The court of appeals rejected the employer's contention that the declaratory judgment action was merely a restated defense because the employee had not only asked for a declaration that the noncompete was void, but also asked for clarification of his confidentiality obligations. This was beyond the scope of the original claim and, therefore, entitled him to fees under the Declaratory Judgment Act. In addition, the court held that the attorneys' fees provisions in 15.51 of the Covenant Not to Compete Act do not preempt the attorneys' fees provisions of the Declaratory Judgment Act.

As noted above, in *Hardy*, the court of appeals similarly held that Section 15.51 did not

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[41] 998 F. Supp.2d 553 (S.D. Tex. 2014).

[42] *Investors Diversified Services v. McElroy*, 645 S.W.2d 338, 339 (Tex. – Corpus Christi 1982, no writ); *Gallagher*, 312 S.W.3d at 654.

[43] *Butler v. Arrow Mirror & Glass, Inc.*, 51 S.W.3d 787 (Tex. App. -- Houston [1st Dist.] 2001).

[44] No. 14-12-01054-CV (June 26, 2014).

[45] *Id.*, 51 S.W.3d at 796-97.

[46] No. 04-00-00676-CV (Tex. App. -- San Antonio 2003).

[47] 2005 WL 1774983 (Tex. App. – Dallas 2005).

preempt a former employee's attorneys' fees claim based on an attorney's fee award provision in the underlying noncompetition agreement. In that case, the employee had initiated the lawsuit to seek a declaration that the noncompetition agreement was unenforceable. The employer had responded with a counter-claim to enforce the agreement. The court reasoned that a challenge to a noncompetition agreement does not constitute an action to "enforce" the agreement and therefore is not preempted.

In *Sentinel Integrity Solutions, Inc. v. Mistas Group, Inc.,*[48] the Houston Court of Appeals affirmed the award of attorneys' fees to a defendant who had shown that a covenant was overbroad. Significantly, the court relied in part on the fact that the noncompetition agreement specifically prescribed that the agreements should be reformed if a court found it to be overbroad. The court found this to be evidence of the employer's bad faith in drafting an overbroad covenant!

In *Franlink v. GJMS Unlimited, Inc*,[49] the court held that under Sections 15.51 and 15.52 of the Covenant Not to Compete Act[50] preempted the award of attorneys' fees to a prevailing plaintiff that successfully enforced a noncompetition agreement and sought statutory attorneys' under Texas Civil Practice and Remedies Code § 38.001(8)(authorizing attorneys' fees and costs for breach of contract claims). That case cited as precedent *Glattly v. Air Starter Components, Inc.,*[51] which found that Sections 15.51 and 15.52 preempted a plaintiff's attorneys' fee claim under a contractual provision that specified the award of attorneys' fees for breach of contract. Both of these have broad language suggesting the party seeking to enforce a noncompetition agreement can never be awarded attorneys' fees. In both cases, however, the courts had reformed the underlying noncompetition agreement, which is expressly governed by Section 15.51. Questions remain whether a prevailing plaintiff can obtain attorneys' fees if the noncompetition agreement is sustained and enforced in full.

D. <u>Choice of Law</u>

Prior to *Drennen,* Texas courts consistently follow the conflict of laws principles with respect to noncompetition agreements set forth in *DeSantis v. Wackenhut.*[52] For example, in *Medtronics*, the court applied Texas law to a noncompetition agreement even in the face of a Minnesota choice of law provision.[53] More recently, in *Rimkus Consulting Group, Inc. v. Cammarata,*[54] a federal district court relied on a Texas choice of law provision to defeat a Louisiana employee's claim that a noncompetition agreement enforcement action against him should be dismissed or transferred to Louisiana, which bars noncompetition agreements.

Cardoni v. Prosperity Bank, 805 F.ed 573 (5th Cir. 2015), represents a mirror image of *DeSantis*. In *Cardoni*, a Texas bank, acquired an Oklahoma bank and imposed

[48] 414 S.W.3d 911 (Tex. App. – Houston [1st Dist.] 2013).

[49] 401 S.W.3d 705 (Tex. App. – Houston [14th Dist.] 2013, no pet.).

[50] Tex. Bus. & Com. Code §§ 15.51 and 15.52.

[51] 332 S.W.3d 620 (Tex. App. – Houston [1st Dist.] 2010, pet. denied).

[52] 793 S.W.2d 670 (Tex. 1990) (applying Texas law despite a foreign state choice of law designation in the agreement).

[53] 97 S.W.3d at 838.

[54] 2007 WL 1520993 (S.D. Tex., May 22, 2007).

noncompete/nonsolicitation agreements on the upper level managers of the Oklahoma bank as a condition of the acquisition. The agreements included a Texas choice of law provision. Some of the Oklahoma managers quickly grew disillusioned with the merger, resigned, and joined a competitor bank in Tulsa. Lawsuits were initially filed in both Texas and Oklahoma, but ultimately were consolidated in the Southern District of Texas. The District Court struck down the restrictive covenants under Oklahoma law.

The appellate opinion written by Fifth Circuit Judge Gregg Costa begins as follows:

> In addition to their well known disagreements over boundaries [footnote 1] and football [footnote 2]. Texas and Oklahoma do not see eye to eye on a less prominent issue: covenants not to compete. Texas generally allws them so long as they are limited both geographically and temporally. *Tex. Bus. & Com. Code Ann. § 15.50(a).* Oklahoma generally does not. *Okla. Stat. tit. 15, § 217*. These different policy choices – Texas's view which prioritizes parties' freedom to contract and Oklahoma's which emplhasizes the right to earn a living and competition – came to a head when Texas-based Prosperity Bank acquired Oklahoma-based F&M Bank and Trust Company.[55]

Footnote 1 of the opinion cites the history of boundary line disputes along the Red River, including a 1931 incident when the Governor of Oklahoma declared marshall law and dispatched the Oklahoma National Guard to occupy both sides of the Red River at a disputed bridge.[56] Footnote 2 of the opinion includes the following statement: "**The authoring judge cannot help but note that the University of Texas leads the University of Oklahoma 61-44-5 in the Red River Rivalry.**[57]

Applying the same conflict of laws principles as *DeSantis, i.e.* Restatement (2d) of Conflict of Laws § 187(2), the Fifth Circuit held that Oklahoma's public interest in protecting its own residents right to work was paramount over Texas's interest in protecting a Texas company's contractual arrangements. The Fifth Circuit acknowledged *Drennen*'s emphasis on Texas interest in protecting nationwide companies with Texas' headquarters, but noted that *Drennen* purportedly did not involve a noncompetition agreement. Therefore, *DeSantis*, rather than *Drennan* controlled. And just as *DeSantis* disregarded a foreign choice of law provision in a noncompetition agreement with a Texas resident, *Cardoni* disregarded a Texas choice of law provision in a noncompetition agreement with an Oklahoma resident. The Fifth Circuit found that Oklahoma law applied and that the noncompetition provisions were invalid under the laws of that State.

Similar reasoning prevailed in *ADP, LLC v. Capote*.[58] In ADP, a New Jersey-based company and its Austin-based employee entered into a stock awards agreement with noncompetition provisions in it. The agreement had a New Jersey choice of law provision. The employee resigned and joined a competitor in Austin. A dispute arose over whether Texas or New Jersey law governed the noncompetition provisions at issue. Following <u>DeSantis and Cardoni, t</u>he District Court held that Texas law governed these provisions.

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[55] 805 F.3d at 576.

[56] *Id.* at 576 n.1.

[57] *Id.* at 576 n.2.

[58] No. A-15-CA-714-SS, 2016 U.S. Dist. Lexis 88222 (W.D. Tex. July 7, 2016).

One final note regarding *Cardoni* and *ADP*, although the courts disregarded the choice of law provisions regarding the noncompetition provisions, the courts held that the choice of law provisions were valid with respect to all other provisions/issues. Thus, disputes over whether the employee's breached a nondisclosure provision, or a variety of tort and statutory claims, were to be governed by the law of the chosen state.

Parker, et al. v. Schlumberger Technology Corp.[59] falls somewhere in between *Cardoni* and *ADP*. In this case, a Texas based business acquired an Oklahoma based oil field service company and retained the services of the former owner and a high level employee of the Oklahoma company. The purchase and related agreements included noncompetition/nonsolicitation and Texas choice of law provisions. When these employees resigned and started a competing business, the Texas company sued in Texas state court. The Texas courts followed the choice of law provision and applied Texas law. In doing so, the Houston Court of Appeals emphasized that the employees, although officed in Oklahoma, performed services in a number of states, including Texas. Also, many of the alleged improper customer solicitations were made to Texas customers.[60]

In *Merritt, Hakins & Associates, LLC v. Caporicci, et al.*[61] a Texas court of appeals reached a result similar to *Cardoni*. Merritt, Hakins & Associates is a California limited liability company with headquarters in Irving, Texas. It hired an employee in Irvine California under an employment agreement with noncompetition and Texas choice of law provisions. Like Oklahoma, California has a strong public policy precluding noncompetition agreements in most ordinary employment relations. As in *Cardoni*, the Dallas court of appeals found that under Restatement (2d) of Choice of Laws § 187(2), California had a paramount public policy compelling the court to disregard the Texas choice of law provision. Applying California law, the court found the noncompetition provisions invalid.

Finally, courts in other states are much less likely to be protective of the Texas public policy concerns underlying *DeSantis.* In *Intermetro Industries Corp. v Kent*,[62] for example, a Pennsylvania corporation brought an enforcement action against a Texas resident/former employee. The employee argued that Texas law should apply in light of *DeSantis.* The federal court disagreed. Relying in part on the new *Sheshunoff* decision, the court concluded that Texas law was no longer so distinct from the law of other jurisdictions like Pennsylvania to justify choice of foreign law.

In *Ally Financial, Inc. v. Gutierrez*,[63] a Michigan based plaintiff included a choice of law provision mandating the application of Michigan law in a phantom stock incentive award agreement. The Fort Worth Court of Appeals found the plaintiff failed to prove that Michigan law was substantially different from Texas law. The court, therefore, refused to honor the Michigan choice of law provision.

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[59] 475 S.W.3d 914 (Tex. App. – Houston [1st Dist.] 2015).

[60] The Court of Appeals, however, ultimately found that the temporary injunction issued by the trial court was overbroad and unenforceable. Specifically, the trial court made no findings as to the plaintiff's business justifications for the noncompetition/nonsolicitation provisions and did not include a time limitation in the injunction.

[61] No. 05-15-00851-CV, 2016 Tex. App. LEXIS 4582 (Tex. App. – Dallas, May 2, 2016).

[62] 2007 WL 518345 (M.D. Pa., Feb. 12, 2007).

[63] No. 02-13-00108-CV (Tex. App. – Fort Worth, January 23, 2014).

E. <u>Forum Selection/Venue</u>

One area of development involves the application of forum selection and venue provisions in the noncompetition context. With respect to forum selection, the issue is the enforceability of such clauses. With respect to venue, issues include application of traditional *forum non conveniens* and venue provisions in this context.

The cases have addressed forum selection clauses with varied results. *In re Tyco Electronics Power Systems, Inc.*,[64] was a case in which an employee sued a former employer to obtain a declaratory judgment invalidating a noncompetition agreement. The defendant responded by asserting that the matter had to be litigated in Pennsylvania pursuant to a forum selection clause in the agreement. The Dallas Court of Appeals agreed. Noting recent Texas Supreme Court decisions, such as *in re AIU Ins. Co.*,[65] that have been more receptive to forum selection clauses, the court held there was no public policy reason why the case should not be transferred to Pennsylvania.

In contrast, in *Autonation, Inc. v. Hatfield*,[66] the Houston Court of Appeals did find a public policy reason to disallow a forum selection clause. Once again, a former employee filed a declaratory judgment action to negate a noncompetition agreement. The defendant sought to enforce a forum selection clause designating Florida as the proper forum. This time, the Court of Appeals refused to enforce the forum selection clause. The court relied on an earlier case brought by the same employer in Florida to enforce a covenant not to compete against a Texas resident. Despite Texas' strong public policy restricting the enforceability of noncompetition agreements, the Florida court decided to follow Florida's more lenient law and enforced the covenant. Faced with this affront to Texas' pride, the Houston Court of Appeals held that this established that a transfer of the case to Florida would defeat Texas public policy.

The Texas Supreme Court reversed the Court of Appeals' *Autonation* decision. Distinguishing the public policy arguments in *DeSantis*, the Court held that forum selection clauses are presumably enforceable under its recent line of cases. In addition, the Court found that the changes caused by the Covenant Not to Compete Act and *Sheshunoff*, narrowed the potential public policy differences between Texas and other states that had motivated the concerns in *DeSantis* to some degree.

In *Jenkins v. Marsh, Berry & Company, Inc.*,[67] the Northern District of Texas construed a forum selection clause to be inapplicable to a former employee's effort to invalidate a noncompetition agreement via declaratory judgment. The clause in question said suits to *enforce* the terms of the contract must be litigated in Ohio. The court held that this was an action to defeat, not enforce, the terms of the contract. Therefore, the forum selection clause did not apply.

Most recently, *Sirius Computer Solutions, Inc. v. Sparks,*[68] involved an interplay between a forum selection clause and the "first-to-file" rule. Sirius, a San Antonio based company, hired Sparks to work for it in Oregon under an employment agreement with a nonsolicitation provision. The

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[64] 2005 WL 237232 (Tex. App. – Dallas 2005).

[65] 148 S.W.3d 109 (Tex. 2004).

[66] 186 S.W.3d 576 (Tex. App. – Houston [14th Dist.] 2005), *rev'd* 50 Tex. Sup. Ct. J. 96, 26 I.E.R. Cases 459 (June 29, 2007).

[67] 2005 WL 900619 (N.D. Tex. 2005).

[68] 138 F.3d 821 (W.D. Tex. 2015).

agreement also provided for mandatory venue in San Antonio.

Sparks resigned and joined a competitor in Oregon. Sirius then filed suit in Texas state court, which was then removed to federal court. Sparks filed a second suit in an Oregon federal court. The cases were consolidated in the Western District of Texas pursuant to the forum selection clause. Sparks, however, filed a motion to transfer venue back to Oregon..

The court noted that the Fifth Circuit generally follows a first-to-file rule under which venue is proper in the court in which a lawsuit was first filed. There are, however, exceptions to this rule based on a number of private and public interest consideration. Private interests, for example, could include the burden of travel for one of the parties. The district court found that the forum selection clause precluded consideration of any private interests of the signatory parties. Only the public interests would be considered, *i.e.* (a) relative court congestion/delay, (b) local interest, and (c) familiarity with applicable law. Applying these factors, the court denied the motion to transfer venue.

F. Forum non Conveniens

Two recent cases apply the *forum non conveniens* doctrine to noncompetition agreement lawsuit. In both cases, the court transferred the case to the federal district in which the employees in question lived and worked. In *Ray Mart, Inc. v. Stock Building Supply of Texas, L.P.*,[69] the defendant employed one of the plaintiffs in Temple, Texas. That plaintiff signed a noncompetition agreement, but later resigned and was hired by the co-plaintiff employer. The former employee and his new employer filed a declaratory judgment action seeking to annul the noncompetition agreement in Jefferson County, Texas. This location was the site of the new employer/plaintiff's principal place of business and lawyer's office. The former employer/defendant removed the case to the Eastern District of Texas and sought a transfer to the Waco Division of the Western District of Texas, i.e. the closest federal court to the former employee/plaintiff's place of employment with both the former and current employers. The court granted the transfer. Likewise, in *Chemical Specialties, Inc. v. Osmose, Inc.*,[70] the court granted a motion to transfer the case from the Southern District of Texas, Houston Division, to the Eastern District of Texas, Tyler Division. Again that was the closest federal court to the place of employment with both the former and current employers. The court further noted that both corporations were out-of-state corporations and that the plaintiff's only connection to Houston appeared to be that its counsel's office was located nearby.

Finally, *in re Daniel*[71]addressed the applicability of Texas' mandatory venue provisions to a suit seeking declaratory and injunctive relief based on a noncompetition agreement. Under Texas Civil Practices and Remedies Code Section 65.023(a), a defendant sued for injunctive relief has the right to mandatory venue in defendant's home county. When multiple claims for relief are asserted, the question is whether the request for injunctive relief is dominant. In this case, the employer sought a declaration of its rights under the agreement and an injunction against violation of the noncompetition agreement. The court held that the injunctive relief request was dominant and transferred the case to the defendant's home county.

G. Removal

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[69] 435 F. Supp.2d 578 (E.D. Tex. 2006).

[70] 2006 WL 237014 (S.D. Tex. 2006).

[71] 2006 WL 2361350 (Tex. App. – Tyler 2006).

The typical noncompetition case arises and is governed by state law. Accordingly, the parties must establish diversity jurisdiction to maintain the action in federal court. This requires that the claim be valued at a minimum of $75,000. The *Ray Mart*[72] case illustrated how this amount-in-controversy standard applies to injunctive relief in the context of a noncompetition agreement. When he changed companies, the former employer/plaintiff sought an injunction to enforce a two year noncompetition provision. The new employer/defendant removed on diversity grounds. The plaintiff alleged that the amount-in-controversy test had not been met. The court disagreed. Since the employee was being paid $75,000 per year at his new job and the covenant would preclude him from working there for two years, the court held that at least $150,000 was in controversy.

H. Injunction Standards

1. Irreparable Harm

There has been some dispute as to whether traditional temporary injunction standards apply to noncompetition agreements. In two cases, the Houston Court of Appeals for the First District initially held that the Covenant Not to Compete Act eliminated the traditional requirement that a movant prove that there is a probability of irreparable harm if the covenant is not enforced by an injunction.[73] This position was noted, but not specifically adopted by the Dallas Court of Appeals.[74]

Subsequently, however, the Houston Court of Appeals for the First District reversed its course and held in *Cardinal Health Staffing Network, Inc. v. Bowen* that the traditional temporary injunction standards, including proof of irreparable injury, apply.[75] The Beaumont Court of Appeals shares this opinion.[76]

Similarly, in *Kent-Anderson Concrete, L.P. v. Nailing*,[77] the court of appeals appears to have applied the traditional temporary injunctions standards quite strictly to deny injunctive relief. This case arose out of an asset sale agreement under which the owner of a construction company agreed to sell his company and work for the new company. Three years later, the former owner entered a new employment agreement that contained a 2 year noncompetition agreement. Three years later, the former owner quit and formed a new, competing company. The new company hired the former owner and several other employees away from the prior employer. The new company promptly won bids on 5 contracts worth $3 million. The former employer had unsuccessfully bid against the new company on 3 of these 5 contracts. The former owner also used his former employer's confidential information to win these bids. Nevertheless, the court held that the trial court had not abused its discretion in denying a temporary injunction since there was insufficient proof of irreparable harm.

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72 435 F. Supp.2d at 587.

73 *Norlyn Enterprises, Inc. v. APDP*, 95 S.W.3d 578 (Tex. App. -- Houston [1st Dist.] 2002, no pet.); *Butler*, 51 S.W.3d at 795.

74 *Tom James*, 97 S.W.3d at 883.

75 106 S.W.3d 230, 236-238 (Tex. App. – Houston [1st Dist.] 2003, no pet. h.).

76 *NMTC Corp. v. Conarroe*, 99 S.W.3d 865 (Tex. App. -- Beaumont 2003, no pet. h).

77 2007 WL 2150213 (Tex. App. - Fort Worth, July 26, 2007).

Most recently, In *Watson v. Willbros Group*,[78] Willbros alleged two of its ex-employees breached their noncompetition/nonsolicitation agreements and sought a temporary injunction. The district court denied the injunction because there was insufficient evidence the agreements were properly executed, and because there was insufficient evidence of irreparable harm. Applying the traditional temporary injunction standards, the federal district court sustained the denial of the injunction.

In *Dickerson v. Acadian Cypress & Hardwoods, Inc.*,[79] however, the underlying noncompetition agreement contained a provision that dictated the issuance of an injunction without "the necessity of showing irreparable harm." Since the defendant had not challenged this provision, and in light of some evidence of harm, the court of appeals found the irreparable harm requirement had been satisfied.[80]

In *Heritage Operating,* the Fort Worth Court of appeals found that Section 15.51 permits the award of a *permanent* injunction, after trial, without the necessity of proof of irreparable injury.[81]

2. <u>Specificity</u>

An issue has arisen regarding the specificity of a temporary injunction. An injunction must be specific as to the conduct enjoined and must not refer to any other document to satisfy this specificity rule. An injunction not to solicit "customers" without listing the customers may be void for vagueness.[82] In *Rugen*,[83] however, the court incorporated the list of customers in a sealed exhibit based on the defendant's admission that he knew who the customers of that list were. In *RenewData Corporation v. Strickler*,[84] after finding that the former employee had misappropriated trade secrets and breached his fiduciary duty to the former employer, the court sustained an injunction prohibiting the employee from "disclosing" any customer information. The court apparently drew a difference between soliciting customers and disclosing customer information because in the latter instance the individual would have to know who the customer was and what the information was before he could disclose it.

More recently, in *Bellefeuille v. Equine Sports Medicine & Surgery*,[85] the defendant entered into a one-year veterinary internship. The internship agreement had a one year/50 mile post-employment noncompetition and a nondisclosure agreement. The defendant allegedly breached the noncompete and nondisclosure provisions. Plaintiff sought and obtained an injunction that, in part,

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[78] No. 4:15CV114., 2015 U.S. Dist. LEXIS 44953 (E.D. Tex. 2015).

[79] No. 09-13-00299-CV, 2014 Tex. App. LEXIS 3889, (Tex. App – Beaumont, April 10, 2014).

[80] *Id*., slip op. at ** 16-17.

[81] 2012 Tex. App. LEXIS 4939, slip op. at ** 19-20.

[82] *See, e.g., Computek Computer & Office Supplies, Inc. v. Walton*, 156 S.W.3d 217, 221-22 (Tex. App. – Dallas 2005, no pet.)

[83] 864 S.W.2d at 551.

[84] 2006 WL 504998, 24 IER Cases 325 (Tex. App. – Austin 2006).

[85] No. 02-15-00268-CV, 2016 Tex. App. LEXIS 3048 (Tex. App. – Fort Worth, March 24, 2016).

enjoined defendant from using plaintiffs confidential information, as defined in the original agreement and also any "trade secrets and confidential information [of plaintiff] in competition with" plaintiff. The court found that, in light of the definition of confidential information in the original agreement and the evidence at the temporary injunction hearing [in which defendant discussed the information she received], this language did not render the injunction impermissibly vague.

In *Dickerson*, however, the Beaumont court of appeals found a temporary injunction defective for not specifically defining the off-limits "customers," "confidential information," and competitors" that were the subjects of the injunction.[86] The necessity of such specific recitals in the injunction remains challenging to parties seeking to enforce an injunction.

Two cases recently have addressed whether the time period of a noncompetition agreement should be extended to compensate for the period of violation. In *Sheshunoff* itself, the Supreme Court stated, in pertinent part, as follows: "Obviously, the one-year period during which Johnson's activities were to be restricted has passed, and [the former employer] is no longer entitled to the injunctive relief it sought . . . ."[87]

In *Farmer v. Holley*,[88] however, the court of appeals acknowledged that equity may justify the extension on a noncompetition provision beyond its initial term. Because the trial court had entered a temporary injunction partially limiting the defendant's actions, however, and in the absence of evidence of a "persistent and consistent" violation of the covenant during the pendency of the litigation, the court refused to extend the noncompetition agreement.

In *Down Time-South Tex., LLC v. Elps*,[89] the Corpus Christi Court of Appeals affirmed the denial of a temporary injunction that was based, in part, on the plaintiff's failure to join the defendant's new employer. While noting that it is not settled whether a new employer is a "necessary party" to a noncompetition lawsuit, the court held that it was not an abuse of discretion to deny a temporary injunction that would affect the interests of the new employer, whose identity was known and recited in the petition, without the joinder of that party.

I. <u>Waiver</u>

In *Ally Financial, Inc. v. Gutierrez*,[90] the Fort Worth Court of Appeals found that an employer waived its right to enforce an employee nonsolicitation agreement because the employer issued one additional phantom stock award after the employer knew that a former employee had joined a competitor, which in turn had hired 8 of the former employer's employees. The former employer had also written a demand letter about a month before the final stock issuance claiming that the employee had breached the nonsolicitation provisions and, therefore, had forfeited rights under the phantom stock incentive plan. Apparently, the person issuing the final award did not receive, understand, or comply with this forfeiture position. For that reason, the court held that the employer had knowingly waived the right to enforce the nonsolicitation agreement.

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86 2014 Tex. App. LEXIS 3889, slip op. at ** 20-22.

87 209 S.W.3d at 657.

88 No. 10-06-00406-CV (Tex. App. – Waco, August 29, 2007).

89 2014 Tex. App. LEXIS 3047, No. 13-13-00495-CV (Tex. App. – Corpus Christi, March 20, 2014).

90 No. 02-13-00108-CV (Tex. App. – Fort Worth, January 23, 2014).

J. Arbitration

In re Pediatrix Medical Services, Inc.,[91] is a rather straightforward illustration of Texas' pro-arbitration rules within the context of a noncompetition agreement. The plaintiff filed a declaratory judgment action challenging the validity of a noncompete with a former employer. The employer moved to stay the lawsuit and compel arbitration pursuant to an arbitration agreement. The plaintiff then filed a summary judgment motion, which the trial court indicated it would entertain. The court of appeals granted mandamus relief staying the case and compelling arbitration.

K. Physician Noncompetition Agreements

Note should be taken that Section 15.50 was amended in 2009 to provide special rules governing the enforcement of noncompetition agreements against physicians licensed by the Texas Medical Board, including a reasonable "buy-out" provision, patient lists, and a patient's right to obtain their medical records.[92] In *Lasikplus of Tex., P.C. v. Mattioli*,[93] the Houston Court of appeals upheld the denial of a temporary injunction against an ophthalmologist under an agreement that lacked the required buy-out provision. The court held that reformation to add a reasonable buy-out amount was not permissible.

VIII. CONFIDENTIALITY AND NONDISCLOSURE AGREEMENTS

The effect of confidentiality and nondisclosure agreements upon the enforceability of a noncompetition agreement has been discussed above. Confidentiality and nondisclosure agreements also have independent utility of their own.

Perhaps most importantly, nondisclosure agreements are not as restrictive as noncompetition agreements and, therefore, are not subject to the limitations imposed on noncompetition agreements.[94]

IX. NONSOLICITATION AGREEMENTS

Another alternative to a noncompetition agreement is a nonsolicitation provision. A nonsolicitation. provision bars a former employee from soliciting and/or doing business with an employer's customers, vendors, or employees.

For a period of time, there was a dispute over the threshold question of whether a nonsolicitation agreement is more like a nondisclosure agreement, which is subject to ordinary contract principles, or a noncompete agreement, which is subject to the more demanding standards of the Act. Some lower courts equated nonsolicitation and noncompetition agreements. For example, in *Miller Paper Co. v. Roberts Paper Co.,*[95] the court expressly held that "the purpose and effect" of a nonsolicitation agreement is the same as a noncompetition agreement and, therefore, is subject to the same demanding standards.[96] Other courts have applied the Covenant Not to Compete Act's standards

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[91] 2005 WL 1776039 (Tex. App. – Dallas 2005)

[92] Tex. Bus. & Com. Code § 15.50(b).

[93] 418 S.W.3d 210 (Tex. App. – Houston [14th Dist.] 2013).

[94] *See, e.g., Zep Manufacturing*, 824 S.W.2d 663.

[95] 901 S.W.2d 593, 599 (Tex. App. -- Amarillo 1995, no writ).

to nonsolicitation agreements without further comment.[97]

Some courts have limited the application of a nonsolicitation agreement to restrict access only to those customers of the former employer with whom the former employee had personal contacts or acquired confidential information in the course of their prior employment.[98]

In *Ally Financial,*[99] the Fort Worth Court of Appeals applied the terms of the Act to an employee nonsolicitation provision to strike it down. The Agreement prohibited solicitation of any employee of a company with thousands of employees. The defendant employee had only worked in the IT department and the provision was not just limited to the solicitation of the IT employee with whom she had worked. The court, therefore, found it overbroad and struck it down.

Similarly, in *Garza Oilfield Mud & Chemical Services, Inc.,*[100]the court upheld a nonsolicitation agreement based on the protection of an employer's goodwill in the oil industry, but reformed it to apply only to those customers with whom the former employee had done business.

In *Nova Consulting*[101], the United States District Court for the Western District of Texas found that customer nonsolicitation provisions are subject to that analysis, but that employee nonsolicitation provisions are not. The court made this determination after an extensive review of Texas cases that are divided on this issue. The Southern District of Texas reached a similar conclusion in *Baker Petrolite Corp.*[102] In *Marsh*, however, the Texas Supreme Court stated, without any elaborate discussion that *both* customer nonsolicitation agreements and employee nonsolicitation agreements are governed by the Act. In doing so, the Court merely cited the line of authority that had subjected customer nonsolicitation agreements to the Act. *Marsh*, however, involved a breach of a *customer* nonsolicitation agreement. There were no allegations of breach of an *employee* nonsolicitation agreement. So while language in *Marsh* supports the application of the Act to both types of agreement, the language concerning employee nonsolicitation is technically just dicta.

Alliantgroup, L.P. v. Solanji,[103] is a recent customer nonsolicitation case with several interesting features. In *Alliantgroup*, several employees worked for Alliantgroup, a tax consulting firm, for several years. Alliantgroup entered into contracts to perform tax credit studies for customers. The defendant employees subsequently quit and started a competing company. In a first lawsuit, Alliantgroup alleged a variety of claims, including misappropriation of trade secrets. That case settled on terms that included a provision that the defendants/former employees and their new company, Paradigm, would not solicit any *known* customers of Alliantgroup.

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[96] *Id.* at 599.

[97] *See, e.g., Olander*, 172 F. Supp.2d 846, *Juliette Fowler Homes v. Welch*, 793 S.W.2d 660, 662-63 (Tex. 1990).

[98] *See, e.g. Stone*, 53 S.W.3d at 694; *John R. Ray,* 923 S.W.2d at 85.

[99] No. 02-13-00108-CV (Tex. App. – Fort Worth, January 23, 2014).

[100] 2012 WL 5520418 (Tex. App. – Eastland 2012).

[101] 2005 WL 2708811.

[102] 2006 WL 1751786.

[103] 2014 Tex. App. LEXIS 2961, No. 01-12-00798-CV (Tex. App. – Houston, March 18, 2014).

These defendants then apparently began to call on some of the same customers for which they had provided consulting work while employed at Alliant. Alliantgroup sued for violation of the nonsolicitation provisions of the original settlement agreement. The trial court granted summary judgment

On appeal, a pivotal question is who should be deemed a "customer." Although the original tax credit studies were for limited durations, Alliantgroup argued that it remained liable to the customers for defending any resulting tax credits claimed until all statutes of limitations ran on the underlying tax filings. This could last for a number of years. Since these customers had not notified Alliantgroup that they were terminating their professional relationship, Alliantgroup argued they remained customers subject to the nonsolicitation provisions.

The court refused to read the nonsolicitation provisions that broadly. In applying a narrower definition of the term customer, the court, in part, indicated, *sua sponte*, that the Covenant Not to Compete Act applied to a nonsolicitation provision in a settlement agreement. Accordingly, the court was disinclined to give the agreement an interpretation that could extend for many years into the future.[104]

Another interesting point this case illustrates is the practical difficulty of proving up a customer solicitation. In *Alliantgroup*, the plaintiff did not produce any testimony from actual customers. Instead, it relied on hearsay statements its own managers had received from customers about such solicitation. An alternative ground for summary judgment, with the court of appeals did not rule of in light of its disposition on the customer identity question, was that such hearsay testimony is insufficient.

X. <u>TRADE SECRETS</u>

In 2013, Texas adopted the Texas Uniform Trade Secrets Act ("TUTSA").[105] While significant, the UTSA adopts many of the rules that had already been developed under the Texas Common law. It, however, was intended to enhance Texas' uniformity with other states. It also enhances the ability to get a protective order to protect trade secrets involved in litigation.

Prior to TUTSA, Texas courts had defined a trade secret as any formula, pattern, device or compilation of information which is used in one's business and presents an opportunity to obtain an advantage over competitors who do not know or use it. *Hyde Corp. v. Huffines*.[106] "A trade secret 'may consist of any formula, pattern, device or compilation of information which is used in one's business, and which gives one an opportunity to obtain an advantage over competitors who do not know or use it. It may be . . . a list of customers.' [Citation omitted.] Before information can be termed a 'trade secret,' there must be a substantial element of secrecy. [Citation omitted.] The word 'secret' implies that the information is not generally known or readily ascertainable by independent investigation. [Citation omitted.]"[107] Trade secret status, however, was not automatically attached to

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[104] *Id., slip op., at *19, n.2.*

[105] Tex. Civ. Prac. and Rem. Code ch. 134A.

[106] 158 Tex. 566, 314 S.W.2d 763, 776, *cert. denied*, 358 U.S. 898 (1958) (quoting RESTATEMENT OF TORTS § 757 (1939)).

[107] *Rugen v. Interactive Business Systems, Inc.*, 864 S.W.2d 548, 552 (Tex. App. -- Dallas 1993, no writ).

such things as a customer list.*[108]*

TUTSA defines trade secret in a similar fashion. Under that Act, "trade secret means:

> "information, including a formula, pattern, compilation, program, devise, method, technique, process, financial data, or list of actual or potential customers or suppliers, that
>
> (A) derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use; and
>
> (B) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.[109]

Significantly, TUTSA creates a presumption in favor of the issuance of protective orders in trade secret litigation.[110] It also gives courts the power to grant attorney's fees against (a) a party who misappropriates trade secrets willfully and maliciously or moves to vacate an injunction in bad faith; and (b) a party who asserts a claim of misappropriation or opposes a motion to vacate an injunction in bad faith.[111] The act also provides triple damages for a willful and malicious misappropriation.[112]

Texas courts are somewhat divided on whether information that can be readily discovered by the public can constitute a trade secret. On the one hand, some courts have stated that the alleged trade secret information must not be publicly available or readily ascertainable.[113] On the other hand, other courts, including at least one Texas Supreme Court decision, have held that trade secret protection will apply even to publicly available information if the defendant obtained the information through improper means.[114]

TUTSA, however, clarifies that it is not a violation to independently discover a putative trade secret by independent development or reverse engineering, or other proper methods.[115]

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108 *Numed, Inc. v. McNutt*, 724 S.W.2d 432, 435 (Tex. App. -- Fort Worth 1987), *citing Allan J. Richardson v. Andrews*, 718 S.W.2d 833 (Tex. App. -- Houston [14th Dist.] 1986, no writ).

109 Tex. Civ. Prac. and Rem. Code § 134A.002(6). Note that the inclusion of financial data and customer or supplier information in Section 134.002(6) goes beyond the Uniform Trade Secrets Act itself.

110 *Id.* at § 134A.006.

111 *Id.* at § 134A.005.

112 *Id.* at § 134A.004.

113 *Numed*, 724 S.W.2d at 435, *citing SCM Corporation v. Triplett Company*, 399 S.W.2d 583, 586 (Tex. Civ. App. – San Antonio 1966, no writ).

114 *K & G Oil Tool and Service Co. v. G & G Fishing Tool Services*, 314 S.W.2d 782 (Tex. 1958); *T-N-T Motorsports, Inc. v. Hennessy Motorsports, Inc.*, 965 S.W.2d 18, 22 (Tex. App. -- Houston [1st Dist.] 1998, no pet.).

115 Tex. Civ. Prac. and Rem. Code § 134A.002(4).

Under Texas law, in order to prevail on a misappropriation claim, a plaintiff must assert and prove the following:

> (1) the existence of a trade secret; (2) knowledge of the trade secret was gained through a confidential relationship, (3) breach of the confidential relationship or some other form of improper discovery of the secret, (4) actual use or disclosure of the trade secret has occurred, (5) use of the trade secret was not authorized; (6) knowledge that the information in question constituted a trade secret, and (7) the party seeking a remedy from the court actually suffered damages.[116]

The Texas Supreme Court has reiterated that a "cause of action for misappropriation of trade secrets accrues when the trade secret is actually used."[117]

A former employer is entitled to use the general knowledge, skills, and experience he acquired in his former employment, provide that he is not utilizing the former employer's legitimate trade secrets.[118]

Finally, courts often examine the practical steps has taken to protect trade secrets. This can include factors such as whether computer or manual access to the information is restricted to certain individuals, whether there are locks, keys, or password protections in place, and whether physical access to the premises is restricted.[119] Obtaining confidentiality agreements and labeling documents as "confidential" is also relevant.

A common question is the extent that customer information constitutes trade secrets. The courts have recognized that customer information may, but not necessarily will, constitute a trade secret depending on the particular facts of the case. In *Nova Consulting,*[120] the Western District recognized that while the *identity* of customers may not be a bona fide trade secret, a collection of business cards and knowledge of particular customer preferences may be. In *Sands*, the Fort Worth Court of Appeals found that the identities of clients of a CPA office in Denton were not confidential. In reaching this conclusion, the court appeared to view Denton as a small community where such information is well known, in part because the clients talk to each other and in part because the CPA practice provided references of existing clients to potential new clients.

In *Aspen Technology, Inc. v. M3 Tech., Inc.*, the Fifth Circuit recently upheld a permanent injunction and over $11 million in damages against a former employee and his new employer for a flagrant pattern of trade secret misappropriation of trade secrets, copyright infringement, and discovery abuse apparently designed to cover up such misappropriation. This dispute arose out of the alleged misuse of computer software for the chemical and petrochemical industry. The jury had awarded nearly $12 million in damages and attorneys' fees and the trial court entered a permanent injunction against

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[116] Troy A. Martin, Comment, *The Evolution of Trade Secret Law in Texas: Is It Time to Recognize the Doctrine of Inevitable Disclosure*? 42 S. Tex. L. Rev. 1361, 1370 (Fall 2001) (hereinafter "Evolution of Trade Secret Law") (citations omitted).

[117] *Computer Associates Intern., Inc. v. Altai, Inc.*, 918 S.W.2d 453, 455 (Tex. 1996) *citing Huffines* 314 S.W.2d at 769.

[118] *Anderson Chemical*, 66 S.W.3d 434.

[119] *See, e.g. T-N-T Motorsports*, 965 S.W.2d at 22.

[120] 2005 WL 2708811.

continued misappropriation. The court of appeals upheld most of these damages, but remanded for the deletion of an attorney's award that had been based only on a tortious interference. The court held that Texas law does not permit attorneys' fees for such a claim. Finally, the court held that the three year statute of limitation on misappropriation and copyright claims is subject to the discovery rule and that the mere fact that an employer had joined a competitor and may be using confidential information is insufficient to trigger the running of the limitations period.[121]

Finally, in *Daily Instruments Corp. v. Heidt*,[122] a Southern District of Texas District Court opinion sets forth a raft of factual findings of flagrant misappropriation. In that case, a new college hire rapidly rose in the sales ranks of another petrochemical industry device manufacturer. When a competitor was taken over by a German conglomerate in the same industry, German company ordered its U.S. acquisition to triple sales within a year. In response, the U.S. company, which had already hired a key manager from the plaintiff, solicited other key sales employees to defect to the U.S. subsidiary. The evidence revealed that the defendant company was not only seeking to expand it talent base, but deliberately attempting to deliver a "severe body blow" to the plaintiff.[123]

The defecting employee had a noncompete with the plaintiff, but obtained an agreement from the defendant company to fully defend and indemnify the employee for its breach. The defecting employee then engaged in a campaign of copying, and disclosing trade secrets to his new employer before resigning. He also deliberately timed his resignation to coincide with an international trade show at which he was scheduled to present, so as to maximize the damage to his former employer.

XI. INEVITABLE DISCLOSURE

An unsettled concept under Texas law is the "doctrine of inevitable disclosure." Although this doctrine has surfaced before, its recent growth traces itself to the landmark Seventh Circuit decision in *PepsiCo v. Redmond*.[124] In that case, a high level PepsiCo manager defected to Quaker Oats, a major competitor of PepsiCo in the sports drink market. The district court and Seventh Circuit affirmed an injunction barring the executive's employment at Quaker Oats based on the similarity of his former and current position, evidence of duplicity by the executive, and the executive's admission that it would be difficult not to use the confidential marketing information he had acquired at PepsiCo.

The current status of the inevitable disclosure doctrine in Texas is uncertain. As the Houston Court of Appeals noted in the *Cardinal Health Staffing case*, "no Texas case expressly adopt[ed] the inevitable disclosure doctrine, and it is unclear to what extent Texas courts might adopt it or might view it as relieving an injunction applicant of showing irreparable injury."[125] As noted above the fundamental premise of the inevitable doctrine is at odds with Texas' longstanding standards for misappropriation of trade secrets cases. In addition, to the extent it constitutes a common law *de facto* noncompetition agreement, it violates the broad preemptive provision in Section 15.50.

Other decisions by the Dallas and Houston Courts of Appeals, and the Southern District of Texas, however, do appear to have adopted some form of a "probable disclosure" rule. For example, in

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[121] 569 Fed. Appx. 259 (5th Cir. 2014) (unpublished).

[122] 998 F. Supp. 2d 553 (S.D. Tex. 2014).

[123] *Id.* at 553.

[124] 54 F.3d 1262 (7th Cir. 1995).

[125] 106 S.W.3d at 242.

Rugen v. Interactive Business Systems,[126] the plaintiff was a computer personnel staffing company. The defendant was an account manager who resigned and immediately started her own computer personnel staffing company in direct competition with the plaintiff. At the time the defendant resigned certain confidential documents disappeared from the plaintiff's office. Although the court found that a noncompetition agreement between the parties was unenforceable, the court found as follows:

> . . . [The defendant] possesses confidential information of [the plaintiff's] and operates a firm in direct competition with [the plaintiff]. [The Defendant] is in possession of [the plaintiff's] confidential information and is in a position to use it. Under these circumstances, it is probable that [the defendant] will use the information for her benefit and to the detriment of [the plaintiff]. At times, an injunction is the only effective relief an employer has when a former employee possesses confidential information. *See Weed Eater, Inv. v. Dowling*, 562 S.W.2d 898, 902 (Tex. Civ. App. – Houston [1st Dist.] 1978, writ ref'd n.r.e.).[127]

Based on the foregoing, the court affirmed a temporary injunction barring the defendant from soliciting or doing business with the plaintiff's customers that were identified on a customer list that was contained in a sealed exhibit and incorporated by reference in the injunction.[128]

Rugen was followed by the Dallas Court of Appeals in its unpublished decision in *Conley v. DSC Communications Corp.*[129] In *Conley*, the defendant headed a team responding to a major Request for Proposal ("RFP") on behalf of the plaintiff. Midway through the process, the defendant resigned and went to a competitor that was also responding to the RFP in direct competition with the plaintiff. The plaintiff sought to enjoin the defendant based on the doctrine of inevitable disclosure. Although though the court held that the specific term "inevitable disclosure" had not been adopted by Texas courts, the court did recognize the concept of "probable" disclosure articulated in *Rugen*.[130]

In applying the probable disclosure concept, the *Conley* court first refused to rigidly apply a checklist of factors proposed by the defendant. This checklist included the following factors: (1) whether the departing employee engaged in misconduct, (2) whether the new employer needed its competitors information due to its own lack of technology, (3) the degree to which the positions in question were similar, (4) the efforts of the new employer to protect the former employer's trade secrets, and (5) the existence of a noncompetition agreement. between the former employer and departing employee.[131] Indeed, although the court acknowledged that the existence of these factors may be helpful in supporting an injunction, the court specifically held that lack of misconduct on the part of the departing employee, efforts by the new employer to avoid misuse, and lack of a

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[126] 864 S.W.2d 548.

[127] *Id*. at 552.

[128] A separate issue was whether an injunction can incorporate such a sealed document by reference in light of Rule 683 of the Texas Rules of Civil Procedure, which generally prohibits reference to any external documents in an injunction. Balancing the needs for privacy protection against this rule, the court found that such a reference was permissible in this type of case. 864 S.W.2d at 553.

[129] 1999 WL 89955 (Tex. App. -- Dallas 1999).

[130] 1999 WL 89955 at *14.

[131] *Id*.

noncompetition agreement were not fatal to a probable disclosure claim. Based on the evidence before it, the court sustained an injunction barring the defendant from using or disclosing confidential information or doing business with the customer for which the defendant had prepared the RFP response.[132]

In *T-N-T Motorsports*,[133] the plaintiff designed and sold high performance engine upgrades to Dodge Viper sports cars. Two employees involved in the manufacturing and sales of the sports cars quit to work for their own competing company. These former employees bragged that their product was identical to their former employer's product, only cheaper. They also provided similar packages, tests, equipment, and warranties. They even adopted a similar name for their product, i.e. "Serpent" rather than "Venom."[134] They acknowledged that they had already taken three of the plaintiff's former customers. Based on this, the court concluded that the defendants "possess appellee's confidential information and are in a position to use it to compete directly with appellee."[135] Based on the foregoing, the court enjoined the defendants from disclosing or using the specific trade secrets of the plaintiff.[136]

In *Maxxim Medical, Inc. v. Michelson,*[137] the defendant was a California sales employee for a Texas corporation. Shortly before he resigned, the defendant asked another employee to print out a large batch of customer information, which subsequently disappeared. The defendant initially denied taking the documents, but later admitted he took them. His contention that the documents were illegible was subsequently contradicted by the other employee.

The district court found that, unlike the case with a noncompetition agreement, California law should apply to a misappropriation of trade secret/inevitable disclosure claim The district court predicted (inaccurately as it turned out) that California would adopt the inevitable disclosure doctrine. The court then identified a number of factors considered by courts around the country that have adopted the inevitable or probable disclosure rule. These included the following: (1) the degree of competition between the former and present employers, (2) the similarity between job positions, (3) lack of candor on the part of the departing employee as to his or her new job, (4) the specificity with which the former employer has clearly identified the trade secrets, (5) the degree of actual use of trade secrets that has already occurred, (6) the existence of nondisclosure and noncompetition agreements between the former employer and employee, (7) the new employer's policies against use of trade secrets, and (8) the ability to sanitize the new position by taking steps to preclude improper use of trade secrets.[138] The court found these factors supported an injunction barring the defendant from working for a competitor.

As noted above, the most recent appellate decision on the inevitable or probable disclosure doctrine is the *Cardinal Staffing* decision. In determining that the inevitable or probable disclosure rule

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[132] *Id.* at 18-19.

[133] 965 S.W.2d 18.

[134] *Id.* at 20-21.

[135] *Id.* at 24.

[136] *Id. at 25-26.*

[137] 51 F. Supp.2d 773 (S.D. Tex. 1999).

[138] 51 F. Supp. at 786.

should not be applied in that case, the Houston Court of Appeals relied on the following factors: (1) the lack of evidence that the former employee retained confidential information after he left the former employer, (2) the limited overlap between the former and present employer's temporary placement employees, (3) the lack of solicitation of the former employer's customers by the former employee, (4) the existence of prior business relationships between the former employer's customers and the present employer, (5) the present employer's development of a business plan prior to the hire of the former employee, (6) the present employer's professed lack of need for the information of the prior employer, and (7) the public availability of information concerning potential temporary placement employees and customers.[139] These factors outweighed the application of the inevitable disclosure rule in *Cardinal Staffing* despite the fact that the former employee had (1) obtained a printout of confidential information from the former employee on the day he resigned, (2) falsely stated that the printout was unreadable and failed to return it, (3) joined the new employer to start up a new business operation in direct competition with the former employer, and (4) obtained the vast majority of his temporary placement employees and customers at the new employers from the old employers employee/customer base.

In *Baker Petrolite Corp. v. Spicer*,[140] the U.S. District Court for the Southern District of Texas appears to have applied a version of the inevitable disclosure doctrine. In this case, the defendant had been an Account Manager for the plaintiff when he signed a nondisclosure/noncompetition agreement. The agreement stated that the employee had or would receive confidential information and imposed an 18 month post-employment nonsolicitation and noncompete period. The employee, in fact, did receive confidential information commencing about a week after the execution of the agreement. The employee continued receiving such information, including sitting in on a sensitive sales meeting on the day he resigned to join a competitor. Thereafter, the employee competed against the former employer, including with respect to the customer discussed in the sensitive sales meeting. The court found that, under these circumstances, the employee could "reasonably be expected to reveal, base judgments upon, or otherwise disclose or use any of the proprietary and confidential information of trade secrets of [the former employer]" and would "have difficulty preventing his knowledge of [the former employer's] products and processes relating to specific locations and customers from infiltrating his work if [the employee] works with those customers [he had worked with at the former employer] in those specific locations [at which he had worked]." The court, therefore, enjoined the employee from soliciting or working with the former customers with whom he worked at the specific locations at which he had worked for the balance of the nonsolicitation/noncompete period. The court, however, did not preclude the employee from working at all for the new employer during this period.

Most recently, in *Cardoni*, the Fifth Circuit reviewed the Texas case law regarding the inevitable disclosure doctrine. Relying on *Cardinal Health Staffing* and *M-I, LLC v. Stelly*,[141] the Fifth Circuit found that the trial court did not commit clear error in finding that Texas courts had not yet adopted the inevitable disclosure doctrine or abuse its discretion in denying a temporary injunction.[142]

This author questions the validity of judicial adoption of the inevitable or probable disclosure doctrine in Texas based on Section 15.52 of the Covenant Not to Compete Act. That Section contains a broad preemption of any common law doctrines in the area of noncompetition law. To the extent the

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[139] 106 S.W.3d at 242-243.

[140] 2006 WL 1751786 (S.D. Tex. 2006).

[141] No. H-09-cv-01552, 2009 U.S. Dist. LEXIS 65866 (S.D. Tex. July 30, 2009).

[142] 805 F.3d at 589-90.

inevitable or probable disclosure doctrine occupies the same field as noncompetition agreements, it can be argued that Section 15.52 precludes its adoption in this state.

A counter-argument can be based on the underlying legislative purpose of Section 15.52. That Section was adopted to fend off judicial hostility towards the enforcement of noncompetition agreement that had been exhibited in cases like *Hill*. Thus, it was intended to supplement a policy in favor of broad enforceability of reasonably drawn and justifiable noncompetition agreements. It would be ironic to use 15.52 to limit judicial *expansion* of noncompetition-like remedies. But perhaps what is good for the goose is good for the gander. Section 15.52 may limit courts' right to limit or expand the noncompetition rules set forth in Section 15.50-15.52.

XII. DAMAGES

There have been several interesting cases recently regarding proof of damages in noncompetition and theft of trade secret cases. For example, in *Acadia HealthCare Company v. Horizon Health Company,*[143] one healthcare company acquired another such company. The President and other top managers of the acquired company entered into noncompetiton and nonsolicitation agreements, but subsequently left to form a competing company. They allegedly copied significant amounts of confidential information and solicited customers in breach of their agreements and common law duties. A jury awarded the former company $6 million dollars, including past and future lost profits of approximately $4.2 million and exemplary damages of $1.75 million. On appeal, the Fort Worth Court of Appeals found that the plaintiff's expert witness testimony was too speculative to be relied on. The court reversed and rendered judgment against plaintiffs regarding the future lost profits. The court then remanded the exemplary damage award to the trial court for a proportionality analysis in light of the reversal of the lost profits verdict and the constitutional rule that exemplary damages must bear a reasonable relation to actual damages. As a rule of thumb, the ratio of punitive to actual damages can be no more that 4:1 or 4.3:1.

In *AZZ Inc. v. Morgan,*[144] the plaintiff's plant manager signed a noncompetition agreement. Subsequently, that manager developed his own business, quit, and solicited business from at least 6 of his former employer's customers, obtaining business from at least one major customer. The jury rendered a verdict finding breach of the noncompete, but finding zero damages. The plaintiff filed for JNOV and appealed on legal sufficiency and factual sufficiency grounds. The plaintiff claimed that there was undisputed evidence of at least some damages resulting from the breach. The court of appeals rejected this argument. Significantly, with respect to the one major customer who had begun doing business with the defendant, the court noted that the customer had been under no contractual obligation to continue doing business with the plaintiff. Moreover, that customer had initially started doing business with a third company before switching to the defendant's new business. Therefore, the court concluded the jury could reasonably have found a lack of evidence the defendant's breach was the reason plaintiff lost any business. The court cited *Acadia* for the proposition that the expert witness's lost profit testimony was too speculative.

In *Merritt Hawkins & Associates, LLC v. Gresham*,[145] a former employee recruited another employee

[143] 472 S.W.3d 74 (Tex. App. – Fort Worth 2015).

[144] 462 S.W.3d 284 (Tex. App. – Fort Worth 2015).

[145] 79 F.Supp.3d 625 (N.D. Tex. 2015).

of Merritt Hawkins to join him at a competitor. The second employee allegedly copied over 400 confidential files before leaving Merritt Hawkins. Merritt Hawkins sued both employees on a number of grounds including breach of the "non-interference" provision and theft of trade secret. It then moved for summary judgment.

Merritt Hawkins designated its president as both an expert and lay witness on damages. The defendants moved to strike this testimony and alleged that there was no evidence of damages for purposes of summary judgment. The court found that the president could testify as a lay witness on his own company's lost profit, but not on the alleged amount defendants' new employer profited from the employees switch. The court also said it was permissible for the president to testify based, in part, on damage calculations that he had not personally prepared and with which he was not fully conversant.