

2017 Update: Suing or Defending the Departing Texas Employee, Including Non-competes, Trade Secrets, and Fiduciary Duties

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I. INTRODUCTION

This paper provides a summary of current Texas law regarding: (1) the inevitable disclosure doctrine; (2) covenants not to compete; (3) non-recruitment covenants; (4) the fiduciary obligations of at-will employees; (5) protecting or obtaining trade secrets in state and federal court litigation; (6) misappropriation of trade secrets cases; and (7) the duty of preservation and spoliation issues in discovery.

II. THE CURRENT STATE OF THE “INEVITABLE DISCLOSURE” DOCTRINE IN TEXAS

A. What Is The “Inevitable Disclosure” Doctrine?

1. Background Regarding Trade Secret Misappropriation

a. In General

To understand the inevitable disclosure doctrine, it is necessary to first have an understanding of the law regarding trade secret misappropriation as it existed before the Texas Uniform Trade Secrets Act (“TUTSA”) took effect on September 1, 2013. Under pre-TUTSA Texas law, trade secret misappropriation was established by showing that a trade secret existed, the trade secret was acquired through a breach of a confidential relationship or was discovered by improper means, and the defendant used the trade secret without the plaintiff’s authorization. *See Tex. Integrated Conveyor Sys., Inc. v. Innovative Conveyor Concepts, Inc.*, 300 S.W.3d 348, 366-67 (Tex. App.–Dallas 2009, pet. denied); *Avera v. Clark Moulding*, 791 S.W.2d 144, 145 (Tex. App.–Dallas 1990, no writ); *CQ, Inc. v. TXU Mining Co.*, 565 F.3d 268, 273 (5th Cir. 2009); *Alcatel USA, Inc. v. DGI Tech.*, 166 F.3d 772, 784 (5th Cir. 1999). As is true even post-TUTSA, upon the formation of an employment relationship, certain duties arise apart from any written contract. For example, an employee is prohibited from using trade secret information acquired during the relationship in a manner adverse to his employer. This obligation survives termination of employment. Furthermore, though it does not bar the former employee from using the general knowledge, skill, and experience acquired during

employment, this duty does prevent him from utilizing trade secrets acquired during the course of employment. *See Rugen v. Interactive Bus. Sys., Inc.*, 864 S.W.2d 548, 551 (Tex. App.–Dallas 1993, no writ); *Executive Tele-Communication Sys., Inc. v. Buchbaum*, 669 S.W.2d 400, 403 (Tex. App.–Dallas 1984, no writ). Injunctive relief is an appropriate remedy to curtail violation of this duty. *Thermotics, Inc. v. Bat-Jac Tool Co.*, 541 S.W.2d 255 (Tex. Civ. App.–Houston [1st Dist.] 1976, no writ); *Hyde Corp. v. Huffines*, 158 Tex. 566, 314 S.W.2d 763 (1958).

Pre-TUTSA, a trade secret was defined 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.” *In re Bass*, 113 S.W.3d 735, 739 (Tex. 2003). To determine whether a trade secret existed pre-TUTSA, a court weighed six fact-intensive factors: (1) the extent to which the information was known outside of the business; (2) the extent to which it was known by employees and others involved in the business; (3) the extent of measures taken to guard the secrecy of the information; (4) the value of the information to the business and to its competitors; (5) the amount of effort or money expended in developing the information; and (6) the ease or difficulty with which the information could be properly acquired or duplicated by others. *See id.* (citing Restatement of Torts § 757 cmt. b. (1939); Restatement (Third) of Unfair Competition § 39 reporter’s note cmt. d. (1995)); *In re Cooper Tire & Rubber Co.*, 313 S.W.3d 910, 915 (Tex. App.–Houston [14th Dist.] 2010, no pet.) (concluding trade secret protection existed). The party claiming a trade secret did not have to satisfy all six factors because trade secrets do not fit neatly into each factor every time. *In re Bass*, 113 S.W.3d at 740; *In re Cooper Tire & Rubber Co.*, 313 S.W.3d at 915. The status of the information claimed as a trade secret had to be determined through a comparative evaluation of all the relevant factors, including the value, secrecy, and definiteness of the information as well as the nature of the defendant’s misconduct. *In re Bass*, 113 S.W.3d at 739.

Under the umbrella of protected data were compilations of information which have a substantial element of secrecy and provided the employer with an opportunity for advantage over competitors. *See In re Bass*, 113 S.W.3d at 739; *Rugen, Inc.* 864 S.W.2d at 552; *Luccous v. J.C. Kinley Co.*, 376 S.W.2d 336, 338 (Tex. 1964). Examples of such data included pricing information, customer lists, client information, customer preferences, buyer contacts, and market strategies. *See Rugen*, 864 S.W.2d at 552; *Murrco Agency, Inc. v. Ryan*, 800 S.W.2d 600, 604-605 & n. 5 & 6 (Tex. App.–Dallas 1990, no writ); *Bertotti v. C.E. Shepherd Co.*, 752 S.W.2d 648, 654-55 (Tex. App.–Houston [14th Dist.] 1988, no writ); *see also Rimkus Consulting Group, Inc. v. Cammarata*, 688 F. Supp. 2d 598, 668 (S.D. Tex. 2010) (Rosenthal, J.) (surveying Texas law on this issue and concluding that “[b]ased on the evidence presented at the injunction hearing held in 2008, this court concluded that Rimkus’s client database, pricing information, and business plan were the type of information that courts had recognized as entitled to trade secret protection.”).

Moreover, the mere fact that knowledge of this information may have been acquired through proper means did not preclude protection from those who would secure that knowledge by unfair means. *See Weed Eater, Inc. v. Dowling*, 562 S.W.2d 898, 901 (Tex. Civ. App.–Houston [1st Dist.] 1978, writ ref’d n.r.e.). When deciding whether to grant or deny a request for a temporary injunction, the trial court did not decide whether the information sought to be protected was a trade secret; rather it determined whether the applicant has established that the information was entitled to trade secret protection until a trial on the merits. *See INEOS Group Ltd. v. Chevron Phillips Chemical Co., LP*, 312 S.W.3d 843, 848 (Tex. App.–Houston [1st Dist.] 2009, no pet.); *Sharma v. Vinmar Int’l, Ltd.*, 231 S.W.3d 405, 424 (Tex. App.–Houston [14th Dist.] 2007, no pet.); *Ctr. for Econ. Justice v. Am. Ins. Ass’n*, 39 S.W.3d 337, 343 (Tex. App.–Austin 2001, no pet.); *T-N-T Motorsports, Inc. v. Hennessey Motorsports, Inc.*, 965 S.W.2d 18, 23-24 (Tex. App.–Houston [1st Dist.] 1998, no pet.). That an order is issued granting trade secret protection did not mean the protected information is a trade secret. *See Ctr. for Econ. Justice*, 39

S.W.3d at 343. Rather, trade secret protection was held to be warranted when an effort was made to keep material important to a particular business from competitors. *See INEOS Group Ltd.*, 312 S.W.3d at 854; *Rugen*, 864 S.W.2d at 552; *Gonzales v. Zamora*, 791 S.W.2d 258, 265 (Tex. App.—Corpus Christi 1990, no writ).

When a defendant possesses trade secrets and is in a position to use them, harm to the trade secret owner could be presumed. *See T-N-T Motorsports, Inc.*, 965 S.W.2d at 24 (holding that appellant possessed confidential information and was in a position to use it; thus, appellant was likely to use information to former employer’s detriment). The threatened disclosure of trade secrets was held to constitute irreparable injury as a matter of law. *Williams v. Compressor Eng’g Corp.*, 704 S.W.2d 469, 471 (Tex. App.—Houston [14th Dist.] 1986, writ ref’d n.r.e.) (citing *FMC Corp. v. Varco Int’l, Inc.*, 677 F.2d 500, 503 (5th Cir. 1982)). Injunctive relief could be employed when one breached his confidential relationship in order to misuse a trade secret. *Luccous*, 376 S.W.2d at 341. Injunctive relief was also found proper to prevent a party, which had appropriated another’s trade secrets, from gaining an unfair market advantage. *T–N–T Motorsports, Inc.*, 965 S.W.2d at 24. Irreparable harm could also be established by evidence that disclosure of trade-secret information could enable competitors to misuse the marketing plans and strategies of the applicant and avoid the less successful strategies as well as the risk and expense of developing the strategies. *Mabrey v. Sandstream, Inc.*, 124 S.W.3d 302, 319 (Tex. App.—Fort Worth 2003, no pet.). The misuse of trade secrets leading to the loss of an existing business was another example of irreparable harm entitling an applicant to injunctive relief. *Miller Paper Co. v. Roberts Paper Co.*, 901 S.W.2d 593, 602 (Tex. App.—Amarillo 1995, no writ).

b. The Texas Uniform Trade Secrets Act, That Became Effective September 1, 2013 – And A Brewing Significant Issue Under That Law

On May 2, 2013, Texas Governor Rick Perry signed TUTSA into law. The new law adopts a version of the Uniform Trade Secrets Act (“UTSA”). TUTSA is found at Texas Civil Practice and Remedies Code Section 134A.001 *et seq.* The law took effect

on September 1, 2013 and applies to a misappropriation of trade secrets that takes place on or after that date. The common law of Texas is very similar to the UTSA in many ways. Of note, the law includes a definition of “trade secret” is:

“[I]nformation, including a formula, pattern, compilation, program, device, method, technique, process, financial data, or list of 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.”

Id. at § 134A.002(6).

Other aspects of the new law are express statutory authority for courts to enjoin actual or threatened misappropriation (*Id.* at § 134A.003(a)), a court’s ability to order the payment of a reasonable royalty in “exceptional circumstances,” (*Id.* at § 134A.003(b)), and a mandate that a court hearing any claim for misappropriation of trade secrets issue protective orders and take other “reasonable means” to preserve the secrecy of the alleged trade secret (*Id.* at § 134A.006). “In appropriate circumstances, affirmative acts to protect a trade secret may be compelled by court order.” *Id.* at § 134A.003. The new law also provides for monetary damages, which can include both the actual damages and unjust enrichment resulting from the misappropriation (*Id.* at § 134A.004(a)). Upon a finding of willful and malicious misappropriation, a court would also be empowered to award exemplary damages in an amount not exceeding twice the award of damages (*Id.* at § 134A.004(b)), and attorneys’ fees are also recoverable in certain circumstances (*Id.* at § 134A.005). However, the law also expressly provides for the payment of attorneys’

fees to a defendant where a claim for misappropriation is made in bad faith (*Id.* at § 134A.005(1)).

With a stated general purpose “to make uniform the law” with respect to the misappropriation of trade secrets, the law displaces existing common law on the subject, to include any law of the state providing for civil remedies for misappropriation of a trade secret, but would not affect contractual remedies, other civil remedies not based upon a misappropriation of trade secrets, or any criminal remedies aimed at addressing misappropriation of trade secrets (*Id.* at § 134A.007 and 134.008). The law’s impact on related theories of legal relief in Texas (like the inevitable disclosure doctrine) and on burdens of proof (such as the level of specificity required in pleadings that describe the trade secret) is not clear. The TUTSA does not separately adopt the inevitable disclosure doctrine – indeed, it does not address the inevitable disclosure doctrine at all. *See* Joseph F. Cleveland Jr. and Heath Coffman, *Protecting Trade Secrets Made Simple*, Tex. Bar Journal, Vol. 76, No. 8 at 754 (Sept. 2013). Texas is the forty-eighth state to adopt the UTSA, so cases from other states interpreting the law may be a rich source of guidance as such cases proceed in Texas.

One important issue that has come up since TUTSA’s passage is the question of whether, to state a claim for misappropriation under TUTSA, the plaintiff must allege and prove that the defendant *acquired* the trade secrets through improper means. To establish a cause of action for trade secret misappropriation under TUTSA, a plaintiff must show that: (1) a trade secret existed; (2) the defendant acquired the trade secret through “improper means”; and (3) the defendant disclosed the trade secret without the plaintiff’s consent. *Educ. Mgmt. Servs., LLC v. Tracey*, 102 F. Supp. 3d 906, 914 (W.D. Tex. 2015); Tex. Civ. Prac. & Rem.Code § 134A.002. Under TUTSA, “improper means” includes “theft, bribery, misrepresentation, breach or inducement of a breach of a duty to maintain secrecy, to limit use, or to prohibit discovery of a trade secret, or espionage through electronic or other means.” Tex. Civ. Prac. & Rem.Code § 134A.002(2). In *Educ. Mgmt. Servs., LLC*, the district court held that if the defendant did not improperly

acquire the trade secret in the first place, then the plaintiff cannot establish a claim for trade secret misappropriation under TUTSA. *Educ. Mgmt. Servs., LLC*, 102 F. Supp. 3d at 914. The district court stated that, “[t]he plain language of § 134A.002(3)(B)(i) requires that a defendant “acquire” knowledge of the trade secrets at issue through “improper means.”” *Id.* Although, under common law, acquisition of the trade secret through improper means was not a requirement (if, for example, the trade secret was acquired during the existence of confidential relationship), the district court noted that, “TUTSA specifically provides that it “displaces conflicting tort ... law of this state providing civil remedies for misappropriation of a trade secret.”” Tex. Civ. Prac. & Rem.Code § 134A.007. *Educ. Mgmt. Servs., LLC*, 102 F. Supp. 3d at 915.

The reading *Educ. Mgmt. Servs., LLC* gave TUTSA would dramatically limit its impact in trade secret cases arising out of the employment relationship, and generally. At least one other district court has not followed *Educ. Mgmt. Servs., LLC* on this point. *See, e.g., AlliantGroup, L.P. v. Mols*, Case No. H-16-3114, 2017 WL 432810, at *10 (S.D. Tex. Jan. 30, 2017) (allowing TUTSA case to proceed based on allegation that the trade secrets were acquired during the existence of a confidential relationship). But, the issue remains to be specifically litigated in higher courts.

2. The Inevitable Disclosure Doctrine

The inevitable disclosure doctrine builds on the legal rules relating to trade secrets, and holds as follows:

[T]here are circumstances in which trade secrets inevitably will be used or disclosed, even if the defendant swears that he or she will keep the information confidential. Courts applying the doctrine have differed over its reach and the circumstances required for its application, but, generally speaking, the doctrine applies when a defendant has had access to trade secrets and then defects to the trade secret owner’s competition to perform duties so similar that the court believes that those duties cannot be

performed without making use of trade secrets relating to the previous affiliation.

See Cardinal Health Staffing Network, Inc. v. Bowen, 106 S.W.3d 230, 242 (Tex. App.—Houston [1st Dist.] 2003, no pet.) (quoting Linda K. Stevens, Trade Secrets & Inevitable Disclosure, 36 Tort & Ins. L.J. 917, 929 (Summer 2001)).

B. Have Texas Courts Adopted The “Inevitable Disclosure” Doctrine?

No Texas case *expressly* adopts the inevitable disclosure doctrine. *Cardinal Health Staffing Network, Inc.*, 106 S.W.3d at 242 (“We have found no Texas case expressly adopting the inevitable disclosure doctrine”). The court in *Cardinal Health Staffing Network, Inc.* refused to apply the doctrine based on the particular facts of the case, which showed the plaintiff’s ex-employee was perfectly capable of performing his job with his new employer without using his ex-employer’s trade secrets or confidential information. Likewise, in *M-I, L.L.C. v. Stelly*, Slip Copy, Civil Action No. H-09-CV-01552, 2009 WL 2355498, at *7 (S.D. Tex. July 30, 2009), Judge Gray H. Miller declined to apply the inevitable disclosure doctrine based on the *Cardinal Health Staffing Network, Inc.* case, and the fact that the “[p]laintiff has similarly failed to show that Stelly and Squyres took any confidential information with them or that they are using such information at Wellbore; the Court will therefore not apply the inevitable disclosure doctrine.” *Id.*

In the 2015 decision of *Cardoni v. Prosperity Bank*, 805 F.3d 573, 589–90 (5th Cir. 2015), the Fifth Circuit noted that Texas courts have not adopted the inevitable disclosure doctrine. *See also Cameron Int’l Corp. v. Steven Abbiss*, No. H-16–2117, 2016 WL 6216667, at *5 n.4 (S.D. Tex. Oct. 25, 2016) (noting that the inevitable disclosure doctrine is not recognized in Texas).

But there are several Texas cases that implicitly rely on a probable or inevitable disclosure theory to enjoin an ex-employee from performing specific types of work for a new employer, even where there is no proof that the ex-employee misappropriated his or

her ex-employer's trade secrets or confidential information. *See* 36 A.L.R. 6th 537, *Applicability of Inevitable Disclosure Doctrine Barring Employment of Competitor's Former Employee* (2008) (summarizing Texas cases applying the probable or inevitable disclosure theory as a basis to enjoin an ex-employee from working in a specific area for a competitor). One such case is *Baker Petrolite Corp. v. Spicer*, No. 06-1749, 2006 WL 1751786 at *10-11 (S.D. Tex. 2006). There, a former employee, Spicer, was accused of misappropriating his former employer's trade secrets and confidential information. *See id.* at *3. Judge Gray H. Miller found that Spicer's covenant not to compete was unenforceable because it was not "ancillary to or part of" an otherwise enforceable agreement, as required by Section 15.50 of the Texas Business and Commerce Code. *See id.* at *7. There was also no proof that Spicer misappropriated or used Baker Petrolite's trade secrets or confidential information. *Id.* at *9.

Nevertheless, Judge Miller applied a probable or inevitable disclosure theory and granted a preliminary injunction in favor of the former employer. *See id.* at *11. The injunction was carefully tailored to allow Spicer the maximum amount of freedom to pursue new employment, while still protecting the former employer's confidential information. *See id.* at *10. In addition to being generally enjoined from disclosing any of his former employer's trade secrets, Spicer was specifically enjoined from working with any customers of his former employer with whom he had sales contact during the last eighteen months of his employment, at the specific locations at which he worked for his former employer. *See id.* at *10-11. The court determined that the injunction would not unfairly limit Spicer's freedom to advance his career because of the large number of non-Baker Petrolite customers he could work with, and the numerous other locations at which he could work. *See id.* Therefore, the court held that it was appropriate and necessary to enjoin Spicer from working with particular customers at particular locations where the risk of using or disclosing Baker Petrolite trade secrets was particularly high. *See id.* As the court held:

Due to the inherent threat of disclosure, the nature of the information at issue, and the direct competitive relationship between Baker and Multichem, Spicer is further enjoined from working with Baker customers with which he had contact in a sales capacity during the last eighteen months of his employment with Baker.

Id. at *11.

Spicer did not use the phrase “inevitable disclosure.” But, it applied the doctrine. *Spicer* relied on *FMC Corp.*, 677 F.2d at 503 and *Weed Eater, Inc.*, 562 S.W.2d at 901. In *FMC Corp.*, the defendant, Best Industries, having tried unsuccessfully to develop its own version of FMC’s technology, recruited an FMC engineer involved in research and product development to come work for Best. *See id.* FMC and the former employee, Witt, had no covenant not to compete, but Witt had signed FMC’s standard nondisclosure agreement as part of his employment. *See id.* at 505. FMC sought a preliminary injunction enjoining Witt from using or disclosing any FMC trade secrets, and enjoining Best from placing Witt in a position that would create the threat of inherent disclosure. *See id.* at 501.

The district court denied the application, but the Fifth Circuit Court of Appeals reversed, holding that FMC had proved all four requirements necessary for preliminary injunctive relief. *See id.* at 502. The Fifth Circuit rejected the defendant’s assertion that Witt would be able to decide for himself what information he could or could not properly disclose to Best while working on the same technology he had worked on for FMC. *See id.* at 504. Instead, the Court noted that “[e]ven assuming the best of good faith, Witt will have difficulty preventing his knowledge of FMC’s ‘Longsweep’ manufacturing techniques from infiltrating his work.” *Id.* In the Court’s view, the only way to safeguard FMC’s trade secrets was to grant the requested injunction, enjoining Witt from divulging any of FMC’s trade secrets, and enjoining Best from placing or maintaining Witt in a position that would pose an inherent threat of disclosure or use of FMC’s trade secrets. *Id.* at 505.

In *Weed Eater, Inc. v. Dowling*, a former employee of the plaintiff was enjoined from working for a competitor who manufactured and developed lawn and garden products. The defendant was a former vice president of manufacturing who had designed and organized an assembly line for the production of string-line trimmers. He left the plaintiff's employment to supervise an assembly line at a company that wanted to start producing the trimmers itself, rather than buy them from Weed Eater. The court found that prohibiting the defendant from using the plaintiff's trade secrets would be insufficient because the defendant inevitably would disclose his knowledge of the trade secrets if allowed to work in the same area of production. Thus, the court prohibited the defendant from working in any capacity relating to the manufacturing of trimmers. As the court reasoned:

Even in the best of good faith, Dowling can hardly prevent his knowledge of his former employer's confidential methods from showing up in his work. The only effective relief for Weed Eater is to restrain Dowling from working for Hawaiian Motor Company in any capacity related to the manufacture by Hawaiian Motor Company of a flexible line trimming device.

562 S.W.2d at 902.

In *Conley v. DSC Communications Corp.*, No. 05-98-01051-CV, 1999 WL 89955, at *3 (Tex. App.–Dallas Feb. 24, 1999, no pet.) (not designated for publication) the Dallas Court of Appeals adopted what might be viewed as a modified version of the inevitable disclosure doctrine, holding that enjoining an employee from using an employer's confidential information is appropriate when it is *probable* that the former employee will use the confidential information for his benefit (or his new employer's benefit) or to the detriment of his former employer. *Conley*, 1999 WL 89955, at *4 (emphasis in original); *see also Rugen*, 864 S.W.2d at 552 (“Rugen is in possession of IBS's confidential information and is in a position to use it. Under these circumstances, it is probable that Rugen will use the information for her benefit and to the detriment of

IBS.”); *Williams*, 704 S.W.2d at 471 (applying doctrine, but not by name). The court also rejected the notion that the new employer’s alleged efforts to protect against the disclosure or use of the ex-employer’s trade secrets defeated the ex-employer’s right to an injunction. As the court stated, “[w]e reject Conley’s suggested factor of the new employer’s efforts to protect the trade secrets of the former employer. At best, relying on the new employer to protect the trade secrets of the former employer when those trade secrets could work to the new employer’s advantage is little better than asking the fox to guard the henhouse. The richer the henhouse, the less wise it is to trust even the most responsible and reliable of foxes.” *Id.* at *6. Likewise, the court held that an injunction was proper notwithstanding the lack of proof of misconduct against the ex-employee, and the fact that there was no non-competition agreement.

In *Rugen*, 864 S.W.2d at 552, the court held that it was not an abuse of discretion to enter a temporary injunction against a former employee, a sales account manager, prohibiting the employee from using any confidential information obtained from her former employer to solicit or transact business with the employer’s consultants or customers, where the evidence indicated that the employee possessed confidential information of the employer and operated a firm in direct competition with employer, so it was “probable” that she would use the confidential information. The employee worked as an account manager for a personnel company providing computer consulting and contracting services. She left the former employer and started her own firm in the same business. The former employer sought an injunction against the employee to enforce a noncompetition agreement she had signed, and to prevent her from using confidential information she had gained while working for the former employer. The trial court determined that the noncompetition agreement was unenforceable, but enjoined the employee from calling on, soliciting, or transacting business with consultants employed or retained by the former employer or customers of the former employer, and from using confidential business information, methods, and trade secrets that she learned while employed by the former employer. The court recognized that an injunction was

appropriate when necessary to prohibit an employee from using confidential information to solicit the former employer's clients. The employee argued that the injunction should not have been granted because the evidence did not show that she had wrongfully used and would continue to so use any confidential information. However, the court found evidence indicating that the employee possessed confidential information of the former employer and operated a firm in direct competition with the former employer. She was in possession of the former employer's confidential information and was in a position to use it. Under these circumstances, the court found it probable that the employee would use the information for her benefit and to the detriment of the former employer. The court noted that at times, an injunction was the only effective relief that an employer had when a former employee possessed confidential information, and it did not believe that the trial court abused its discretion by granting the temporary injunction.

In *Cardoni*, 805 F.3d at 589–90, the Fifth Circuit found that cases like *FMC Corp.*, *Weed Eater*, and *Rugan* did not adopt a blanket rule that Texas law always presumes there will be improper disclosure of trade secrets where a departing employee has been exposed to trade secrets. Rather, according to *Cardoni*, those cases found on their specific facts that such disclosure either had occurred, or was likely to occur, absent an appropriate injunction. *Id.* at 589-90.

C. What Factual Factors Militate Towards Application Of The So-Called “Inevitable Disclosure” Doctrine, Or Its Equivalent?

As mentioned, the TUTSA does not address the inevitable disclosure doctrine. *See supra*. From an analysis of the above-referenced cases in this area, it appears that an inevitable disclosure doctrine type of claim is most likely to be accepted by a Texas court when:

- An employer targets specialized employees for hire specifically because the employer is weak in the technology areas and needs to obtain talent from competitors to catch up. *Compare Cardinal Health Staffing Network, Inc.*, 106 S.W.3d at 241-42 (declining to apply the inevitable disclosure doctrine,

in part because the new employer had devised a business plan for its own interim pharmacy staffing business over a year before it hired the plaintiff's ex-employee and it was clear that the new employer would have started this business with or without him) *with FMC Corp.*, 677 F.2d at 505 (applying doctrine because plaintiff company had clearly superior product that it invested in heavily and the company that hired plaintiff's ex-employee was far behind in technology). *But see Conley*, 1999 WL 89955, at *4-5 (noting that this type of evidence is not required in all cases to support the imposition of the inevitable disclosure doctrine).

- The case involves research and product development employees – the key employees a company relies on to develop and refine valuable new technologies and give it a competitive edge. *See FMC Corp.*, 677 F.2d at 505 (applying doctrine because plaintiff company had clearly superior product in which it invested \$85 million dollars, and took extraordinary steps to protect its secrecy).
- The case involves an employee who went to work for a company that will become more competitive in the at-issue technology areas more quickly because it hired the employee. *Weed Eater, Inc.*, 562 S.W.2d at 902 (relying on same proof in granting injunctive relief).
- The company the employee went to work for has rejected requests to describe the employee's duties or to ensure the ex-employer's confidential information will not be utilized. *See Spicer*, 2006 WL 1751786 at *9-11 (relying on the fact that the new employer had done nothing to ensure that the former employer's confidential information would not be used by the defendant in applying the legal equivalent of the inevitable disclosure doctrine); *FMC Corp.*, 677 F.2d at 504 (same). Note: Even when the new employer has taken such efforts, some courts still apply the inevitable disclosure doctrine. *See Conley*, 1999 WL 89955, at *6 (noting that “the

richer the henhouse, the less wise it is to trust even the most responsible and reliable of foxes”).

- The facts show the employee’s duties are significantly the same or similar at their new employer as they were at their former employer. *Conley*, 1999 WL 89955, at *5 (noting that this type of evidence is relevant to support the imposition of the inevitable disclosure doctrine).
- The employee could easily memorize his or her ex-employer’s confidential information and trade secrets. *See Spicer*, 2006 WL 1751786 at *9-11 (relying on such evidence in applying the legal equivalent of the inevitable disclosure doctrine); *Williams*, 704 S.W.2d at 471 (noting that plaintiff’s ex-employee testified that he “had a photographic memory and is able to observe the way something is made and then copy it” in applying doctrine).
- The new employer refuses to acknowledge that the information is a trade secret – so that any promise not to use or disclose confidential or trade secret information is not truly an effective protection for the former employer. *See FMC Corp.*, 677 F.2d at 505 (applying inevitable disclosure doctrine partially because the new employer argued that some information that was clearly a trade secret was not and, therefore, “without the injunction, Witt [the ex-employee] may, out of ignorance of what information constitutes a trade secret, reveal the confidential matters FMC seeks to protect”).
- The former employee worked on projects in specific technology areas for their former employer that they are now working in for their new employer. *Conley*, 1999 WL 89955, at *4-5 (noting that this type of evidence tends to support the imposition of the inevitable disclosure doctrine).
- The fact that the former employer would not know for years if the former employee’s use of its trade secrets has resulted in harm helps prove

irreparable harm. *See Williams*, 704 S.W.2d at 471 (relying upon same evidence in similar case to enjoin plaintiff's former manufacturing manager).

- The information and expertise that the ex-employee took with him or her (if even just in his or her head) regarding the technology areas are: (a) information the employee must have to do his or her job with his or her new employer; and (b) truly the former employer's trade secrets, not general concepts and information that are publicly available. *See Cardinal Health Staffing Network, Inc.*, 106 S.W.3d at 241-42 (declining to apply the inevitable disclosure doctrine, in part because the information that the plaintiff's ex-employee needed to develop business contacts for the new employer was available publicly).
- Note that proof of misconduct or wrongdoing by the ex-employee is not required under Texas case law, though it is helpful. *See Conley*, 1999 WL 89955, at *4-5 (noting that proof of ex-employee's misconduct is helpful to a plaintiff seeking an injunction based on inevitable disclosure, but it is not required in all cases); *FMC Corp.*, 677 F.2d at 504 (applying doctrine without proof of actual misappropriation).

III. UPDATE ON COVENANTS NOT TO COMPETE LAW IN TEXAS

A. Requirements Of An Enforceable Noncompetition Agreement In Texas

A noncompetition covenant's enforceability is ultimately a question of law for the court. *Light v. Centel Cellular Co. of Texas*, 883 S.W.2d 642, 644 (Tex. 1994). To be enforceable, a noncompetition covenant must: (1) be ancillary to an otherwise enforceable agreement at the time that the agreement is made; and (2) contain limitations of time, geographic area, and scope of activity that are reasonable and that do not impose greater restraint than necessary to protect the company's goodwill or other business interests. TEX. BUS. & COM. CODE ANN. § 15.50 (Vernon 2002). The Court must find only one non-illusory promise to support a noncompetition agreement. *Ireland v.*

Franklin, 950 S.W.2d 155, 158 (Tex. App.–San Antonio 1997, no pet.). Both of these two requirements are discussed below.

1. Ancillary To An Otherwise Enforceable Agreement

a. In General

In *Light*, a case decided in 1994, the Texas Supreme Court held that a covenant not to compete is “ancillary to or part of” an otherwise enforceable agreement at the time it was made if: (a) the consideration given by the employer in that agreement gives rise to the employer’s interest in restraining the employee from competing; and (b) the covenant is designed to enforce the employee’s consideration or return promise in that agreement. *Light*, 883 S.W.2d at 647; *see also Alex Sheshunoff Mgmt Servs., L.P. v. Johnson*, 209 S.W.3d 644, 648-51 (Tex. 2006).¹ In 2011, the Texas Supreme Court rejected the “gives rise to the employer’s interest in restraining the employee from competing” requirement set out in *Light*, stating that “there is no compelling logic in *Light’s* conclusion that consideration for the otherwise enforceable agreement gives rise to the interest in restraining the employee from competing.” *Marsh USA Inc. v. Cook*, 354 S.W.3d 764, 775 (Tex. 2011). Rather, it held, the proper test is whether the consideration given by the employer merely is “reasonably related to,” an “interest worthy of protection.” *Id.* at 774-76.

The clearest type of consideration that satisfies the first requirement is an employer’s promise to give an employee confidential information or trade secrets in exchange for the employee’s promise not to disclose such information. *Light*, 883 S.W.2d at 647 fn. 14.² “[B]usiness goodwill and confidential or proprietary information” are examples of interests that warrant protection by a non-compete covenant. *Sheshunoff*,

¹ Note: non-solicitation of customer agreements are subject to the same analysis as covenants not to compete. *See Miller Paper Co. v. Roberts Paper Co.*, 901 S.W.2d 593, 600 (Tex. App.–Amarillo 1995, no writ) (stating that “other than the moniker assigned it, nothing truly differentiates the [non-solicitation] promise at bar from a covenant not to compete”).

² In the aforementioned 2011 *Marsh USA Inc.* decision, the Texas Supreme Court also found that stock options can provide sufficient consideration. That decision is discussed in greater detail below.

209 S.W.3d at 649. *See also Curtis v. Ziff Energy Group, Ltd.*, 12 S.W.3d 114, 118 (Tex. App.–Houston [14th Dist.] 1999, no pet.) (finding a noncompete covenant ancillary to an otherwise enforceable agreement where “the covenant not to compete [was] designed to enforce [the employee’s] consideration not to disclose or use the confidential information or trade secrets after employment”); *Ireland*, 950 S.W.2d at 158 (finding a noncompete covenant ancillary to an otherwise enforceable agreement where “the covenant not to compete [was] designed to enforce [the employee’s] consideration not to disclose or use . . . trade secrets”).

A wide variety of confidential information can satisfy this first requirement, and give rise to an interest worthy of protection through a non-compete agreement. For example, knowledge of a unique customer base and knowledge of the equipment or products used by each of the employer’s customers are protectable interests. *See Stone v. Griffin Comm. & Security Systems, Inc.*, 53 S.W.3d 687, 694 (Tex. App.–Tyler 2001, no pet.). Likewise, information concerning acquisition strategies, compensation and benefits formulas, and payment rates may be considered confidential information that is protectable through a non-compete. *See TransPerfect Translations, Inc. v. Leslie*, 594 F. Supp. 2d 742, 754 (S.D. Tex. 2009); *Teel v. Hospital Partners of America, Inc.*, No. H-06-cv-3991, 2008 WL 346377, *7 (S.D. Tex. Feb. 6, 2008). The information need not be a trade secret: “Moreover, a covenant not to compete is enforceable not only to protect trade secrets but also to protect proprietary and confidential information.” *Gallagher Healthcare Ins. Services v. Vogelsang*, 312 S.W.3d 640, 652 (Tex. App.–Houston [1st Dist.] 2009, pet. denied) (citing *Light*, 883 S.W.2d at 647 n. 14). “Customer information is a legitimate interest which may be protected in an otherwise enforceable covenant not to compete.” *Id.* (citations omitted).

After *Light*, the courts struggled with the question of whether the employer had to give the employee the confidential information at the very moment the employee signed the non-compete agreement for the agreement to be enforceable. In 2006, the Texas Supreme Court resolved that question in a pro-enforcement fashion. It held that non-

compete covenants can be considered unilateral contracts, made at the time a non-compete is signed, that become binding once an employer provides the employee confidential information. *Sheshunoff*, 209 S.W.3d at 651. *Sheshunoff* overruled *Light*, which had interpreted § 15.50 to require that the non-compete covenant must be supported by a valid promise and actual performance at the very time the agreement is made. Under *Sheshunoff*, employers may enforce non-compete agreements even if they do not provide the employee with the confidential information until days, weeks, months, or even years after the agreements are executed. If, however, such information is never provided, then the noncompete agreement is not enforceable. See, e.g., *Digital Generation, Inc. v. Boring*, NO. 3:12-CV-00329-L, 2012 WL 1413386, at *10 (N.D. Tex. Apr. 24, 2012) (finding noncompete unenforceable where employer did not prove that it gave employee confidential information after he signed the noncompetition agreement).

After *Sheshunoff*, yet another question remained: must the employer's agreement to provide confidential information to the employee be express, or may it be implied? In 2009, the Texas Supreme Court resolved that question in a pro-enforcement way, and held that such a promise may be express or implied. See *Mann Frankfort Stein & Lipp Advisors, Inc. v. Fielding*, 289 S.W.3d 844 (Tex. 2009). Regarding implied promises, in *Mann Frankfort* the Court concluded that a non-compete agreement is enforceable even if the employer does not expressly promise to provide the employee with any confidential information in the non-competition agreement, so long as: (a) the employee promises not to disclose or use the employer's confidential information; and (b) the nature of the contemplated employment will reasonably require the employer to furnish the employee with confidential information. In such an instance, the court held that an employer impliedly promises to provide the employee confidential information. In that case, Mann Frankfort required the defendant to sign an agreement promising not to disclose any confidential information he obtained during his employment. It then provided the defendant access to its client database, containing clients' names, billing information, and tax and financial information, which constitute confidential information. The court found

that Mann Frankfort provided sufficient consideration to support a non-disclosure agreement and, thus, the non-competition agreement was ancillary to or part of an otherwise enforceable agreement under the typical “employer promises to give employee confidential information or trade secrets and in return employee promises not to disclose such information” analysis set out in footnote 14 of *Light*. See *Light*, 883 S.W.2d at 647 fn. 14. Since *Mann Frankfort* has been decided, several courts have enforced non-competition agreements, applying its holding that even an employer’s implied agreement to provide an employee with trade secrets or confidential information can support a non-competition agreement. See, e.g., *Gallagher Healthcare Ins. Services*, 312 S.W.3d at 650-51 (decision enforcing non-compete agreement under *Mann Frankfort* standard); *York v. Hair Club for Men, L.L.C.*, No. 01-09-00024-CV, 2009 WL 1840813 (Tex. App.–Houston [1st Dist.] June 25, 2009, no pet.) (unpublished) (same).

Mann Frankfort has its limits, however. For example, if the noncompete agreement does not mention confidential information or trade secrets at all – i.e. is merely a stand alone noncompete – then *Mann Frankfort* does not apply and the agreement is unenforceable (assuming no other form of valid consideration, such as specialized training or stock options supports it). See *Hunn v. Dan Wilson Homes, Inc.*, 789 F.3d 573, 586 (5th Cir. 2015) (finding noncompete invalid because it was devoid of any reference to confidential information or trade secrets).

Another form of consideration that can support a noncompete is specialized training. *Neurodiagnostic Tex, L.L.C. v. Pierce*, NO. 12-14-00254-CV, 2016 WL 6426830, at *6 __ S.W.3d __ (Tex.App.–Tyler Oct. 31, 2016). In this case, the court defined “specialized training” as follows:

“Specialized” training is training that “concentrate[s] on a particular activity or product” or training by which a person is “develop[ed] so as to become adapted to a specific environment or function.” THE AMERICAN HERITAGE DICTIONARY 1172 (2nd College Ed. 1982). The definition of the word “specialized” does not indicate that the information or methods imparted to the employee must be confidential or proprietary. See *id.* But neither does it include the type of training that is commonplace or typical in

an industry. *See id.*; *see also, e.g., Lazer Spot, Inc.*, 387 S.W.3d at 49 n.15 (citing *Evan’s World Travel, Inc. v. Adams*, 978 S.W.2d 225, 231 (Tex. App.–Texarkana 1998, no pet.) (general skills and knowledge, i.e., “housekeeping functions,” developed through course of employment not types of interests that justify protection under restrictive covenant)).

Id. at *6.

Applying this standard, the court found that the ex-employee had received “specialized training” sufficient to support his noncompete agreement, stating, “[t]he summary judgment record reflects that NeuroTex expended its resources for Pierce to receive training and knowledge, which enabled him to receive two additional board certifications. As a result, he was qualified to apply his skillset in an operatory setting. Moreover, he was better at performing his job than he otherwise would have been had he not received these two additional certifications.” *Id.*

Finally, it should be noted that the mere fact that an employee is employed at-will does not invalidate a noncompetition agreement. *See Jon Scott Salon, Inc. v. Garcia*, 343 S.W.3d 532, 535 (Tex. App.–Dallas 2011, no pet.) (“Because *Sheshunoff* specifically states a covenant not to compete made part of an employment at-will agreement may be enforceable, the trial court in this case erred in concluding otherwise.”).

b. Stock Options Recognized As Sufficient To Support A Noncompetition Agreement

In 2011, the Texas Supreme Court held that stock options given in consideration for a noncompete agreement were reasonably related to the employer’s interest in protecting its goodwill and could support a noncompetition agreement. *Marsh USA Inc. v. Cook*, 354 S.W.3d 764, 774-76 (Tex. 2011). Texas Supreme Court rejected language from its decision in *Light* by holding that consideration for a covenant not to compete need not “give rise” to the employer’s interest in restraining the employee from competing. *Id.* In doing so, the court ruled by a 6-3 majority that stock options granted to a valuable employee are sufficient consideration to support a post-employment restrictive covenant because they are “reasonably related” to the company’s interest in

protecting its goodwill. As it did in its *Sheshunoff* decision in 2006, the court again sent a strong signal to lower courts that in analyzing noncompetition agreements, the primary focus is whether or not the covenant is reasonable, not whether the agreement passes muster under a highly technical analysis not contemplated by the Texas Legislature.

Marsh involved a former managing director of Marsh USA Inc., a risk management and insurance business. According to the company, the director was a “valuable employee who had successfully performed at his position,” and had both attracted and retained business for the company. During the director’s employment, and to encourage further good performance, Marsh offered him options to purchase 500 shares of stock in Marsh’s parent company. The options vested in increments and fully vested after four years. Upon exercise of the options, the director was required to sign a non-solicitation agreement in which he promised that if he left the company within three years after exercising the options, he would not solicit certain company clients or certain employees for a period of two years.

In attempting to enforce these promises after the director left the company, the company argued that the stock options were sufficient consideration because they furthered the company’s “goodwill,” which is specifically listed as protectable interest under the Texas Covenants Not to Compete Act, TEX. BUS. & COMM. CODE § 15.50, but which had received very little attention from the courts until this case.

The appellate court in *Marsh* had held that stock options and similar financial incentives were not sufficient consideration because, unlike confidential information or specialized training, mere financial consideration does not “give rise to the employer’s interest in restraining the employee from competing.” The Supreme Court held that this was the wrong test to apply, and thus overruled a portion of its prior decision in *Light v. Centel Cellular Co. of Texas* setting out this test. Instead, the *Marsh* Court held, the proper test is whether the consideration merely gives rise to, or is “reasonably related to,” an “interest worthy of protection.” *Marsh USA Inc.*, 354 S.W.3d at 774-76. Under this test, the Court found, stock options were sufficient consideration because they made the

employee an “owner” of the company and linked his interests with the company’s long-term business interests, including the development of solid, long-term customer and employee relationships. Thus, the stock options furthered the company’s goodwill, which is expressly an “interest worthy of protection.” The Court stressed, however, that the “hallmark” of enforcement was whether the particular restrictions at issue are reasonable and do not impose greater restraints than necessary to protect the employer’s interests. *Id.* at 777. The Court did not attempt to determine whether the particular restrictions at issue in this case were reasonable, but sent the case back to the trial court to make this determination.

As the three dissenting Justices pointed out, the Court’s opinion in *Marsh* leaves unclear what other forms of financial benefit create sufficient business goodwill. The majority opinion could conceivably be read to suggest that *any* form of financial consideration to any employee – such as a bonus, promotion, or even payment of a salary – could further business goodwill, and thus satisfy the majority’s test. The majority does not directly address this point, except perhaps to explain that stock options generally further goodwill because they are designed to give the employee a greater stake in the company’s performance and in its long-term relationships with customers and employees, and to note that the employee at issue was a valued high-level employee who had already been successful in developing customer relationships. It is thus possible that other fact patterns involving stock options may not necessarily be sufficient to support a noncompetition agreement. It will take further court decisions to sort out these and other open questions after *Marsh*.

Note that the Texas Supreme Court’s ruling was consistent with the Houston First Court of Appeals decision in *Totino v. Alexander & Assocs., Inc.*, No. 01-97-01204-CV, 1998 WL 552818, (Tex. App.–Houston [1st Dist.] Aug. 20, 1998, no pet.) (not designated for publication). In *Totino*, the Houston First Court of Appeals found that stock options involved an interest worthy of a competitive restraint. In that case, the evidence showed that the stock options awards were offered in recognition of the employee’s contributions

to the employer's business, were one part of a long-term employee incentive plan, and were meant to reaffirm management's commitment to linking employee interests to those of the company's shareholders. In other words, the options were offered to encourage the employee's loyalty and continued employment. The *Totino* court held that this interest may be protectable through a competitive restraint, and upheld the noncompetition covenant as "ancillary to" the stock option agreement. *See Totino*, 1998 WL 552818, at *7.

2. **The Agreement Contains Limitations Of Time, Geographic Area, And Scope Of Activity That Are Reasonable And That Do Not Impose Greater Restraint Than Necessary To Protect The Employer's Goodwill Or Other Business Interest**

a. **In General**

The noncompetition provision must also contain limitations of time, geographic area, and scope of activity that are reasonable and that do not impose greater restraint than necessary to protect the employer's goodwill or other business interest. TEX. BUS. & COM. CODE ANN. § 15.50 (Vernon 2002). In determining the reasonableness of a noncompetition agreement's restraints, the court is to consider the restraints "in combination with one another, rather than as stand alone requirements. *M-I LLC v. Stelly*, 733 F. Supp. 2d 759, 799 (S.D. Tex. 2010).

Regarding time, a non-competition agreement of one or two years is typically reasonable under Texas law, and some courts also find much longer time periods reasonable. *See, e.g., Gallagher Healthcare Insurance Services*, 312 S.W.3d at 655 ("[t]wo to five years has repeatedly been held as a reasonable time [limitation,]"); *Stone*, 53 S.W.3d at 696 (upholding a five year restraint and stating that "two to five years has repeatedly been held a reasonable time restriction in a non-competition agreement.") (citing *AMF Tuboscope v. McBryde*, 618 S.W.2d 105, 108 (Tex. Civ. App.—Corpus Christi 1981, writ ref'd n.r.e.), citing *Arevalo v. Velvet Door, Inc.*, 508 S.W.2d 184 (Tex. Civ. App.—El Paso 1974, writ ref'd n.r.e.); *Electronic Data Systems Corp. v. Powell*, 508

S.W.2d 137 (Tex. Civ. App.–Dallas 1974, writ ref'd n.r.e.); *Weber v. Hesse Envelope Co.*, 342 S.W.2d 652 (Tex. Civ. App.–Dallas 1960, no writ)).

Texas courts generally require some geographic limitation in a valid covenant not to compete. *See, e.g., Goodin v. Jolliff*, 257 S.W.3d 341, 352 (Tex. App.–Fort Worth 2008, no pet.) (citing cases); *Zep Mfg. Co. v. Harthcock*, 824 S.W.2d 654, 660-61 (Tex. App.–Dallas 1992, no pet.). “A reasonable geographic scope is generally considered to be the territory in which the employee worked for the employer.” *TransPerfect Translations, Inc.*, 594 F. Supp. 2d at 754 (citing *Harthcock*, 824 S.W.2d at 660); *see also Cobb v. Caye Publ’g Grp., Inc.*, 322 S.W.3d 780, 783–84 (Tex. App.–Fort Worth 2010, no pet.) (“Generally, a reasonable area for purposes of a covenant not to compete is considered to be the territory in which the employee worked while in the employment of [her] employer.”). “[N]on-compete covenants with restrictions covering a wide geographic area may be reasonable if they are limited in scope to a firm’s current or prospective clients such that they do not pose a greater restraint than necessary to protect the firm’s goodwill.” *TransPerfect Translations, Inc.*, 594 F. Supp. 2d at 754 (citing cases). Covenants with wide geographic areas have been upheld frequently in Texas courts, especially when the area covered constitutes the employee’s actual sales or work territory. *See, e.g., Vais Arms, Inc. v. Vais*, 383 F.3d 287, 295 (5th Cir. 2004).

A reasonable restriction on scope of activity can substitute for a geographic restriction, even absent a geographic restriction – for example, limiting the employee from contacting customers he or she had contact with during a reasonable time frame before he or she left his or her employer is generally reasonable and enforceable. *See, e.g., Sheshunoff*, 209 S.W.3d at 657 (holding covenant prohibiting employee from soliciting or providing services to employer’s clients for period of one year following termination reasonable); *Gallagher Healthcare Ins. Services*, 312 S.W.3d at 654-55 (restraints tied to employee’s own work at the prior employer are reasonable); *Drummond American, LLC v. Share Corp.*, 692 F. Supp. 2d 650 (E.D. Tex. 2010) (enforcing restriction prohibiting employees from calling on any customer of theirs from whom they

solicited orders or to whom they sold competitive products on behalf of the company during the last year of their employment for a period of two years following termination of their employment).

On the other hand, extremely broad restraints likely are unenforceable. *See Weatherford Oil Tool Co. v. Campbell*, 340 S.W.2d 950, 951-52 (Tex. 1960) (geographic scope described as “any area where Weatherford Oil Tool Company, Inc., may be operating or carrying on business” held overbroad); *McNeilus Companies, Inc. v. Sams*, 971 S.W.2d 507, 511 (Tex. App.—Dallas 1997, no writ) (holding covenant prohibition on former employee from working “in any capacity” for competitor of former employer was overbroad in scope); *Recon Exploration, Inc. v. Hodges*, 798 S.W.2d 848, 853 (Tex. App.—Dallas 1990, no writ) (non-competition covenant prohibiting employment in any business of type and character engaged in and competitive with former employer presented question of reasonableness); *cf. Butler v. Arrow Mirror & Glass, Inc.*, 51 S.W.3d 787 (Tex. App.—Houston [1st Dist.] 2001, no pet.) (“Restraints are ‘easier to justify if . . . limited to one field of activity among many that are available to the employee”). “The Texas Supreme Court has held that an industry-wide exclusion is unreasonable.” *John R. Ray & Sons, Inc. v. Stroman*, 923 S.W.2d 80, 85 (Tex. App.—Houston [14th Dist.] 2010, no pet.), *citing Peat Marwick Main & Co. v. Haass*, 818 S.W.2d 381, 386-88 (Tex. 1991).

In the context of sales employees, “a covenant not to compete that extends to clients with whom a salesman had no dealings during his employment is unenforceable.” *Wright v. Sport Supply Group, Inc.*, 137 S.W.3d 289, 292 (Tex. App.—Beaumont 2004, no pet.). In other words, “[i]n the case of covenants applied to a personal services occupation, such as that of a salesman, a restraint on client solicitation is overbroad and unreasonable when it extends to clients with whom the employee had no dealings during his [or her] employment.” *John R. Ray & Sons, Inc.*, 923 S.W.2d at 85; *EMS USA, Inc. v. Shary*, 309 S.W.3d 653 (Tex. App.—Houston [14th Dist.] 2010, no pet.) (“A restraint on client solicitation in a personal services contract is overbroad and unreasonable if it

extends to clients with whom the employee had no dealings during his employment.”) (citation omitted); *Poole v. U.S. Money Reserve, Inc.*, No. 09-08-137CV, 2008 WL 4735602, at *8 (Tex. App.—Beaumont Oct. 30, 2008) (mem. op., not designated for publication); *Daytona Group of Tex., Inc. v. Smith*, 800 S.W.2d 285, 288 (Tex. App.—Corpus Christi 1990, writ denied). In *SafeWorks, LLC v. Max Access, Inc.*, No. H-08-2860, 2009 WL 959969, at *5 (S.D. Tex. Apr. 8, 2009), Judge Nancy Atlas found that such an overbroad restraint on salespersons was unenforceable as a matter of law.

Where the employee at-issue is not merely a salesperson, however, the above-mentioned rule does not necessarily apply. For example, in *M-I LLC v. Stelly*, 733 F. Supp. 2d 759 (S.D. Tex. 2010), Judge Keith Ellison reviewed a non-compete agreement that prohibited the employee from all contact with his former employer’s customers, not merely the customers he had dealings with. *Id.* at 798. Nevertheless, Judge Ellison upheld the non-compete agreement, stating:

Three important factors bring the Court to this conclusion. First, the short six-month duration of the covenant not to compete imposes a limited burden on Knobloch. During that six-month period, Knobloch still had several options: he could have chosen to work outside the wellbore completion industry, to work in that industry but outside of the Americas, or not to work and launch a competing business six months later. The Court is convinced that, given Knobloch’s scientific background and in-depth knowledge of the industry, all of those options remained open to him when he left his employment with SPS/GCS.

The second factor is the upper management position held by Knobloch at SPS/GCS. M-I has submitted evidence showing that Knobloch was much more than a manager and salesman for his former employer. He oversaw SPS/GCS’s relationships with major international clients. (Knobloch Dep. 85:15-86:25; Doc. No. 196, Exs. 25-27.) An engineer by training, Knobloch participated in the design of SPS/GCS’s tools and in facilitating

wellbore completions. He delivered technical presentations internationally, formulated company growth strategies, and discussed product development with engineers. (Doc. No. 196, Ex. 16.) Given Knobloch's high level of involvement in the company's growth and development, the Court believes that restricting him from contacting SPS/GCS's customer base was reasonable.

The third, and perhaps most important, factor goes to SPS/GCS's protectable interest. Texas courts are generally concerned about customer contract restrictions where the client base is the protectable business interest. *See, e.g., Peat Marwick Main & Co. v. Haass*, 818 S.W.2d 381, 387 (Tex. 1991) (defining the business interest in that case to include preserving the firm's client base). M-I has made a strong case that the business interest in this case extends beyond SPS/GCS's client base, given Knobloch's intimate knowledge of tool designs and functionality. Knobloch had access to sensitive company information, including many trade secrets. The Court is convinced that the definable business interests in this case involve not just preserving a client base, but also maintaining trade secrets and other sensitive information. The restriction on all customer contact is accordingly not an unreasonable restraint of trade as to this particular employee. *See Weed Eater, Inc. v. Dowling*, 562 S.W.2d 898, 902 (Tex. Civ. App.–Houston [1st Dist.] 1978, writ ref'd n.r.e.).

Id. at 798-800.

In reaching his decision in *M-I LLC*, Judge Ellison relied on *Curtis v. Ziff Energy Group*. That case also teaches that a combination of factors, including the high rank of the departing employee and unique aspects of the industry involved, may make a seemingly overbroad non-competition agreement reasonable and enforceable. In *Curtis*, the employee worked for the employer as the Vice President of Pipelines and Energy Marketing. The relevant covenant not to compete prohibited the employee from

engaging in competitive business in Canada or the United States. In the ensuing litigation over the covenant's enforceability, the employee claimed that he was restricted from working for any oil and gas company in North America. The employer disagreed, and submitted evidence to show the court that it limited its competitors to twenty companies, which were comprised of oil and gas consulting firms. 12 S.W.3d at 119. The Court sided with the employer, holding that, based on the employee's "job description and responsibilities, it was reasonable to restrict [him] from working in other oil and gas consulting firms in North America for a six month period." *Id.* (citing *Weed Eater, Inc. v. Dowling*, 562 S.W.2d 898, 902 (Tex. Civ. App.—Houston [1st Dist.] 1978, writ ref'd n.r.e.). *See also Daily Instruments Corp. v. Heidt*, 998 F. Supp. 2d 553 (S.D. Tex. 2014) (granting ex-employer's motion for preliminary injunction in a noncompete case involving a high level manager like and broadly prohibiting the ex-employee from working for a competitor in numerous countries); *AmeriPath, Inc. v. Hebert*, 447 S.W.3d 319, 335 (Tex.App.—Dallas 2014, pet. denied) (upholding broad geographic restriction beyond area where the defendant had worked for the plaintiff, because the defendant had been a high level manager and therefore the plaintiff's "interest in limiting Hebert's competition grew out of not only his employment as a pathologist, but also his service as a member of appellants' highest level management team. For this reason, we do not discern the Noncompete's limitation as to Hebert's affiliation with pathology practices that operate in the Dallas area as overly broad geographically: even if Hebert were working for such a company in New York, for example, his management knowledge of and experience with appellants' Dallas-area operations would be valuable to his new employer.").

b. Reformation Of Overbroad Non-Compete Agreements

The Covenants Not to Compete Act provides procedures and remedies in actions to enforce covenants not to compete. Regarding reformation, it provides:

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....

TEX. BUS. & COM. CODE ANN. § § 15.51(c) (Vernon 2011).

Thus, instead of invalidating overbroad covenants not to compete, Texas courts reform them by revising the unenforceable provisions to those that would be reasonable under the circumstances. *See Butler*, 51 S.W.3d at 794 (reforming and then enforcing an overbroad non-compete agreement). Specifically, where a covenant not to compete is ancillary to a separate, enforceable agreement, but its limitations on time, geographic area, or scope of activity impose greater restraint than is necessary, the court must reform the covenant to make the restraints reasonable. *Evan’s World Travel, Inc. v. Adams*, 978 S.W.2d 225, 233 (Tex. App.–Texarkana, 1998, no pet.); *Am. Nat’l Ins. Co. v. Cannon*, 86 S.W.3d 801, 808 (Tex. App.–Beaumont 2002, no pet.). The court has the power to reform the agreement even if neither party pleads for reformation. *TransPerfect Translations, Inc.*, 594 F. Supp. 2d at 756. As one court stated in reforming an overbroad noncompetition agreement: “Section 15.51 requires a court to reform a non-compete agreement if it is unreasonably broad in scope. TEX. BUS. & COMM. CODE § 15.51(c).” *Alliantgroup, L.P. v. Feingold*, Civil Action No. H-09-0479, 2009 WL 1357209, at *1 (S.D. Tex May 11, 2009) (Rosenthal, J.).

Regarding the timing of reformation, some Texas state court appeals courts have stated that reformation is not appropriate at the temporary injunction stage. For example, in *Cardinal Health Staffing Network, Inc.*, 106 S.W.3d 238–39 the court stated that, “[r]eformation is generally a final remedy.” *See also Sentinel Integrity Solutions, Inc. v.*

Mistras Group, Inc., 414 S.W.3d 911, 920 (Tex. App.–Houston. [1st Dist.] 2013, pet. denied) (“Reformation pursuant to section 15.51 is a remedy to be granted at a final hearing, whether on the merits or by summary judgment, not as interim relief”); *Gray Wireline Serv., Inc. v. Cavanna*, 374 S.W.3d 464, 470 (Tex. App.–Waco 2011, no pet.) (same).

But, federal district courts in Texas have generally taken a different view. For example, in *TransPerfect Translations, Inc.*, Judge Ellison decided to reform the non-compete agreement and grant a preliminary injunction based on it. 594 F. Supp. 2d at 756. As he stated, “In light of this unsettled law, the Court will enter a limited injunction and reform the contract as necessary based on the current evidence, noting that any reformation or permanent injunction to be entered may differ from this temporary reformation based on arguments presented in the parties’ dispositive motions or at trial.” *Id.* In reforming the covenant, the court should take the individual circumstances of the case into account. *Am. Nat’l Ins. Co.*, 86 S.W.3d at 808. The court must then enforce the covenant as reformed. TEX. BUS. & COM. CODE § 15.51(c). For example, in *Inter/National Rental Ins. Services, Inc. v. Albrecht*, NO. 4:11-CV-00853, 2012 WL 4506140, at *6 (E.D. Tex. Mar 14, 2012), the court enforced a noncompetition agreement against a former salesperson, but reformed the agreement so that the plaintiff was not precluded from soliciting his former employer’s “active prospective customers.”

Section 15.51(c) “precludes a damages award for conduct prior to any necessary reformation of the scope of the covenant.” *Mann Frankfort*, 289 S.W.3d at 855 (Hecht, J., concurring); *see also SafeWorks*, 2009 WL 959969, at *5 (“If a court reforms a covenant not to compete in order to make it reasonable and enforceable, ‘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.’”) (quoting TEX. BUS. & COM. CODE § 15.51(c)); *Butler*, 51 S.W.3d at 796 (“Applying section 15.51 to this case, once the trial judge reformed the covenant, money damages were precluded. No damages can be awarded for breach prior to the reformation; after reformation, the

current injunction was in place preventing ReGlaze from competing with, and thus, harming Arrow.”). *See also Alliantgroup, L.P.*, 803 F. Supp. 2d at 621 (granting summary judgment against employer’s claim for monetary damages based on breach of non-compete because all of the conduct that caused the damages occurred prior to the court’s reformation of the overbroad non-compete); *Rimkus Consulting Group, Inc.*, 688 F. Supp. 2d at 673 (same).

B. Noncompetition Agreements Concerning Physicians

Special rules apply to noncompetition agreements concerning physicians. Specifically, sections 15.50(b) and (c) of the Texas Business and Commerce Code provide as follows:

(b) A covenant not to compete relating to the practice of medicine is enforceable against a person licensed as a physician by the Texas Medical Board if such covenant complies with the following requirements:

(1) the covenant must:

(A) not deny the physician access to a list of his patients whom he had seen or treated within one year of termination of the contract or employment;

(B) provide access to medical records of the physician’s patients upon authorization of the patient and any copies of medical records for a reasonable fee as established by the Texas Medical Board under Section 159.008, Occupations Code; and

(C) provide that any access to a list of patients or to patients’ medical records after termination of the contract or employment shall not require such list or records to be provided in a format different than that by which such records are maintained except by mutual consent of the parties to the contract;

(2) the covenant must provide for a buy out of the covenant by the physician at a reasonable price or, at the option of either party, as determined by a mutually agreed upon arbitrator or, in the case of an inability to agree, an arbitrator of the court whose decision shall be binding on the parties; and

(3) the covenant must provide that the physician will not be prohibited from providing continuing care and treatment to a specific patient or patients during the course of an acute illness even after the contract or employment has been terminated.

(c) Subsection (b) does not apply to a physician's business ownership interest in a licensed hospital or licensed ambulatory surgical center.

In *Greenville Surgery Center, Ltd. v. Beebe*, 320 S.W.3d 850, 853 (Tex. App.—Dallas 2010, no pet.), the Dallas Court of Appeals applied this section to invalidate a non-compete that did not comply with it, stating:

Section 15.50(b) outlines the situations in which a covenant not to compete is enforceable against a person licensed as a physician by the Texas State Board of Medical Examiners. Here, the record demonstrates the Doctors are licensed physicians. Section 15.50(b)(2) requires the covenant to include a buy-out provision if the covenant is to be enforceable against a physician. TEX. BUS. & COM. CODE ANN. § 15.50(b)(2). This buy-out clause requirement provides physicians with the unique opportunity to buy out their covenants that is not available to any other employee subject to a covenant. *See* Mike Kreager, *The Physician's Right in § 15.50(b) to Buy Out a Covenant Not to Compete in Texas*, 61 *Baylor L.Rev.* 357, 419 (Spring 2009). The covenant before us, however, contains no buy-out clause as required by section 15.50(b)(2). Therefore, the covenant is unenforceable against the Doctors. *See Gulf Coast Cardiology Group, P.A., v. Samman*, No. 09-02-009-CV, 2002 WL 1877175 (Tex. App.—

Beaumont Aug. 15, 2002, pet. denied) (physician’s covenant not to compete was unenforceable since it did not contain a buy-out provision).

See also LasikPlus of Tex., P.C. v. Mattioli, 418 S.W.3d 210, 216 (Tex. App.–Houston [14th Dist.] 2013, no pet.) (ophthalmologist’s covenant not to compete was unenforceable since it did not contain a buy-out provision).

C. Non-compete Agreements In The Context Of A Sale Of A Business

A non-compete signed by an owner selling a business is quite different than one signed by an employee. *Marsh USA Inc.*, 354 S.W.3d at 790 n.5 (noting that section 15.50 does not address the “distinction between what type of agreement is enforceable to protect goodwill in the context of the sale of a business and the context of a post-employment restriction”); *Hill v. Mobile Auto Trim, Inc.*, 725 S.W.2d 168, 177 (Tex. 1987) (Gonzalez, J., dissenting) (noting that courts “scrutinize covenants not to compete in employment relationships more closely than covenants not to compete associated with the sale of a business”), *superseded by statute*, TEX. BUS. & COM. CODE § 15.50(a). Courts have been more inclined to enforce a long or limitless time period barring competition after a sale of a business. *See, e.g., Oliver v. Rogers*, 976 S.W.2d 792, 801 (Tex. App.–Houston [1st Dist.] 1998, pet. denied) (holding that a lack of a time limitation did not render non-compete unreasonable as a matter of law); *Greenstein v. Simpson*, 660 S.W.2d 155, 159 (Tex. App. – Waco 1983, writ ref’d n.r.e.) (“[A] person may agree [] in connection with the sale of his business[] not to re-enter a similar competitive business for the remainder of his life.”); *York v. Dotson*, 271 S.W.2d 347, 348 (Tex. Civ. App.–Fort Worth 1954, writ ref’d n.r.e.) (“One may lawfully agree not to compete in a particular business, in a reasonably limited territory, during the remainder of his life. Such contracts are held not to be in restraint of trade.”); *Clay v. Richardson*, 290 S.W. 235, 236 (Tex. Civ. App.–Fort Worth 1926, writ dism’d w.o.j.) (upholding covenant of theater seller never to open a theater again in town where theater was located).

In the context of the sale of a business, Texas courts extend a non-compete to a non-signatory in two scenarios: (1) an entity is created by a signatory for the purpose of

competing to circumvent, or perpetuate a “fraud” on, the non-compete, *see Texas Shop Towel, Inc. v. Haire*, 246 S.W.2d 482, 484 (Tex. Civ. App.–San Antonio 1952, no writ), or (2) a signatory significantly aids, abets, consults, or advise another entity or person’s competition with the buyer when the non-compete forbids aiding, abetting, consulting or advising. *See Barrett v. Curtis*, 407 S.W.2d 359, 362 (Tex. Civ. App.–Dallas 1966, no writ); *Pitts v. Ashcraft*, 586 S.W.2d 685, 692 (Tex. Civ. App.–Corpus Christi 1979) (“[T]he covenantor must also undertake a more active participation in the competing enterprise, such as giving the competitor the benefit of his experience, knowledge, and/or influence to assist the competitor in the conduct of his competing business;” mere financial assistance is not enough.).

D. Non-compete Agreements That Do Not Bar Competition, But Rather Impose Monetary Penalties For Competing

The rules regarding the enforceability of noncompetition agreements also apply to agreements that do not expressly prohibit a former employee from competing, but instead impose a severe economic penalty on the departing employee if he engages in competition. *See Peat Marwick*, 818 S.W.2d at 388 (“We hold that provisions clearly intended to restrict the right to render personal services are in restraint of trade and must be analyzed for the same standards of reasonableness as covenants not to compete to be enforceable.”). *See also Frankiewicz v. Nat’l Comp Assocs.*, 633 S.W.2d 505, 507 (Tex. 1982) (holding that an agreement forfeiting renewal commissions in the event of competition is a restraint on trade and is unenforceable unless the restrictions are reasonable). The reason is as follows:

If the damages provided are sufficiently severe, then the economic penalty’s deterrent effect functions as a covenant not to compete as surely as if the agreement expressly stated that the departing member will not compete. The practical and economic reality of such a provision is that it inhibits competition virtually the same as a covenant not to compete.

Haass, 818 S.W.2d at 385–86.

In *Exxon Mobil Corp. v. Drennen*, 452 S.W.3d 319 (Tex. 2014), the Texas Supreme Court distinguished cases where employers imposed penalties for competition from ones where employers merely withheld a purely gratuitous benefit. In *Drennen*, the plaintiff worked for Exxon for 31 years. In August 2007, he tendered his retirement papers. During his employment, Drennen participated in Exxon's Incentive Program that awarded restricted stock awards and bonuses to reward high-performing employees and to dissuade high-achieving executive-level employees from leaving Exxon to work for competitors. At his retirement, Drennen had 73,900 shares (approximately \$6.2 million) of Exxon stock through the Incentive Program.

The Incentive Program allowed Exxon to cancel the employee's awards if he engaged in "detrimental activity." Detrimental activity was defined, in relevant part, as the employee's acceptance of duties to a third party that creates or appears to create a material conflict of interest and includes becoming "employed or otherwise engaged by an entity that regulates, deals with, or competes with" Exxon. The Incentive Program provided that New York law would be used to govern the agreement. The program also lacked any restrictions as to time, geographic area or scope of activity that might constitute detrimental activity.

After Drennen retired, he interviewed for a position with the Hess Corporation, a global, integrated energy company. Drennen informed Exxon that he was considering taking a position with Hess and Exxon warned Drennen that he would likely forfeit his incentive awards if he accepted the position. Nonetheless, Drennen accepted the job with Hess and Exxon notified Drennen that his incentive awards were canceled.

Drennen sued Exxon on a variety of theories. Exxon won following a jury trial. Drennen appealed arguing that the "detrimental activity" clause of the Incentive Program was tantamount to a noncompete that was unenforceable under Texas law. The Court of Appeals reasoned that under Texas law, "covenants that place limits on former employees' professional mobility are restraints of trade and are governed by the Covenants Not to Compete Act." According to the Court of Appeals, because the

“detrimental-activity” provision subjected Drennen to a severe economic penalty if he competed (*i.e.*, a forfeiture of over six million dollars), the Covenants Not to Compete Act applied. It was undisputed that the Incentive Program lacked limitations as to time, geographical area and scope of activity to be restrained, and therefore was held not to be enforceable under the Covenants Not to Compete Act. *Id.*

The Texas Supreme Court, however, disagreed with the Court of Appeals, and reversed. It found that “there is a distinction between a covenant not to compete and a forfeiture provision in a non-contributory profit-sharing plan because such plans do not restrict the employee’s right to future employment; rather, these plans force the employee to choose between competing with the former employer without restraint from the former employer and accepting benefits of the retirement plan to which the employee contributed nothing.” *Drennen*, 452 S.W.3d at 329 (citing *Dollgener v. Robertson Fleet Servs., Inc.*, 527 S.W.2d 277, 278–80 (Tex. Civ. App.–Waco 1975, writ ref’d n.r.e.)). “Whatever it may mean to be a covenant not to compete under Texas law, forfeiture clauses in non-contributory profit-sharing plans, like the detrimental-activity provisions in ExxonMobil’s Incentive Programs, clearly are not covenants not to compete.” *Drennen*, 452 S.W.3d at 329. The Court then concluded that since ExxonMobil’s plan did not constitute a covenant not to compete, then it did not contravene Texas’s fundamental policy concerning covenants not to compete, thus allowing for the application of New York law, despite *DeSantis v. Wackenhut Corp.*, 793 S.W.2d 670, 677-78 (Tex. 1990), which is summarized below. Because the Court did not analyze the forfeiture clause under Texas law, Texas employers are left with uncertainty as to whether Texas law allows the enforcement of such “forfeiture” provisions. Specifically, the Court stated this “is a separate question and one which we reserve for another day.” *Drennen*, 452 S.W.3d at 329.

E. Attorney's Fees Issues

1. For Prevailing Employees

Under section 15.51 of the Texas Business and Commerce Code a court may award costs and attorneys' fees incurred by an employee in defending an action to enforce covenants not to compete and covenants not to solicit clients if:

- (a) the primary purpose of the agreement to which the covenant is ancillary is to obligate the promisor to render personal services;
- (b) the employer knew, at the time the agreement was executed, that the agreement did not contain reasonable limitations as to time, geographical area, and scope of activity to be restrained;
- (c) the limitations were unreasonable; and
- (d) the employer sought to enforce the agreement to a greater extent than necessary to protect its goodwill or business interests.

See also Sentinel Integrity Solutions, Inc., 414 S.W.3d at 921-30 (noting that because the statute provides that "the court may award" attorney's fees, the award of attorney's fees is within the trial court's discretion and is never mandatory) (citing *Spring v. Walthall, Sachse & Pipes, Inc.*, No. 04-09-00474-CV, 2010 WL 2102988, at *11 (Tex. App.-San Antonio May 26, 2010, no pet.) (mem. op.) (citing *Bocquet v. Herring*, 972 S.W.2d 19, 20 (Tex. 1998) (holding that statutes providing that court "may award" are permissive and require abuse of discretion to overturn order granting or denying award)).

In *Rimkus Consulting Group, Inc.* 688 F. Supp. 2d at 678, Judge Lee Rosenthal found that the prevailing employee was not entitled to attorneys' fees under this section, stating that, "[a]lthough Texas case law on noncompetition and nonsolicitation restrictions was clear in 1996, there is no evidence that Rimkus knew that the relevant provisions of Cammarata's Employment Agreement were unreasonable under Texas law." (citing *SafeWorks, LLC*, 2009 WL 959969, at *7) (granting summary judgment on a claim for attorneys' fees under § 15.51 because even though Texas law was clear, there

was “no evidence that SafeWorks representatives actually knew that the relevant non-solicitation provisions were unreasonable under Texas law”).

On the other hand, in *Kenyon Intern. Emergency, Services, Inc. v. Malcolm*, No. Civ. A. H-09-3550, 2010 WL 2303328 (S.D. Tex. Jun 07, 2010), *aff’d*, 421 Fed. Appx. 413, 2011 WL 1332167 (5th Cir. 2011), Judge Lynn Hughes awarded attorneys’ fees to the prevailing employees in defending against their former employer’s attempt to enforce a covenant not to compete. Judge Hughes found that the ex-employees were entitled to recover their fees under section 15.51 because the non-competition clause was unreasonably broad; the employer demonstrated no investment in training that would justify any restriction; and the employer knew when the agreements were signed that the covenants were unreasonable. Similarly, in *Sentinel Integrity Solutions, Inc.*, 414 S.W.3d at 921-30, the Houston First Court of Appeals affirmed the trial court’s award of \$750,000 in attorney’s fees for trial expenses to an employee who had been sued by his ex-employer on an overbroad and unenforceable non-competition agreement.

There is a question under Texas law regarding whether an employee who fails to satisfy the requirements of section 15.51 may still be entitled to attorneys’ fees under a declaratory judgment action or private agreement with the employer that provides for attorneys’ fees to the prevailing party. The court in *Perez v. Tex. Disposal Sys., Inc.*, 103 S.W.3d 591, 594 (Tex. App.–San Antonio 2003, pet. denied) held that section 15.52’s preemption language (set forth in the section below) applied to employees, so that the only way prevailing employees could obtain attorneys’ fees is if they were entitled to them under section 15.51’s criteria (set out above). The Beaumont Court of Appeals agrees. *See Sadler Clinic Ass’n, P.A. v. Hart*, 403 S.W.3d 891, 900 (Tex. App.–Beaumont 2013, pet denied) (holding that doctors sued by their ex-employer on their noncompete agreements could not obtain attorneys fees under the Declaratory Judgments Act because, “the exclusivity and preemption provision of the Covenants Not To Compete Act precludes an award of attorney fees under the Declaratory Judgments Act”).

Several courts, however, have taken a contrary position, and have held that because section 15.52's preemption language only covers actions "to enforce a covenant not to compete," a prevailing employee may be entitled to attorneys' fees under a declaratory judgment theory or a private agreement, even if they did not fulfill the criteria set out in section 15.51. *See, e.g., Hardy v. Mann Frankfort Stein & Lipp Advisors, Inc.*, 263 S.W.3d 232, 256 (Tex. App.–Houston [1st Dist.] 2007), *rev'd on other grounds*, 289 S.W.3d 844 (Tex. 2009); *Contemporary Contractors, Inc. v. Strauser*, No. 05-04-00478-CV, 2005 WL 1774983, at *2, (Tex. App.–Dallas July 28, 2005, no pet.) (mem. op.); *Gage Van Horn & Assocs., Inc. v. Tatom*, 26 S.W.3d 730, 732 (Tex. App.–Eastland 2000), *pet. denied improvidently granted*, 87 S.W.3d 536 (Tex. 2002) (per curiam).

2. For Prevailing Employers

Section 15.52 of the Texas Business and Commerce Code provides that:

The criteria for enforceability of a covenant not to compete provided by Section 15.50 of this code and the procedures and remedies in an action to enforce a covenant not to compete provided by Section 15.51 of this code are exclusive and preempt any other criteria for enforceability of a covenant not to compete or procedures and remedies in an action to enforce a covenant not to compete under common law or otherwise.

The only provision regarding attorneys' fees in the Covenants Not to Compete Act is the one mentioned above, in section 15.51 of the Texas Business and Commerce Code. That provision makes no mention of an award of attorneys' fees to a prevailing employer. Under section 15.52, section 15.51 preempts all other claims for attorneys' fees that could be brought (under a declaratory judgment theory, a private agreement that provided for attorneys' fees, or Chapter 38 of the Civil Practice and Remedies Code). *See Perez*, 103 S.W.3d at 594 ("section 15.52 preempts an award of [attorney's] fees under any other law."). Thus, under this logic, prevailing employers are not entitled to attorneys' fees in an action brought under the Covenants Not to Compete Act to enforce a non-compete agreement in any circumstances. *See Ginn v. NCI Bldg. Sys., Inc.*, 472 S.W.3d 802, 827

(Tex. App.–Houston [1st Dist] 2015, no pet.) (“Because the Act preempts NCI's claim for attorney's fees under section 27.01 and the Act does not allow employers to recover attorney's fees in suits to enforce covenants not to compete, we hold that the trial court did not err in denying NCI's claim for attorney’s fees”); *Glattly v. Air Starter Components, Inc.*, 322 S.W.3d 620, 645 (Tex. App.–Houston [1st Dist.] 2010, pet. denied) (“We hold that the trial court properly denied Air Starter’s requests for attorney’s fees because the Covenants Not to Compete Act does not permit employers to recover their attorney’s [fees] in suits to enforce their rights under the Act.”)

F. Choice Of Law And Choice Of Forum Clauses

1. Choice Of Law Clauses

In Texas, contractual choice-of-law provisions are typically enforced, unless the provision violates a fundamental public policy of Texas or the contract bears no reasonable relation to the chosen state. TEX. BUS. & COMM. CODE § 1.301; *Smith v. EMC Corp.*, 393 F.3d 590, 598 (5th Cir. 2004); *Exxon Corp. v. Burglin*, 4 F.3d 1294, 1298 n. 5 (5th Cir. 1993); *Access Telecom, Inc. v. MCI Telcomms. Corp.*, 197 F.3d 694, 705 (5th Cir. 1999) (citing *DeSantis v. Wackenhut Corp.*, 793 S.W.2d 670, 677-78 (Tex.1990)).

In 1990, the Texas Supreme Court held that the law governing enforcement of non-competition agreements is fundamental policy in Texas. *DeSantis*, 793 S.W.2d at 681. *DeSantis* remains good law. *In re AutoNation, Inc.*, 228 S.W.3d 663, 669 (Tex. 2007) (declining to overrule *DeSantis* following the enactment of § 15.50 and *Sheshunoff*); *Turford v. Underwood*, 952 S.W.2d 641 (Tex. App.–Beaumont 1997, orig. proceeding) (following *DeSantis* and applying Texas law because Texas has a greater interest in enforcing non-compete covenants in Texas than does Michigan).

A choice-of-law provision will not be applied if another jurisdiction has a more significant relationship with the parties and their transaction than the state they choose, that jurisdiction has a materially greater interest than the chosen state, and the jurisdiction’s fundamental policy would be contravened by the application of the law of

the chosen state. *See* Restatement (Second) of Conflict of Laws (“Restatement”) § 187; *Access Telecom, Inc. v. MCI Telecommunications Corp.*, 197 F.3d at 705; *International Interests, L.P. v. Hardy*, 448 F.3d 303, 308 (5th Cir. 2006). To reject the parties’ choice-of-law, each element of the Restatement’s test must be met. *Mary Kay Inc. v. Woolf*, 146 S.W.3d 813, 816-17 (Tex. App.–Dallas 2004, pet. denied). To understand whether a state has a more significant interest than the chosen state, the Restatement emphasizes several factors: (a) the place of contracting; (b) the place of negotiation of the contract; (c) the place of performance; (d) the location of the subject matter of the contract; and (e) the domicile, residence, nationality, place of incorporation and place of business of the parties. Restatement §§ 6, 188(2); *Minnesota Mining & Manufacturing Co. v. Nishika, Ltd.*, 955 S.W.2d 853, 856 (Tex. 1996); *DeSantis*, 793 S.W.2d at 678. These contacts are evaluated by their importance, not their number. *Minnesota Mining & Manufacturing Co.*, 955 S.W.2d at 856.

Based on these factors, courts sometimes conclude that a choice of law clause must be disregarded, and Texas law applied – under *DeSantis*, this is especially the case if the employee worked most or all of their tenure in Texas and the proposed enforcement would occur in Texas. *See DeSantis*, 793 S.W.2d at 679 (holding that where the “gist” of the agreement, including the non-compete, was the performance of services in Texas, the relationship of the parties to Texas was more significant than the Florida state law identified in the choice of law clause, and Texas law applied); *Turford*, 952 S.W.2d at 642-43 (disregarding Michigan choice of law clause and applying Texas law based on *DeSantis* because Texas has a greater interest in enforcing non-compete covenants in Texas than does Michigan).

As summarized above, in *Exxon Mobil Corp. v. Drennen*, *Exxon Mobil Corp. v. Drennen*, 452 S.W.3d 319 (Tex. 2014), the appellate court concluded that Texas rather than New York law applied because Texas had a materially greater interest in the dispute between the parties. The court stated that Texas has a strong public policy interest in determining the enforceability of covenants not to compete used in this state because the

plaintiff, Drennen, worked the majority of his career in Texas; he signed the agreements in Texas; he resided in Texas, and Exxon is based in Texas. The court rejected Exxon's argument that, as a large multi-national corporation, it had a stronger interest in uniform application of its employment agreements than Texas's public policy interest because the Incentive Program at issue provides exceptions to New York law application for foreign-national employees that there was no showing that making other exceptions would significantly impede Exxon's operations. Because the restriction at-issue in the case was not enforceable under Texas law, the plaintiff-employee prevailed. However, the Texas Supreme Court granted review of the case in 2013, and reversed in 2014. It found that ExxonMobil's forfeiture clause was not a covenant not to compete, and thus it did not contravene Texas fundamental public policy, thereby permitting the application of New York law. The Court nevertheless revisited its holding in *DeSantis*, that noncompete provisions implicate Texas's fundamental public policy concerns, observing that "the policy concerns regarding uniformity of law raised in *DeSantis* have changed in the past twenty-four years." *Drennen*, 452 S.W.3d at 329. Specifically, the Court noted that:

With Texas now hosting many of the world's largest corporations, our public policy has shifted from a patriarchal one in which we valued uniform treatment of Texas employees from one employer to the next above all else, to one in which we also value the ability of a company to maintain uniformity in its employment contracts across all employees, whether the individual employees reside in Texas or New York. This prevents the "disruption of orderly employer-employee relations" within those multistate companies and avoids disruption to "competition in the marketplace."

Id. at 329-30 (quoting *DeSantis*, 793 S.W.2d at 680). As noted, the Court determined that enforcement of the contractual choice of New York law did not contravene any fundamental public policy of Texas and held that New York law applied. *Id.* at 331.

Based in part on this language from *Drennen*, later in 2014, the Houston First Court of Appeals reversed the trial court, and found enforceable a Delaware choice of law clause in a case involving a Texas-based international corporation and a resident of Colorado, stating, “Texas has no overriding interest in protecting an employment relationship between a multinational corporation and a resident of another state.” *Cameron Intern. Corp. v. Guillory*, 445 S.W.3d 840, 848 (Tex. App.–Houston [1st Dist.] 2014, no pet.).

2. Choice Of Forum Clauses

In the 2007 case of *In re AutoNation, Inc.*, the Texas Supreme Court faced an argument that enforcement of a forum-selection clause in a covenant not to compete, such as selecting an out-of-state forum (in this case Florida) for a suit against a Texas resident, would violate Texas public policy. *In re AutoNation, Inc.*, 228 S.W.3d at 668. The clause would have compelled a Texas worker, working in Texas, to litigate his challenge to his non-compete agreement in Florida, where his nationwide employer was headquartered. The employee argued that such a result would violate public policy and the forum selection clause should be disregarded. The court rejected the argument. *Id.* at 668-69.

The primary reason for the court’s decision in *In re AutoNation, Inc.* was that neither Texas courts nor the Texas Legislature had ever declared a fundamental Texas policy requiring every employment dispute with a Texas resident be litigated in Texas. The court explained that therefore its decision was not inconsistent with *DeSantis*:

Our decision today in no way questions the reasoning of *DeSantis*, but we decline Hatfield’s invitation to superimpose the *DeSantis* choice-of-law analysis onto the law governing forum-selection clauses. While *DeSantis* and the instant case both concern Texas citizens working in Texas for a Florida-based company, there are critical distinctions. *DeSantis*, decided before the now-applicable version of the Covenants Not to Compete Act and our recent decision in *Sheshunoff* construing the Act, did not concern a

mandatory forum-selection clause or first-filed litigation in the parties' chosen jurisdiction. *DeSantis* concerned how Texas courts should construe employment contracts of Texas employees. We observed that "Texas has a materially greater interest than Florida in deciding whether the noncompetition agreement in this case should be enforced." But we have never declared that fundamental Texas policy requires that every employment dispute with a Texas resident must be litigated in Texas. We recognized in [*In re AIU Insurance Company*, 148 S.W.3d 109 (Tex. 2004)] that even where Texas statutory provisions specify the application of Texas law, these provisions are irrelevant to the enforceability of a forum-selection clause where no statute "requires suit to be brought or maintained in Texas." Along similar lines, even if *DeSantis* requires Texas courts to apply Texas law to certain employment disputes, it does not require suit to be brought in Texas when a forum-selection clause mandates venue elsewhere. No Texas precedent compels us to enjoin a party from asking a Florida court to honor the parties' express agreement to litigate a non-compete agreement in Florida, the employer's headquarters and principal place of business.

Id. at 669 (footnotes omitted).

G. Obtaining Injunctive Relief Based On A Non-compete Agreement

1. In General

To obtain a temporary injunction in state court, an applicant must plead and prove: (1) a cause of action against the defendant; (2) a probable right to the relief sought; and (3) a probable, imminent, and irreparable injury in the interim. *Reach Group, L.L.C. v. Angelina Group*, 173 S.W.3d 834, 837 (Tex. App.—Houston [14th Dist.] 2005, no pet.). To show a probable right of recovery, an applicant need not establish that it will finally prevail in the litigation, but it must, at the very least, present some evidence that, under

the applicable rules of law, tends to support its cause of action. *Camp v. Shannon*, 162 Tex. 515, 348 S.W.2d 517, 519 (1961).

To obtain a preliminary injunction in federal court, an applicant must prove four elements: (1) a substantial likelihood of success on the merits; (2) a substantial threat that plaintiffs will suffer irreparable harm if the injunction is not granted; (3) that the threatened injury outweighs any damage that the injunction might cause the defendant; and (4) that the injunction will not disserve the public interest. *Johnson Serv. Group, Inc. v. France*, 763 F. Supp. 2d 819, 825 (N.D. Tex. 2011); *Nichols v. Alcatel USA, Inc.*, 532 F.3d 364, 372 (5th Cir. 2008). *Compare Inter/National Rental Ins. Services, Inc. v. Albrecht*, NO. 4:11-CV-00853, 2012 WL 4506140, at *5 (E.D. Tex. Mar. 14, 2012) (granting injunction based on non-compete agreement where plaintiff was given access to proprietary information) and *Courtroom Sciences, Inc. v. Andrews*, NO. CIV. A. 3:09-CV-251-O, 2009 WL 1313274 (N.D. Tex. May 11, 2009) (granting injunction based on non-compete agreement where substantial evidence showed bad acts by ex-employee, including misappropriation of employer's critical information) with *M-I, L.L.C. v. Stelly*, 2009 WL 2355498, at *6 (assuming non-competition agreements were enforceable and still refusing to enter injunction where there was no such evidence).

Texas Rule of Civil Procedure 682 provides that “[n]o writ of injunction shall be granted unless the applicant therefor shall present his petition to the judge verified by his affidavit and containing a plain and intelligible statement of the grounds for such relief.” However, a verified petition for injunctive relief is not required to obtain an injunction when a full evidentiary hearing on evidence has been held. *Nguyen v. Intertex, Inc.*, 93 S.W.3d 288, 298 (Tex. App.–Houston [14th Dist.] 2002, no pet.).

To obtain injunctive relief based on a non-compete agreement, most courts have held that the employer must still prove that it will suffer irreparable injury if an injunction is not granted. Specifically, the general rule stated is that a covenant not to compete “will not be enforced by an injunction where the party seeking the injunction has failed to show that without injunctive relief he will suffer irreparable injury for which he has no

adequate legal remedy.” *Reach Group, L.L.C.*, 173 S.W.3d at 837-38; *see also Cardinal Health Staffing Network, Inc.*, 106 S.W.3d at 241. That is not always an easy burden to carry, and provides a basis for a court to deny injunctive relief if it wants to do so without attacking the validity of the noncompetition agreement. *See Primary Health Physicians, P.A. v. Sarver*, 390 S.W.3d 662, 665-66 (Tex. App.–Dallas 2012, no pet.) (affirming district court’s denial of a temporary injunction in a noncompetition case because the employer failed to prove irreparable harm); *Cardinal Health Staffing Network, Inc.*, 106 S.W.3d at 241 (holding that since employer could calculate its damages, it failed to prove irreparable harm even though its non-compete agreement was valid and enforceable); *Criterion Brock, Inc. v. Aguirre*, Civil Action No. H–11–1877, 2011 WL 2517319, at *4 (S.D. Tex. June 23, 2011) (reaching same conclusion); *Shoreline Gas, Inc. v. McGaughey*, No. 13-07-364-CV, 2008 WL 1747624, at *12 (Tex. App.–Corpus Christi April 17, 2008, no pet.) (not designated for publication) (although non-compete agreement was enforceable, employer was not entitled to a temporary injunction because it failed to prove probability of irreparable injury); *W.R. Grace & Co. - Conn v. Taylor*, No. 14-06-01056-CV, 2007 WL 1438544 (Tex. App.–Houston [14th Dist.] May 17, 2007, no pet.) (same).

However, there are three relevant notes here. First, Texas law provides that “proof that a highly trained employee is continuing to breach a non-competition covenant gives rise to a rebuttable presumption that the applicant is suffering irreparable injury.” *Electro-Motor, Inc. v. Industrial Apparatus Services, Inc.*, 390 B.R. 859, 867 (Bankr. E.D. Tex. 2008) (quoting *Cardinal Health Staffing Network, Inc.*, 106 S.W.3d at 236); *see also Beasley v. Hub City Tex., L.P.*, No. 01–03–00287–CV, 2003 WL 22254692, at *7–8 (Tex. App–Houston [1st Dist.] Sept. 29, 2003, no pet.) (mem. op.).

Second, several federal courts in Texas have held that harm arising out of a breach of non-compete covenants is the “epitome of irreparable injury.” *See American Exp. Financial Advisors, Inc. v. Scott*, 955 F. Supp. 688, 693 (N.D. Tex. 1996); *Amerispec, Inc. v. Metro Inspection Serv., Inc.*, No. 3:01–CV–0946–D, 2001 WL 770999, at *6

(N.D. Tex. July 3, 2001); *A & A Global Industries, Inc. v. Wolfe*, No. 3:01–CV–1515–D, 2001 WL 1388020, at *5 (N.D. Tex. Nov. 6, 2001).

Third, at least one Texas state court has done away with the irreparable injury requirement altogether. As the Fort Worth Court of Appeals stated in 2012 in an unpublished decision:

Under the common law, a party seeking an injunction must show that without injunctive relief he will suffer irreparable injury for which he has no adequate legal remedy. *Tom James Co. v. Mendrop*, 819 S.W.2d 251, 252 (Tex. App.–Fort Worth 1991, no writ). However, in its motion for rehearing, Heritage notes that if a party relies on a statute that defines the requirements for injunctive relief, then the express statutory language supersedes common law requirements. *Butler v. Arrow Mirror & Glass, Inc.*, 51 S.W.3d 787, 795 (Tex. App.–Houston [1st Dist.] 2001, no pet.). The Covenants Not to Compete Act provides for “damages, injunctive relief, or both” for a breach of a non-compete by the promisor. TEX. BUS. & COM. CODE § 15.51(a). Thus, a party seeking injunctive relief under the Covenants Not to Compete act does not have to show irreparable injury for which he has no adequate legal remedy as a prerequisite to injunctive relief. *See Letkeman v. Reyes*, 299 S.W.3d 482, 486 (Tex. App. – Amarillo 2009, no pet.) (“It is enough simply to prove a distinct or substantial breach.”); *see also* TEX. BUS. & COM. CODE § 15.52 (stating that “the procedures and remedies ... provided by Section 15.51 ... are exclusive and preempt any other criteria for enforceability of a covenant not to compete or procedures and remedies in an action to enforce a covenant not to compete under common law or otherwise”).

Heritage Operating, L.P. v. Rhine Brothers, LLC, NO. 02-10-00474-CV, 2012 WL 2344864, at *6 (Tex. App.–Fort Worth June 21, 2012) (unpublished).

Most Courts of Appeals, however, have continued to require proof of irreparable harm. *See Argo Group U.S., Inc. v. Levinson*, 468 S.W.3d 698, 701-02 (Tex.App. – San Antonio 2015, no pet.); *Down Time–South Texas, LLC v. Elps*, 13–13–00495–CV, 2014 WL 1464320, at *7 (Tex.App.–Corpus Christi–Edinburg Mar. 20, 2014, no pet.) (mem. op.) (requiring proof of injury). *Sarver*, 390 S.W.3d at 665 (holding that the Covenants Not to Compete Act does not preempt the requirements for obtaining temporary injunctive relief and citing multiple cases in support of its holding). *EMSL Analytical, Inc. v. Younker*, 154 S.W.3d 693, 695 (Tex.App.–Houston [14th Dist.] 2004, no pet.); *Cardinal Health Staffing Network, Inc. v. Bowen*, 106 S.W.3d 230, 239–40 (Tex.App.–Houston [1st Dist.] 2003, no pet.); *NMTC Corp. v. Conarro*, 99 S.W.3d 865, 867–68 (Tex.App.–Beaumont 2003, no pet.)).

An injury is irreparable if the injured party cannot be adequately compensated in damages or if the damages cannot be measured by any certain pecuniary standard. *See Butnaru v. Ford Motor Co.*, 84 S.W.3d 198, 204 (Tex. 2002). Because a company’s loss of goodwill, clientele, marketing techniques, and office stability are not easily assigned a dollar value, they qualify as “probable injury” for purposes of injunctive relief. *Graham v. Mary Kay Inc.*, 25 S.W.3d 749, 753 (Tex. App.–Houston [14th Dist.] 2000, pet. denied). However, the evidence must show a probable loss of goodwill, clientele, marketing techniques, or office stability to obtain injunctive relief. *See id.* (holding that loss of goodwill and business stability was established by evidence that Graham actively sought Mary Kay salespersons who were willing to breach their contracts); *see also Armendariz v. Mora*, 526 S.W.2d 542, 543 (Tex. 1975) (holding that applicant has the burden of offering some evidence establishing probable injury); *W.R. Grace & Co. – Conn*, 2007 WL 1438544, at * 2 (“Although Taylor admitted that, while working for SIKA, he has had discussions with several WRG customers, there is no evidence that WRG lost sales, marketing advantage, or goodwill, or otherwise suffered an irreparable injury; or that it has no adequate remedy at law for any such violation”).

In *York*, 2009 WL 1840813 at *4-6 the Houston First Court of Appeals upheld the trial court's entry of a temporary injunction against Hair Club for Men's ex-employees and new employer under the ex-employees' non-competition (customer non-solicitation) agreements as well as under a misappropriation of trade secrets theory. The court observed that the non-competition agreements at-issue in the case were similar to the one at issue in *Mann Frankfort*. *Id.* at *5. Likewise, in *Vaughn v. Intrepid Directional Drilling Specialists, Ltd.*, 288 S.W.3d 931, 938 (Tex. App.–Eastland 2009, no pet.), the Eastland Court of Appeals affirmed the trial court's issuance of an injunction to enforce non-competition agreements. The Fort Worth Court of Appeals in *O'Brien v. Rattikin Title Co.*, NO. 2-05-238-CV, 2006 WL 417237 (Tex. App.–Fort Worth Feb. 23, 2006, pet. dis'd w.o.j.) also affirmed the trial court's entry of a temporary injunction enforcing the terms of a non-competition agreement.

Generally, applications for injunctive relief are required to be verified, *see* TEX. R. CIV. P. 682; however, the verification requirement of rule 682 can be waived. *Crystal Media, Inc. v. HCI Acquisition Corp.*, 773 S.W.2d 732, 734 (Tex. App.–San Antonio 1989, no writ); *see Ex parte Stiles*, 958 S.W.2d 414, 419 n. 2 (Tex. App. – Waco 1997, pet. denied). When a full evidentiary hearing on evidence has been held, a verified petition for injunctive relief is not required. *Nguyen v. Intertex, Inc.*, 93 S.W.3d 288, 298 (Tex. App.–Houston [14th Dist.] 2002, no pet.), *overruled, in part, on other grounds by Glassman v. Goodfriend*, No. 14–09–00522–CV, 2011 Tex. App. LEXIS 4189, at *23, 2011 WL 2150225 (Tex. App.–Houston [14th Dist.] June 2, 2011, no pet.) (en banc); *see Town of Palm Valley v. Johnson*, 17 S.W.3d 281, 288 (Tex. App.–Corpus Christi 2000, pet. denied); *Georgiades v. Di Ferrante*, 871 S.W.2d 878, 882 (Tex. App.–Houston [14th Dist.] 1994, writ denied). “The reason for not requiring literal compliance with Rule 682 is that the writ of injunction is not granted upon the averments of the petition alone, but upon sworn and competent evidence admitted at a full hearing.” *Nguyen*, 93 S.W.3d at 298.

Under Texas state court practice, every order granting an injunction must set forth the reasons for its issuance. TEX. R. CIV. P. 683. The trial court is not required to explain its reasons for believing that the applicant has shown a probable right to final relief, but it must give the reasons why injury will be suffered if the interlocutory relief is not ordered. *Transp. Co. of Tex. v. Robertson Transp.*, 152 Tex. 551, 261 S.W.2d 549, 553 (1953). The reasons given by the trial court for granting or denying a temporary injunction must not be mere conclusory statements. *Int'l Bhd. of Elec. Workers Local Union 479 v. Becon Const. Co., Inc.*, 104 S.W.3d 239, 244 (Tex. App.–Beaumont 2003, no pet.). The requirement of specifying the reasons for granting a temporary injunction is mandatory, and noncompliance amounts to an abuse of discretion. *Toby Martin Oilfield Trucking, Inc. v. Martin*, 640 S.W.2d 352, 355 (Tex. Civ. App.–Houston [1st Dist.] 1982, no writ).

Rule 683 further provides, in relevant part, that orders granting injunctions “shall be specific in terms” and “shall describe in reasonable detail and not by reference to the complaint or other document, the act or acts sought to be restrained.” This does not necessarily mean that each customer the restrained party is not to solicit must be specifically named in the injunction order. *See Vaughn*, 288 S.W.3d at 938 (rejecting that argument); *Amalgamated Acme Affiliates, Inc. v. Minton*, 33 S.W.3d 387, 397-98 (Tex. App.–Austin 2000, no pet.) (a temporary injunction that did not specifically name the applicant’s customers and advertisers complied with Rule 683 where the party enjoined admitted it could identify the customers and advertisers.); *Safeguard Bus. Sys., Inc. v. Schaffer*, 822 S.W.2d 640, 644 (Tex. App.–Dallas 1991, no writ) (in reviewing a permanent injunction, the court stated that “[o]rders generally restraining solicitation of customers and not specifically listing the individual customers have not been found to be overbroad.”).

The trial court is required to set a bond when it grants a temporary injunction. TEX. R. CIV. P. 684. The applicant must post the bond, and it is payable to the adverse party if the temporary injunction is dissolved at trial. *Id.* The purpose of a bond is to provide protection to the enjoined party for any possible damages occurring as a result of

the injunction. *Bayoud v. Bayoud*, 797 S.W.2d 304, 312 (Tex. App.–Dallas 1990, writ denied). The determination of the adequacy of the bond set by the trial court is to be made on a case-by-case basis based upon the record before the reviewing court. *Maples v. Muscletech, Inc.*, 74 S.W.3d 429, 431 (Tex. App.–Amarillo 2002, no pet.); *Stone*, 53 S.W.3d at 696. The amount of a bond is within the trial court’s sound discretion and will not be disturbed on appeal absent an abuse of that discretion. *Four Stars Food Mart, Inc. v. Tex. Alcoholic Beverage Comm’n*, 923 S.W.2d 266, 269 (Tex. App.–Fort Worth 1996, no writ); *Khaledi v. H.K. Global Trading, Ltd.*, 126 S.W.3d 273, 286 (Tex. App.–San Antonio 2003, no pet.); *Maples*, 74 S.W.3d at 431.

2. Successor Companies’ Rights To Seek Injunctive Relief Enforcing A Noncompetition Agreement

In *Dittmer v. Source EDP, Texas, Inc.*, 595 S.W.2d 877, 881 (Tex. Civ. App.–Dallas 1980, no writ), the Dallas Court of Appeals found that the trial court had not erred in inferring that the plaintiff corporation was the successor-in-interest to the company that had entered the non-compete agreement with the defendant-employee. The district court entered an injunction in the successor’s favor enforcing its predecessor’s non-compete agreement, and the appeals court affirmed on that issue.

There is a limitation, however: Specifically, Texas courts have held that when a business is sold and the covenant not to compete is assigned to the purchaser, the reasonable geographic restriction must be “no larger than to protect the business sold.” *Williams v. Powell Elec. Mfg. Co.*, 508 S.W.2d 665, 668 (Tex. Civ. App.–Houston [14th Dist.] 1974, no writ) (citing *Barrett v. Curtis*, 407 S.W.2d 359 (Tex. Civ. App.–Dallas 1966, no writ)). In *M-I LLC v. Stelly*, 733 F. Supp. 2d 759, 795 (S.D. Tex. 2010), Judge Keith Ellison reiterated and applied this rule.

3. The Effect Of Contractual Stipulations Of Irreparable Harm

Non-compete agreements often contain recitations that the employer will suffer irreparable harm if the agreement is breached. Most courts hold that such clauses are not dispositive and do not do away with the need to present independent evidence of

irreparable harm in order to obtain an injunction. *See W.R. Grace & Co.–Conn*, 2007 WL 1438544, at * 2 n. 7 (“such stipulations have been held insufficient to support a finding of irreparable harm for injunctive relief”) (citing *Dominion Video Satellite, Inc. v. Echostar Satellite Corp.*, 356 F.3d 1256, 1266 (10th Cir. 2004); *Smith, Bucklin & Assocs., Inc. v. Sonntag*, 83 F.3d 476, 481 (D.C. Cir. 1996); *Baker’s Aid, Inc. v. Hussmann Foodservice Co.*, 830 F.2d 13, 16 (2nd Cir. 1987); *Traders Int’l, Ltd. v. Scheuermann*, No. H-06-1632, 2006 WL 2521336, at *8 (S.D. Tex. Aug. 30, 2006) (not designated for publication); *Sec. Telecom Corp. v. Meziere*, No. 05-95-01360-CV, 1996 WL 87212, at *2 (Tex. App.–Dallas Feb. 28, 1996, no writ.) (not designated for publication)); *Shoreline Gas, Inc.*, 2008 WL 1747624, at *11 (“Shoreline has pointed us to no Texas case holding that an agreement such as this establishes, for injunction purposes, that remedies at law will be inadequate or that irreparable injury will necessarily be suffered.”).

However, some Texas courts have found that such contractual clauses are themselves at least some evidence of irreparable harm. *See Brink’s Inc. v. Patrick*, Civil Action No. 3:14–CV–775–B, 2014 WL 2931824, at *7 (N.D. Tex. June 27, 2014) (“Furthermore, the parties themselves apparently recognized the serious harm that the breach of the non-compete agreement could cause, because Greco expressly agreed in his Confidentiality and Non–Competition Agreement that Brink’s would have the right to a preliminary injunction in order to enforce the non-competition provisions.”); *Wright*, 137 S.W.3d at 293-94 (relying on such a clause to conclude that some evidence supported the trial court’s finding of irreparable harm); *see also Argo Group U.S., Inc. v. Levinson*, 468 S.W.3d 698, 702 (Tex.App. – San Antonio 2015, no pet.) (following *Wright*, but still affirming district court’s decision to deny temporary injunction).

4. The Effect Of A Party’s Delay On Its Ability To Obtain Injunctive Relief

Texas state courts hold that delay alone is not sufficient to bar a plaintiff from obtaining injunctive relief. As one court explained, “Texas case law does not prevent

injunctive relief merely because a potential plaintiff did not file a claim as quickly as possible.” *Garth v. Staktek Corp.*, 876 S.W.2d 545 (Tex. App.–Austin 1994, writ dismissed w.o.j.) (citing *K & G Oil Tool & Serv. Co. v. G & G Fishing Tool Serv.*, 158 Tex. 594, 314 S.W.2d 782, 790-91 (Tex. 1958)). In *K & G*, laches was not a bar where the defendant in an action for an injunction and damages based on misappropriation of trade secrets argued that the plaintiff’s action, even though filed within the limitations period, should be barred by laches because the defendant continued to develop and market the product with the information the plaintiff claimed to be proprietary. *K & G*, 314 S.W.2d at 790-91. In another trade secrets misappropriation case, the Austin Court of Appeals followed *K & G* and issued the same holding. See *Garth*, 876 S.W.2d at 550-51. Rather, a party asserting the defense of laches must show both an unreasonable delay by the other party in asserting its rights, and harm resulting to it because of the delay. *Rogers v. Ricane Enters. Inc.*, 772 S.W.2d 76, 80 (Tex. 1989).

Federal courts tend to take a somewhat harsher view of parties who delay seeking injunctive relief. See *SafeWorks, LLC*, 2009 WL 959969, at *6-7 (“In addition, SafeWorks’ delay in seeking a preliminary injunction weighs heavily against a finding of irreparable injury.”); *Rimkus Consulting Group, Inc. v. Cammarata*, 255 F.R.D. 417, 438-39 (S.D. Tex. 2008) (“Rimkus’s delay in seeking injunctive relief in this court weighs heavily against a finding of irreparable injury.”); *Gonannies, Inc. v. Goaupair.Com, Inc.*, 464 F. Supp. 2d 603, 609 (N.D. Tex. 2006) (“Delay in seeking a remedy is an important factor bearing on the need for a preliminary injunction. Absent a good explanation, a substantial period of delay militates against the issuance of a preliminary injunction by demonstrating that there is no apparent urgency to the request for injunctive relief. Evidence of an undue delay in bringing suit may be sufficient to rebut the presumption of irreparable harm.”) (citation omitted); but see *Daily Instruments Corp. v. Heidt*, 998 F. Supp.2d 553, 570 (S.D. Tex. 2014) (stating in a noncompete and trade secrets case that “Plaintiff’s initial delay of perhaps four months does not preclude it from recovering the equitable preliminary relief it seeks in the present motion”).

5. Court Ordered Equitable Extensions Of The Period Of Restraint

Regarding equitable extension of the contractual period of restraint, in *Guy Carpenter & Co. v. Provenzale*, 334 F.3d 459, 464 (5th Cir. 2003), a case arising out of Texas law, the Fifth Circuit held that the expiration of the contractually agreed upon period of non-competition did not render an appeal moot because “[i]f this Court remands, the district court has the power under Texas law to craft an injunction that extends beyond the expiration of the non-solicitation covenant. Exercising this equitable power might be particularly appropriate given the district court’s year-long delay before ruling on the motion to reconsider.” *See also Premier Indus. Corp. v. Tex. Indus. Fastener Co.*, 450 F.2d 444, 448 (5th Cir. 1971) (applying Texas law and stating that “[an] argument that the trial judge exceeded his discretion by enjoining the appellants beyond the time specified in the . . . contract is without merit”).

In *RenewData Corp. v. Strickler*, No. 03-05-00273-CV, 2006 WL 504998, at *5 (Tex. App.–Austin Mar. 3, 2006, no pet.), the employer, Renew, complained that the district court refused to equitably extend the term of the non-compete agreement. The appeals court rejected the employer’s complaint, stating, “[t]his chronology shows that the delays in the enforcement of the covenant not to compete were not simply “inherent to litigation” but were attributable to Renew. We find that Renew did not diligently pursue its remedies under the covenant not to compete and that the district court, in the exercise of its equity jurisdiction, did not abuse its discretion in denying Renew’s motion for equitable extension of the covenant not to compete.”

In *Farmer v. Holley*, 237 S.W.3d 758 (Tex. App.–Waco 2007, pet. denied), the district court equitably extended the term of the non-competition agreement. The Waco Court of Appeals found this was error, stating, “[w]e do not hold that a covenant not to compete cannot be equitably extended, but hold that the record does not support Holley’s argument that the violations of the covenant, if any, were “continuous and persistent.”

Thus the trial court erred in equitably delaying the start of the covenant not to compete until the date of the judgment rather than the date of the agreement.”

In *SafeWorks, LLC*, 2009 WL 959969, at *6-7, Judge Nancy Atlas agreed that the expiration of the term of restraint did not preclude her from entering an injunction based on the court’s equitable powers. However, Judge Atlas declined to enter an injunction anyway because the movant had failed to establish a substantial likelihood of success on the merits.

In *Travelhost, Inc. v. Brady*, NO. 3:11-CV-454-M-BK, 2012 WL 556036 (N.D. Tex. Feb. 17, 2012), the court held that exercising its equitable power to extend the time period covered by the covenants not to compete was “particularly appropriate” because the “record shows that the Defendants’ violations of the covenants not to compete have been continuous and persistent.” (citing *Guy Carpenter & Co., Inc., v. Provenzale*, 334 F.3d 459, 464 (5th Cir. 2003) (holding that a district court may exercise its equitable power to craft an injunction that extends beyond the expiration of the covenant not to compete) and *Farmer v. Holley*, 237 S.W.3d 758, 761 (Tex. App.–Waco 2007, review denied) (holding that under Texas law, covenants not to compete can be equitably extended if the violations of the covenant were “continuous and persistent.”)). Likewise, in *Travelhost, Inc. v. Modglin*, NO. 3:11-CV-0456-G, 2012 WL 2049321, at *6 (N.D. Tex. June 6, 2012), the court concluded that the ex-employee’s consistent and persistent violation of his noncompetition agreement made it “only fair that this court use its equitable power to extend the term of the non-compete agreement for an additional two years.”

6. The Unclean Hands Defense

In *Central Texas Orthopedic Products, Inc. v. Espinoza*, NO. 04-09-00148-CV, 2009 WL 4670446 (Tex. App.–San Antonio Dec. 9, 2009, pet. denied) (unpublished), the employee tried to avoid the enforcement of his non-competition agreement by raising the defense of “unclean hands.” The equitable doctrine of “unclean hands” requires that a party seeking equity must come to court with clean hands. *In re EGL Eagle Global*

Logistics, L.P., 89 S.W.3d 761, 766 (Tex. App.–Houston [1st Dist.] 2002, orig. proceeding [mand. denied]). The doctrine of unclean hands will be applied only to “one whose conduct in connection with the same matter or transaction has been unconscientious, unjust, or marked by a want of good faith, or one who has violated the principles of equity and righteous dealing.” *In re Jim Walter Homes, Inc.*, 207 S.W.3d 888, 899 (Tex. App.–Houston [14th Dist.] 2006, orig. proceeding) (quoting *Thomas v. McNair*, 882 S.W.2d 870, 880-81 (Tex. App.–Corpus Christi 1994, no writ.)).

In *Central Texas Orthopedic Products, Inc. v. Espinoza*, CTOP sued Espinoza after he resigned his employment and went to work for a direct competitor in violation of a noncompetition agreement he signed with CTOP. Espinoza contended that the noncompetition agreement could not be enforced against him because CTOP had violated a separate Compensation Agreement by failing to pay all wages and commissions owed to him. The trial court agreed and granted summary judgment for Espinoza. The San Antonio Court of Appeals reversed the judgment for Espinoza and held that since CTOP’s alleged failure to pay Espinoza did not grow out of the obligations outlined in the noncompetition agreement, the alleged breaches of the separate Compensation Agreement could not, as a matter of law, constitute an unclean hands defense to the noncompetition agreement. *See also French v. Community Broadcasting of Coastal Bend, Inc.*, 766 S.W.2d 330, 334 (Tex. App.–Corpus Christi 1989, writ dism’d w.o.j.) (evidence did not require finding that the employer’s allegedly unclean hands barred enforcement of covenant not to compete against former general manager for television station; the covenant itself stated it was to be construed as agreement independent of any other contractual provision and that other causes of action should not constitute defense to covenant, and the contract contained a clause allowing for recovery of damages for breach of contract).

In *Premier Polymers, LLC v. Wendt*, Civil Action No. H–15–1812, 2015 WL 4434551, at *5 (S.D. Tex. July 17, 2015), the defendant-employee claimed that his ex-employer had hired employees and then put them to work soliciting potential customers

in violation of those employees' non-solicitation obligations to their former employers. Based on this, the employee alleged that under the unclean hands doctrine his ex-employer should be barred from enforcing its non-solicitation agreement against him. The district court rejected the defendant-employee's unclean hands defense, stating, "[t]he evidence presented regarding former Premier employees and their non-solicitation agreements does not relate to Wendt's conduct or Agreement in this case. The court will not consider this defense."

7. **Is The Ex-Employee's New Employer A Necessary Party In An Action Against The Employee For An Injunction?**

In *Down Time-South Texas, LLC v. Elps*, NO. 13-13-00495-CV, 2014 WL 1464320, at *7 (Tex. App.–Corpus Christi Mar. 20, 2014, no pet.) (unpublished), the Corpus Christi Court of Appeals held that the new employer is a necessary party to a case where the new employer's rights would be affected by entry of the requested injunction, and its absence precludes the granting of injunctive relief. Whether other courts will follow this case remains to be seen.

IV. UPDATE ON NON-RECRUITMENT COVENANTS UNDER TEXAS LAW

Texas courts generally enforce employee non-recruitment or non-solicitation agreements as they would any other contract, holding that they are not restraints of trade and, therefore, not subject to the requirements of section 15.05(a) of the Texas Business and Commerce Code. See *Spicer*, 2006 WL 1751786 at *4 (finding such an agreement enforceable as an ordinary contract); *Nova Consulting Group, Inc. v. Engineering Consulting Servs., Ltd.*, 2005 WL 2708811, *17-18 (W.D. Tex. 2005) (finding such an agreement enforceable as an ordinary contract after reviewing Texas law); see also *Smith, Barney, Harris Upham & Co., Inc. v. Robinson*, 12 F.3d 515, 518 (5th Cir. 1994) (finding that employee "nonrecruitment covenants . . . do not necessarily restrict a former employee's ability to compete . . . [and] should not significantly restrain trade").

There is, however, one Texas court that analyzed such an employee non-recruitment agreement under section 15.50(a) of the Texas Business and Commerce Code, but found it enforceable anyway. *See Totino*, 1998 WL 552818, at *8–9. And, in the 2011 *Marsh USA Inc.* decision, the Texas Supreme Court did, in fact, actually state that “[c]ovenants that place limits on former employees’ professional mobility or restrict their solicitation of the former employers’ customers *and employees* are restraints on trade and are governed by the Act.” 354 S.W.3d at 768 (italics added). Whether other courts will view this is pure dicta (and perhaps unintended dicta at that) is yet to be seen. Even if they do, it is likely that courts will often find restrictions against soliciting current employees enforceable. *See Merritt Hawkins & Assocs., LLC v. Gresham*, 79 F. Supp. 3d 625, 639-40 (N.D. Tex. 2015) (three year non-solicitation of employees provision limited to solicitation of employer’s employees was reasonable and enforceable).

Where the requirements of a temporary injunction are satisfied, an ex-employee who breaches a non-recruitment agreement may be enjoined from further breaches, as may anyone working in concert with him, including his new employer. *Compare Totino*, 1998 WL 552818, at *8–9 (affirming grant of injunction barring not only ex-employees who had signed non-recruitment agreements, but also their new employer, from soliciting the former employer’s current employees) (not designated for publication) *with Spicer*, 2006 WL 1751786 at *4-5 (finding such a non-recruitment agreement enforceable under Texas law but refusing to enforce it through a preliminary injunction because the court concluded that the employer did not clearly demonstrate that a substantial threat existed that it would suffer irreparable injury if the preliminary injunction was denied.).

V. UPDATE ON AT-WILL EMPLOYEES’ FIDUCIARY OBLIGATIONS IN TEXAS

In Texas, an at-will employee breaches his or her fiduciary duty to his or her employer if, during his or her employment, he or she: (1) misappropriates the employer’s trade secrets; (2) solicits the employer’s customers while still working for the employer; (3) solicits the departure of other employees while still working for the employer; or (4)

carries away confidential information. See *Johnson v. Brewer & Pritchard, P.C.*, 73 S.W.3d 193, 202 (Tex. 2002); *Abetter Trucking Co., Inc. v. Arizpe*, 113 S.W.3d 503, 512 (Tex. App.–Houston [1st Dist.] 2003, no pet.). In *Rimkus Consulting Group, Inc.*, 688 F. Supp. 2d at 669-70, Judge Lee Rosenthal denied summary judgment against the former employer’s breach of fiduciary duty claim because there were disputed fact issues on whether the employee-defendant breached his fiduciary duty to Rimkus by misappropriating confidential, proprietary, or trade secret information obtained while he was an officer of Rimkus, and then used that information to solicit Rimkus customers and compete against Rimkus.

Aside from the above limitations, however, Texas law is clear that taking preparatory steps to compete with an employer while still working for that employer is not actionable. See *Navigant Consulting, Inc. v. Wilkinson*, 508 F.3d 277, 284 (5th Cir. 2007) (“[U]nder Texas law, an at-will employee may properly plan to go into competition with his employer and may take active steps to do so while still employed. Even the existence of a fiduciary relationship between employee and employer does not preclude the fiduciary from making preparations for a future competing business venture; nor do such preparations necessarily constitute a breach of fiduciary duties.” (quotation marks and citations omitted)); *Ameristar Jet Charter, Inc. v. Cobbs*, 184 S.W.3d 369, 374 (Tex. App.–Dallas 2006, no pet.) (holding there was no breach of fiduciary duty when an employee formed a competing business while still employed but did not actually compete with the employer until he resigned); *Abetter Trucking Co.*, 113 S.W.3d at 510; *Augat, Inc. v. Aegis, Inc.*, 409 Mass. 165, 565 N.E.2d 415, 419 (1991) (quoted by the Texas Supreme Court in *Johnson v. Brewer & Pritchard, P.C.*, 73 S.W.3d 193, 201 (Tex. 2002)). Indeed, in Texas, as a legal matter, to resign from one’s employment and go into business in competition with one’s former employer is, under ordinary circumstances, a constitutional right. *Abetter Trucking Co.*, 113 S.W.3d at 510.

The employee has no general duty to disclose his plans and may secretly join with other employees in the endeavor without violating any duty to the employer. *Id.*; *M P I*,

Inc. v. Dupre, 596 S.W.2d 251, 254 (Tex. Civ. App.–Fort Worth 1980, writ ref’d n.r.e.). Further, an employee may use his general knowledge, skill, and experience acquired in the former employment to compete. *Abetter Trucking Co.*, 113 S.W.3d at 512. Moreover, the possibility of crippling, or even destroying, a competitor is inherent in a competitive market. *Id.* at 510; *Augat*, 565 N.E.2d at 422.

In 2010, the Fifth Circuit U.S. Court of Appeals affirmed a \$1.43 million award against a company’s two former employees and the new company they formed to compete against their former employer. *See Meaux Surface Protection, Inc. v. Fogleman*, 607 F.3d 161 (5th Cir. 2010). Judge David Hittner was the trial court judge. The defendants challenged the damages award, claiming that there was no evidence their breaches of fiduciary duty caused plaintiff any harm. *Id.* at 169. The court rejected that argument, stating:

A jury may infer proximate cause from circumstantial evidence. . . . In *Navigant*, the evidence showed that the defendants solicited fellow employees to join them in defecting to a competitor. *Id.* at 290. Following the defendants’ departure, their erstwhile employer lost many key employees to the competitor and experienced a drop-off in business. *Id.* We held that the jury could reasonably conclude, based on this evidence, that the defendants’ actions sent the plaintiff’s business into a maelstrom. *Id.* at 290-91. “Alert avoidance of the classical fallacy of *post hoc, ergo propter hoc* does not require rejection of common sense inferences.” *Id.* at 291 (quoting *Swanner v. United States*, 406 F.2d 716, 718 (5th Cir. 1969)). The evidence showed that Fogleman and Kotrla set up CleanBlast several months before they resigned from Meaux. Defendants informed many of Meaux’s foremen and staff that they would form a new company, and indicated that several of Meaux’s jobs would be commandeered by CleanBlast. Patricia Duhon, an employee of Meaux, testified that prior to resigning, Kotrla actively recruited many of Meaux’s employees. Duhon’s

testimony was that Kotrla said that once Meaux's foremen were working for CleanBlast, CleanBlast would get business from Meaux's clients, because the clients "pretty much followed the foremen." Within days of Fogleman's and Kotrla's resignation from Meaux, several of Meaux's work crews were working under CleanBlast's ensign. In suspiciously short order, CleanBlast also procured insurance, master service agreements ("MSAs"), and job contracts with several of Meaux's largest customers. Meaux's sales to those customers sank like an anchor.

Defendants say Meaux's fusillade of evidence fails to strike below the waterline because Ennemann did not have direct knowledge of the above facts, and because other factors could have caused a drop-off in business. Defendants note that 2006 was a bumper year for their industry due to repairs necessitated by hurricanes Katrina and Rita, and business was somewhat becalmed in 2007. Defendants also say that their lawful competition could have caused a drop in Meaux's business, and note that there is a high degree of turnover in their industry. But defendants cannot navigate a perilous shoal: such arguments are matters for the trier of fact. They do not undermine the legal sufficiency of properly admitted evidence in support of the verdict.

Based on the evidence submitted at trial, the jury was well within its province to find that defendants' recruitment of Meaux's employees was not mere palaver, but rather, directly caused Meaux to suffer a loss in business. *See id.* at 290-91. The district court properly denied defendants' motions for judgment as a matter of law as to causation.

Id. at 170.

The defendants also argued that the jury's \$1.43 million damages award for lost profits was too speculative to be affirmed. *Id.* The court rejected that argument too, stating:

The Texas Supreme Court instructs that “[r]ecovery of lost profits does not require that the loss be susceptible to exact calculation.” *Szczepanik v. First S. Trust Co.*, 883 S.W.2d 648, 649 (Tex. 1994) (citing *Tex. Instruments v. Teletron Energy Mgmt., Inc.*, 877 S.W.2d 276, 279 (Tex. 1994)). Nevertheless, the party claiming injury must show more than some lost profits: “[t]he amount of the loss must be shown by competent evidence with reasonable certainty.” *Id.* This inquiry is fact intensive. *Id.* (citing *Holt Atherton Indus., Inc. v. Heine*, 835 S.W.2d 80, 84 (Tex. 1992)). “At a minimum, opinions or estimates of lost profits must be based on objective facts, figures, or data from which the amount of lost profits may be ascertained.” *Id.* (quoting *Heine*, 835 S.W.2d at 84). The proper measure is lost net profits. *Heine*, 835 S.W.2d at 83 n. 1. Unless the issues concerning lost profits are “highly technical,” expert testimony is not required. *Fairmont Supply Co. v. Hooks Indus., Inc.*, 177 S.W.3d 529, 532 n. 1 (Tex. App.–Houston [1st Dist.] 2005, pet. denied).

Texas law recognizes that for enterprises with a record of profitability, records of past profits, with other relevant facts and circumstances, may support a finding of lost profits. *See Sw. Battery Corp. v. Owen*, 131 Tex. 423, 115 S.W.2d 1097, 1098-99 (Tex. 1938). In contrast, new or unestablished ventures must meet more exacting standards to prove that the profits claimed are not “too uncertain or speculative.” *See id.* The “requirement of ‘reasonable certainty’ in the proof of lost profits is intended to be flexible enough to accommodate the myriad circumstances in which claims for lost profits arise.” *Tex. Instruments*, 877 S.W.2d at 279. The proper focus is not on the business entity, but on whether the activity in which it engages is generally profitable. *See id.* at 280.

The jury heard an estimate from Carsten Ennemann that Meaux had suffered a \$2.3 million loss of treasure in 2007 thanks to their employees-

turned-freebooters. Ennemann was personally familiar with the drop in business suffered by Meaux. Ennemann compared 2007 sales figures for several major clients with the budget projections which were prepared by Fogleman himself before he jumped ship. At trial, Fogleman stood by the projections as reasonable estimates of Meaux's likely business, taking into account the factors he deemed relevant. Fogleman's testimony supported Meaux's case; he was keelhailed by his own windlass. In light of the evidence tending to show that defendants' acts harmed Meaux, the jury was entitled to find that Fogleman's and Kotrla's acts in derogation of a fiduciary duty to Meaux harmed it to the tune of \$1.43 million. *See Navigant Consulting*, 508 F.3d at 291.

Id. at 170-71.

In *PAS, Inc. v. Engel*, 350 S.W.3d 602 (Tex. App.–Houston [14 Dist.] 2011, no pet.), the Houston Fourteenth Court of Appeals found that a genuine issue of material fact as to whether employer had fiduciary relationship with its vice president of sales precluded summary judgment on the employer's claim that its former vice president breached his fiduciary duties to it by failing to disclose, while negotiating a narrower non-compete agreement, that he had already taken steps to establish a competing business that would have violated the terms of the parties' initial non-compete agreement and that he intended to collaborate with employer's competitor. The court stated:

Whether Engel had a fiduciary duty to disclose the creation of the competing business Caputech and his plans to associate with Matrikon depends on what his job responsibilities were at PAS. If the fact-finder determines that his job responsibilities were those of a fiduciary, in dealing with his principal on a matter involving his own self-interest that would limit his employer's contractual rights, he owed a duty of full disclosure of all material facts. *See Navigant Consulting, Inc. v. Wilkinson*, 508 F.3d 277, 285 (5th Cir. 2007) (holding fiduciary employee had duty to disclose plans

to compete with employer when employee negotiated lease on behalf of employer and employer would be burdened with substantial lease payments when employee left); *see also Abetter Trucking*, 113 S.W.3d at 510 (noting fiduciary employee has duty to deal openly with employer about matters affecting the employer's business). If so, he could not legally put his interests above that of PAS "by a course of conduct designed to hurt [PAS]." *Johnson*, 73 S.W.3d at 202.

Id. at 614.

A similar result was reached in *AmeriPath, Inc. v. Hebert*, 447 S.W.3d 319 (Tex. App.—Dallas 2014, pet. denied). There, Hebert, a pathologist, was bound by a non-compete agreement with DFW, an entity owned by AmeriPath. He resigned and took employment with a competitor, ProPath. His move was facilitated by a contract he signed in 2008 with an AmeriPath client, Columbia Medical Center of McKinney (the "Hospital"), on behalf of DFW. The agreement contained a key-man provision, which essentially provided that if Hebert was no longer employed by DFW, then his agreement not to compete was waived as to the Hospital. Thus, when Hebert resigned, the client Hospital followed him to ProPath, and Hebert took the position he was not violating his non-compete agreement. AmeriPath contended Hebert negotiated his own deal with the Hospital and signed that form of the agreement without authority from AmeriPath, so that he could effectuate a scheme to take the Hospital with him to a new employer without technically violating any non-compete agreement. Hebert also allegedly provided information to ProPath so that it could hire away employees from DFW. The trial court granted summary judgment for Hebert. The Dallas Court of Appeals reversed, finding that appellants had raised material fact questions as to whether Hebert breached his fiduciary duties, "for example, in the process of negotiating his employment with ProPath, taking the business of the Hospital from appellants to ProPath, and enabling the move of other employees of appellants to ProPath's employ." *Id.* at 341.

VI. THE DEFEND TRADE SECRETS ACT OF 2016³

A. Overview

On May 11, 2016, President Obama signed into law the Defend Trade Secrets Act of 2016 (“DTSA”). The DTSA, which took effect that day, provides a new federal court civil remedy for acts of trade secret misappropriation occurring on or after May 11, 2016. The passage of the DTSA means trade secret owners now have a uniform federal law under which to pursue trade secret misappropriation claims.

The operative provision of the 2016 Defend Trade Secrets Act provides:

An owner of a trade secret that is misappropriated may bring a civil action under this subsection if the trade secret is related to a product or service used in, or intended for use in, interstate or foreign commerce.

The DTSA is an amendment to the Economic Espionage Act (“EEA”), 18 U.S.C. §1831, *et seq.* The quoted provisions will be inserted in the EEA at 18 U.S.C. § 1836(b). The EEA has been around since 1996, but until now was primarily a criminal law enforcement statute that did not provide for a private right of civil action. The DTSA now provides for civil claims and original (but not exclusive) jurisdiction in federal court over claims brought under the statute.

There are several key features to the DTSA of particular interest to employers. The DTSA:

- Provides uniform definitions for “trade secrets” and “misappropriation” that are generally consistent with the Uniform Trade Secrets Act but with a few differences.
- Allows for a civil action in federal courts, providing a uniform set of procedural and evidentiary rules (the Federal Rules of Civil Procedure and Rules of Evidence).

³ This section of the paper is from an outstanding article written by lawyers from Littler Mendelson P.C., that may be found at: <https://www.littler.com/publication-press/publication/trade-secrets-finally-get-federal-law-protection>.

- Allows for the seizure of trade secrets from an alleged misappropriator without notice or an evidentiary hearing in extraordinary circumstances.
- Provides for a variety of different remedies including injunctive relief (for actual and threatened misappropriation), damages (under a variety of different theories), and exemplary damages (up to two times the amount of damages).
- Limits injunctive relief that can be awarded to avoid conflicts with state law limitations regarding noncompete contracts and other restraints of trade.
- Allows a prevailing party to recover attorneys' fees under certain conditions.
- Provides protection from prosecution for whistleblowers and retaliation claimants.
- Requires that employers provide employees notice of the whistleblower protection in order to preserve the ability to recover attorneys' fees or exemplary damages.
- Does not preempt or eliminate state law claims and remedies related to trade secrets, or modify other federal laws on intellectual property or unauthorized computer access.
- Has a three-year statute of limitations that applies a discovery rule.
- Addresses *international* trade secret theft and economic espionage.

B. Specific Provisions of the DTSA

1. Uniform Definitions

The DTSA retains most of the definition of “trade secrets” used in the Economic Espionage Act, which generally follows the UTSA definition. Under this definition, the term “trade secrets” covers “all forms and types of” information, regardless of how stored, where:

the owner thereof has taken reasonable measures to keep such information secret; and

the information derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable

through proper means by another person who can obtain economic value from the disclosure or use of the information; ...

The DTSA adds definitions for “misappropriation” and “improper means” to the Economic Espionage Act.

Under the DTSA definition, the term “misappropriation” tracks the UTSA and divides misappropriation into two categories: (1) improper acquisition and (2) improper use or disclosure. More specifically, it provides that “misappropriation” means:

- 1) acquisition of a trade secret of another by a person who knows or has reason to know that the trade secret was acquired by improper means; or
- 2) disclosure or use of a trade secret of another without express or implied consent by a person who
 - a) used improper means to acquire knowledge of the trade secret; or
 - b) at the time of disclosure or use, knew or had reason to know that his/her knowledge of the trade secret was
 - i. derived from or through a person who had utilized improper means to acquire it;
 - ii. acquired under circumstances giving rise to a duty to maintain its secrecy or limit its use; or
 - iii. derived from or through a person who owed a duty to the person seeking relief to maintain its secrecy or limit its use; or
 - c) before a material change of his or her position, knew or had reason to know that it was a trade secret and that knowledge of it had been acquired by accident or mistake.

The DTSA states that “improper means” includes theft, bribery, misrepresentation, breach or inducement of a breach of a duty to maintain secrecy, or espionage through electronic or other means, but does not include reverse engineering, independent derivation, or any other lawful means of acquisition.

2. Uniform Procedures and Evidentiary Standards

The DTSA provides that the U.S. district courts have original jurisdiction over civil actions brought under the law. It is notable that this statement of jurisdiction is not exclusive. This may create issues as to whether pleading a claim under the DTSA is compulsory in certain circumstances if it is going to be preserved, even if the party is attempting to litigate only state law claims in state court. This issue aside, employers will still have the ability to capitalize on uniformity advantages of the DTSA because as long as the action is brought in a federal court, the Federal Rules of Civil Procedure and Federal Rules of Evidence will control instead of state procedural and evidentiary rules.

To avoid unnecessary disputes related to discovery protections, the statute expressly states that a court may *not* authorize or direct the disclosure of any information the owner asserts to be a trade secret unless the court allows the owner the opportunity to file a submission under seal that describes the interest of the owner in keeping the information confidential. And, providing information relating to a trade secret to the government or a court in connection with a prosecution under the DTSA constitutes no waiver of trade secret protection unless the trade secret owner expressly consents to such waiver.

3. Seizure Feature

A unique feature of the DTSA is its seizure of evidence provisions. The legislature recognized significant concerns over the potential for trade secrets to be compromised through use that destroys the value of its secret nature before an evidentiary hearing can be held, and the possibility of destruction of evidence or its removal from the country by a misappropriator as soon as the person or entity learns legal action is being taken. Consequently, the law provides for the ability of a party to, on an *ex parte* basis (meaning without notice to the opposing party), apply for and secure an order from a court to have the trade secret material seized by law enforcement authorities (state or federal) – thereby removing the trade secret information from the alleged misappropriator's possession until an evidentiary hearing can be held.

However, the DTSA also expressed the sense of Congress that it is important when applying this seizure mechanism to balance the need to prevent or remedy misappropriation against both (a) legitimate interests of the party accused of wrongdoing and (b) the need to avoid interrupting the business of third parties. The seizure mechanism is an extraordinary remedy and has several safeguards. These safeguards include the requirement to show “extraordinary circumstances” such as evidence that a normal court order would not be complied with by the alleged misappropriator, or that immediate irreparable injury will occur absent seizure, and that the risk of harm to the business is greater than that to the misappropriator or third parties. The entity alleging misappropriation must also show it is likely to prevail on the merits. In addition, the entity cannot have publicized the requested seizure.

The seizure order must contain provisions protecting the confidentiality of the information, provide guidance to law enforcement officials executing the seizure on their scope of authority, and require the applicant to post a bond or other security. An evidentiary hearing is then set to determine whether the seizure order should remain in place. The applicant must prove the elements to sustain the seizure.

The DTSA contains provisions prohibiting publicity of the seizure that might damage the alleged misappropriator. There are special provisions covering materials held in the custody of the court as well, such as rules regarding the storage medium, steps to be taken to protect the confidentiality of the materials seized, and appointment of a special master to handle logistical matters. And, a party or a person who claims to have an interest in the subject matter seized may make a motion at any time, which may be heard *ex parte*, to encrypt any material seized.

Abuse of the seizure mechanism has consequences. A party that can prove it was damaged by a wrongful or excessive seizure order can potentially obtain lost profits, costs of materials, loss of goodwill, punitive/exemplary damages and attorneys' fees.

4. Injunctive Relief Standards

The DTSA expressly provides for injunctive relief as a remedy to prevent any actual or threatened misappropriation “on such terms as the court deems reasonable.” It allows for an injunction requiring a party to take affirmative actions to protect a trade secret. And, under exceptional circumstances that render an injunction inequitable, the future use of the trade secret can be conditioned on the payment of a reasonable royalty to the trade secret owner for as long a period of time as the misappropriators could have been prohibited from using the trade secret.

However, there are also some unique limitations to injunctive relief under the DTSA. The DTSA provides that an injunction under the statute may not prevent a person from entering into an employment relationship, and any conditions or limitations placed on an individual’s employment as a result of an injunction must be based on evidence of threatened misappropriation and not “merely” the fact that the individual knows certain information. This signals a limitation on the use of the inevitable disclosure doctrine as it has been applied in some jurisdictions.

In addition, the injunction cannot conflict with an applicable state law prohibiting restraints on the practice of a lawful profession, trade or business. This is clearly intended to create some deference to state noncompete statutes such as the law in California that would prohibit or put significant limits on actions that restrain an employee’s employment options. *See* Cal. Bus. & Prof. Code § 16600.

5. Whistleblower / Retaliation Claim Immunity Protections

The DTSA contains a provision designed to protect whistleblowers. Specifically, it provides that an individual shall not be held criminally or civilly liable under any federal or state trade secret law for the disclosure of a trade secret that is made “in confidence” to a federal, state, or local government official, either directly or indirectly, or to an attorney, provided that: it is disclosed “solely for the purpose of” reporting or investigating a suspected violation of law, or is made in a complaint or other document

filed in a lawsuit or other proceeding filed under seal so that it is not disclosed to the public.

The law also contains an anti-retaliation provision. Under the DTSA, an individual who files a lawsuit for retaliation stemming from the employer's suspected law violation may disclose the trade secret to his/her attorney and use the trade secret information in the court proceeding, provided the individual files any document containing the trade secret under seal, and does not disclose the trade secret, except pursuant to court order.

6. Notice Requirement

The DTSA provides that employers must give notice of the immunity provisions of the law described above in any contract or agreement with an employee that governs the use of a trade secret or other confidential information. An employer will be deemed to be in compliance with this notice requirement if it provides a cross-reference to a policy document provided to the employee that describes the employer's reporting policy for a suspected law violation.

If an employer does not comply with the notice requirement described above, the employer may not be awarded exemplary damages or attorneys' fees under the statute in an action against an employee who misappropriates trade secrets. The notice obligation for contracts applies only to contracts that are entered into or updated after the date of enactment of the DTSA. Consequently, the law does not require employers to replace existing contracts with new ones. However, for existing employees, even if an existing contract is not replaced or modified, notice of a policy amendment applicable to the employee that provides notice of the immunity protection is still advisable.

Notably, the DTSA's definition of "employee" for these protections is expansive. It defines employee to include not only ordinary employees but also "any individual performing work as a contractor or consultant for an employer." This suggests that there is a need to examine not only ordinary employee policy documents for

purposes of the statutory notice but also independent contractor and consultant agreements.

7. No Preemptive Effect

The DTSA has no preemptive effect on other trade secret protection laws. It is part of the Economic Espionage Act, which already provides that it “shall not be construed to preempt or displace any other remedies, whether civil or criminal, provided by United States Federal, State, commonwealth, possession, or territory law for the misappropriation of a trade secret, or to affect the otherwise lawful disclosure of information by any Government employee under section 552 of title 5 (commonly known as the Freedom of Information Act).” The DTSA confirms that it retains this limitation by stating that “[n]othing in the amendments made by this section shall be construed to modify the rule of construction under section 1838 of title 18, United States Code, or to preempt any other provision of law.”

The DTSA expressly provides that it will not be construed to be “a law pertaining to intellectual property” for purposes of any other act of Congress (presumably intended to distinguish it from federal patent, trademark, and copyright laws). And, while there are whistleblower and retaliation claimant protections in the DTSA, the DTSA is also clear in stating that nothing in its protections will be construed to “authorize, or limit liability for, an act that is otherwise prohibited by law, such as unlawful access of matter by unauthorized means.” This would presumably include conduct such as trespass, ordinary theft, or unauthorized access to a computer system that would violate the Federal Computer Fraud and Abuse Act.

8. Statute of Limitations

A civil action under the DTSA may not be commenced later than three years after the date on which the misappropriation is discovered or by the exercise of reasonable diligence should have been discovered. For these purposes, “a continuing misappropriation constitutes a single claim of misappropriation.”

This single-claim construction that triggers the running of the statute of limitations is the same construction used in the UTSA. Consequently, there is a considerable body of law to help guide employers on the timing issues it creates. However, this does not mean that the issue is without wrinkles. The knowledge and intent elements in the definition of “misappropriation” have created some difficult issues with the statute of limitations under the UTSA, and those will likely carry through to the DTSA.

9. **Enhanced Focus on International Trade Secret Theft**

A significant part of the congressional focus on trade secret laws that gave birth to the DTSA was concern over international economic espionage. There is no uniformly applicable international law or treaty that specifically addresses the protection of trade secrets, and the protections that do exist within the rules of the World Trade Organization and similar bodies have significant weaknesses. Some have argued that “the United States has not consistently received cooperation from international jurisdictions in protecting trade secrets in part because it does not have its own federal civil statute to reference in encouraging the adoption and enforcement of similar legislation by its treaty partners.” See *Trade Secrets: Promoting and Protecting American Innovation, Competitiveness and Market Access in Foreign Markets: Hearings Before the House Judiciary Comm., Subcomm. on Courts, Intellectual Property and Internet*, 113th Cong. 2d Sess. (2014) (statement of Thaddeus Burns, Senior Counsel, General Electric, on behalf of the Intellectual Property Owners Association). The DTSA remedies this problem.

There are also a number of features in the DTSA (beyond the importance of its existence as a *federal* law protecting trade secrets) that are designed to help focus on and address the international theft issue. The seizure feature is expressly designed to be used “in instances in which a defendant is seeking to flee the country ...”, as well as in other circumstances. S. Rept. 114-220, at 6. And, the DTSA requires the Attorney General to make a biannual report to the House and Senate Judiciary Committees on international trade secret theft affecting U.S. companies. The report is to include recommendations for

legislative and executive actions to address the problem along with educational material for U.S. companies to help protect themselves and to provide a means for U.S. companies to report any theft occurring outside the United States.

10. **Practical Takeaways**

Employers looking to take advantage of the new options provided under the DTSA should consider the following practical measures:

- 1 Examine contracts and confidential information protection policies with employees and independent contractors to evaluate the need for notice language regarding the DTSA whistleblower and retaliation claimant protections. Inclusion of this language can help preserve remedies for misappropriation.
- 2 Examine contracts covering confidential information and/or trade secrets and consider the use of savings clause language to help safeguard rights provided under the DTSA.
- 3 Examine applicable state law options in the most likely states for a legal action involving your company (e.g., the location of the principal place of business), and identify *in advance* any substantive and procedural advantages of the state law versus the new federal law (DTSA) so that a decision on which option to pursue (state or federal court action) can be made more quickly when need for injunctive relief arises.
- 4 Examine hiring and on-boarding procedures to make sure that reasonable steps are being taken to avoid newly hired employees bringing trade secrets of a prior employer into the workplace or using them.
- 5 Examine employee termination and exit processing procedures to ensure appropriate protocols are in place to secure the return of confidential and trade secret information that might be in a departing employee's possession or control, and to identify criteria indicative of the possible need to pursue a seizure order.

- 6 Consider establishing an identification process to flag in advance trade secret information that is of the highest priority to protect, and that might require the pursuit of a seizure order if misappropriated.
- 7 If international theft is a concern, monitor the biannual reports from the Attorney General to Congress and the recommendations and educational materials generated by this process, and evaluate reporting options to be pursued so that the company's industry is appropriately represented in any future congressional evaluations and developments on the issue.

VII. UPDATE ON PROTECTING OR OBTAINING TRADE SECRETS DURING DISCOVERY IN STATE AND FEDERAL COURT

The issue of protecting or obtaining trade secrets during discovery arises in both Texas state court and federal court litigation. Cases regarding this subject in state and federal court are summarized below.

A. Protecting Or Obtaining Trade Secrets During Discovery In Texas State Court

1. Pre-TUTSA Law

Rule 507 of the Texas Rules of Evidence provides for the protection of trade secrets:

A person has a privilege, which may be claimed by the person or the person's agent or employee, to refuse to disclose and to prevent other persons from disclosing a trade secret owned by the person, if the allowance of the privilege will not tend to conceal fraud or otherwise work injustice. When disclosure is directed, the judge shall take such protective measure as the interests of the holder of the privilege and of the parties and the furtherance of justice may require.

TEX. R. EVID. 507.

The trade secret privilege seeks to accommodate two competing interests. *In re Continental Gen. Tire, Inc.*, 979 S.W.2d 609, 612 (Tex. 1998) (orig. proceeding). First, it recognizes that trade secrets are an important property interest, worthy of protection. *Id.* Second, it recognizes the importance placed on fair adjudication of lawsuits. *Id.* Rule 507 accommodates both interests by requiring a party to disclose a trade secret only if necessary to prevent “fraud” or “injustice.” *Id.* Disclosure is required only if necessary for a fair adjudication of the requesting party’s claims or defenses. *Id.*

The party asserting the trade secret privilege has the burden of proving that the discovery information sought qualifies as a trade secret. *In re Bass*, 113 S.W.3d 735, 737 (Tex. 2003) (orig. proceeding). If the resisting party meets its burden, the burden shifts to the party seeking the trade secret discovery to establish that the information is necessary for a fair adjudication of its claim. *Id.* It is an abuse of discretion for the trial court to order production once trade secret status is proven if the party seeking production has not shown necessity for the requested materials. *Id.* at 738.

As mentioned above, to determine whether a trade secret exists, the following six factors are weighed in the context of the surrounding circumstances: (1) the extent to which the information is known outside of the business; (2) the extent to which it is known by employees and others involved in the business; (3) the extent of measures taken to guard the secrecy of the information; (4) the value of the information to the business and to its competitors; (5) the amount of effort or money expended in developing the information; and (6) the ease or difficulty with which the information could be properly acquired or duplicated by others. *In re Union Pac. R.R. Co.*, 294 S.W.3d 589, 592 (Tex. 2009) (orig. proceeding) (per curiam). The party claiming a trade secret is not required to satisfy all six factors because trade secrets do not fit neatly into each factor every time. *In re Bass*, 113 S.W.3d at 740.

The Texas Supreme Court has not stated conclusively what would or would not be considered necessary for a fair adjudication; instead, the application depends on the circumstances presented. *In re Bridgestone/Firestone, Inc.*, 106 S.W.3d 730, 732 (Tex.

2003) (orig. proceeding). The degree to which information is necessary depends on the nature of the information and the context of the case. *Id.* However, “the test cannot be satisfied merely by general assertions of unfairness.” *Id.* “Just as a party who claims the trade secret privilege cannot do so generally but must provide detailed information in support of the claim, so a party seeking such information cannot merely assert unfairness but must demonstrate with specificity exactly how the lack of the information will impair the presentation of the case on the merits to the point that an unjust result is a real, rather than a merely possible, threat.” *Id.* at 732-33. An appellate remedy does not exist if a trial court orders a party to produce privileged trade secrets absent a showing of necessity. *In re Bass*, 113 S.W.3d at 745. Hence mandamus is an appropriate vehicle to challenge such an order. *Id.*

In 2010, the Houston First Court of Appeals decided *In re Cooper Tire & Rubber Co.*, 313 S.W.3d 910 (Tex. App.–Houston [14th Dist.] 2010, no pet.). The plaintiffs were involved in a head-on collision when the tread came off a Cooper Weather Master S/T tire on Dustin Langstaff’s vehicle, causing him to lose control. They sued Cooper in the Harris County 127th District Court for strict liability, negligence, and defects in design, manufacturing and marketing. The suit alleged specifically that Cooper failed to use belt edge gumstrips, or BEGs, in the Weather Master, which purportedly would have made the tire safer.

The plaintiffs sought documents on a different model Cooper tire in order to show that the company had added and removed BEGs from that tire. They claimed the data could establish that Cooper knew of the Weather Master defect, and that BEGs would rectify the problem, but continued to produce the defective tires. Cooper countered that the information was not relevant and that the documents contained trade secrets. The trial court ordered Cooper to disclose the documents under a protective order but did not rule on the trade secret issue. The tire maker then filed a petition for writ of mandamus, asking the appeals court to set aside the trial judge’s order. Granting the petition, the court found that five of the six factors that determine whether trade secrets exist all

weighed in favor of Cooper's argument. The factors involved the extent to which people inside and outside Cooper's business already know the information, what measures Cooper took to guard the data, the information's value to Cooper, and the ease or difficulty with which other parties could properly obtain or duplicate the data. The court concluded that the plaintiffs did not establish that they needed the trade secret information for a fair hearing on their claim. Accordingly, the panel concluded that the trial court abused its discretion in ordering Cooper to produce the documents. *Id.* at 919.

Also in 2010, the Dallas Court of Appeals issued a very similar decision. *See In re Goodyear Tire & Rubber Co.*, NO. 05-10-00485-CV, 2010 WL 2510371 (Tex. App.—Dallas June 23, 2010, no pet.) (also finding that the trial court abused its discretion in ordering the production of trade secrets).

2. Post-TUTSA Law

As set forth above, Texas Rule of Evidence 507 provides that trade secret information is privileged and need not be disclosed absent protective measures imposed by the court. But prior to the enactment of TUTSA, there was no specific provision in Texas law for protecting the secrecy of a trade secret during court proceedings. Instead, parties ordinarily requested the court to enter a protective order under general discovery rules. Parties would also seek to seal court records using the cumbersome procedures outlined in Texas Rule of Civil Procedure 76(a), which requires public notice and the public's opportunity to be heard. Section 134A.006 of TUTSA provides a new rule governing the disclosure of trade secrets during a court proceeding:

In an action under this chapter, a court shall preserve the secrecy of an alleged trade secret by reasonable means. There is a presumption in favor of granting protective orders to preserve the secrecy of trade secrets. Protective orders may include provisions limiting access to confidential information to only the attorneys and their experts, holding in-camera hearings, sealing the records of the action, and ordering any person

involved in the litigation not to disclose an alleged trade secret without prior court approval.

TUTSA thus provides the ability for aggrieved parties to pursue their legal rights in court without fear of having to disclose the very information they are trying to keep secret. Consistent with that point, in 2016, the Texas Supreme Court ruled that Section 134A.006 of TUTSA authorized a trial court, in an action involving claims for breach of a non-compete agreement and misappropriation of trade secrets, to conduct portions of a temporary injunction hearing involving alleged trade secrets outside the presence of the designated representative of a party defendant to which the secret had not yet been disclosed. *See In re M-I L.L.C.*, 505 S.W.3d 569 (Tex. 2016) (orig. proceeding).

B. Protecting Or Obtaining Trade Secrets During Discovery In Federal Court

The federal rules allow a court, in the discovery context, to “make any order which justice requires to protect a party or person from . . . undue burden or expense, including . . . that a trade secret or other confidential research, development, or commercial information not be revealed or be revealed only in a designated way” FED. R. CIV. P. 26(c)(7). Federal courts applying this rule recognize that “[t]here is no absolute privilege for trade secrets and similar confidential information.” *Federal Open Mkt. Comm. v. Merrill*, 443 U.S. 340, 362, 99 S. Ct. 2800, 61 L.Ed.2d 587 (1979) (quoting 8 Wright & Miller, *Federal Practice and Procedure* § 2043, at 300 (1970)); *see also Centurion Indus. v. Warren Steurer & Assocs.*, 665 F.2d 323, 325 (10th Cir. 1981); *National Util. Serv., Inc. v. Northwestern Steel & Wire Co.*, 426 F.2d 222, 227 (7th Cir. 1970); *A.H. Robins Co. v. Fadely*, 299 F.2d 557, 561 (5th Cir. 1962); *Kleinerman v. United States Postal Serv.*, 100 F.R.D. 66, 69 (D. Mass. 1983); 6 Moore’s *Federal Practice* § 26.46[16], at 26.144 (3d ed. 1998). Rather, federal courts apply a balancing test with shifting burdens.

Specifically, in federal court, the party resisting discovery must establish that the information sought is indeed a trade secret and that disclosure would be harmful. The burden then shifts to the requesting party to establish that the information is “relevant and

necessary” to his or her case. If the trial court orders disclosure, it should enter an appropriate protective order. *See, e.g.*, 8 Wright & Miller, Federal Practice & Procedure § 2043 (1994); *see also, e.g.*, *American Standard, Inc. v. Pfizer Inc.*, 828 F.2d 734, 740- 41 (Fed. Cir. 1987); *Heat & Control, Inc. v. Hester Indus., Inc.*, 785 F.2d 1017, 1025 (Fed. Cir. 1986); *Centurion Indus. v. Warren Steurer & Assocs.*, 665 F.2d 323, 325 (10th Cir. 1981); *In re Independent Serv. Org. Antitrust Litig.*, 162 F.R.D. 355, 356 (D. Kan. 1995); *Exxon Chem. Patents, Inc. v. Lubrizol Corp.*, 131 F.R.D. 668, 671 (S.D. Tex. 1990); *Culligan v. Yamaha Motor Corp.*, 110 F.R.D. 122, 125 (S.D.N.Y. 1986). *Cf. Kleinerman v. United States Postal Serv.*, 100 F.R.D. 66, 69 (D. Mass. 1983) (discovery of trade secrets required where “the issues cannot be fairly adjudicated unless this information is available”) (quoting *Melori Shoe Corp. v. Pierce & Stevens, Inc.*, 14 F.R.D. 346, 347 (D. Mass. 1953)); *Duplan Corp. v. Deering Milliken, Inc.*, 397 F. Supp. 1146, 1185 (D. S.C. 1974) (“[T]he courts are loath to order disclosure of trade secrets absent a clear showing of an immediate need for the information requested.”) (quoting 4 Moore’s Federal Practice, ¶ 26.60[4], at 242-45 (2d ed.1970)).

This is ultimately a balancing test, in which the trial court must weigh all pertinent facts and circumstances. *See Wright & Miller*, § 2043 at 559 (“[T]he burden is on the party seeking discovery to establish that the information is sufficiently relevant and necessary to his case to outweigh the harm disclosure would cause to the person from whom he is seeking the information.”). *See also Centurion Indus.*, 665 F.2d at 325 (“The district court must balance the need for the trade secrets against the claim of injury resulting from disclosure.”).

In *Farouk Systems, Inc. v. Costco Wholesale Corp.*, 700 F. Supp. 2d 780 (S.D. Tex. 2010), Judge Keith Ellison found that although “supplier information [regarding Costco’s suppliers] sought by Farouk is a trade secret, Farouk has adequately demonstrated that it needs this information to effectively adjudicate its claims and defenses.” *Id.* at 788. Judge Ellison rejected Costco’s argument that disclosure only occur after Farouk made out a colorable claim. *Id.* Judge Ellison entered a protective

order limiting disclosure to Farouk's outside counsel "unless, after receiving the information, outside counsel finds that it cannot reasonably use the disclosed information, [in which case] it may make a motion with this Court to designate a neutral third party with knowledge of the industry to examine the issue." *Id.* at 789. Costco also proposed that the protective order restrict Farouk from using the information found in Costco's trade secrets to sue suppliers that sold Farouk products to Costco. Judge Ellison rejected that proposal, stating that "the Court does not consider it appropriate to require Farouk to relinquish its substantive rights simply to obtain discovery in this matter." *Id.*

In *M-I LLC v. Stelly*, 733 F. Supp. 2d 759 (S.D. Tex. 2010), Judge Ellison again ordered discovery of trade secrets. This time, the lawsuit was a misappropriation of trade secrets case. The defendants, however, still resisted discovery of their alleged trade secrets. In rejecting the defendants' arguments, Judge Ellison stated:

Parties are generally given wide latitude in conducting discovery, even as to trade secret matters. Indeed, in most cases concerning trade secret discovery, "the key issue is not whether the information will be disclosed but under what conditions." 8 CHARLES ALAN WRIGHT, ARTHUR R. MILLER & RICHARD L. MARCUS, FEDERAL PRACTICE AND PROCEDURE § 2043 (2d ed. 1994). The Supreme Court has recognized that "orders forbidding any disclosure of trade secrets or confidential commercial information are rare." *Federal Open Mkt. Comm. v. Merrill*, 443 U.S. 340, 362, 99 S. Ct. 2800, 61 L.Ed.2d 587 (1979). "More commonly, the trial court will enter a protective order restricting disclosure to counsel, or to the parties." *Id.* (internal citations omitted). Defendants have failed to cite to any federal cases that prohibited trade secret disclosure outright. Indeed, from the Court's own research, it is clear that such action is exceedingly rare. Defendants have failed to set forth compelling reasons for why this material should be entirely exempt from discovery. The Court

finds that the material is relevant and necessary to the claims at issue in this case.

Id. at 804.

Regarding third-party discovery, if a subpoena “requires disclosure of a trade secret or other confidential research, development, or commercial information,” and the party seeking discovery “shows a substantial need for the . . . material that cannot otherwise be met without undue hardship . . . , the court may order . . . production only upon specified conditions.” FED. R. CIV. P. 45(c)(3)(B). The court must balance the need for discovery by the requesting party and the relevance of the discovery to the case against the harm, prejudice or burden to the other party. *Truswal Systems Corp. v. Hydro-Air Engineering, Inc.*, 813 F.2d 1207, 1210 (Fed. Cir. 1987). One factor to be considered in assessing the burden of complying with a subpoena is whether the moving party is a non-party to the litigation. *Truswal Systems Corp.*, 813 F.2d at 1210. Modification of a subpoena is preferable to quashing it. *Tiberi v. CIGNA Ins. Co.*, 40 F.3d 110, 112 (5th Cir. 1994).

Rule 45 provides that a court may place conditions upon the production of documents where the request requires disclosure of a trade secret or other confidential commercial information and the party seeking discovery shows a substantial need for the material that cannot otherwise be met without undue hardship. FED. R. CIV. P. 45(c)(3)(B). The moving party has the burden to establish that the information sought is a trade secret and that its disclosure might be harmful. *Exxon Chemical Patents, Inc.*, 131 F.R.D. at 671. Disclosure to a competitor is presumptively more harmful than disclosure to a non-competitor. *Echostar Communications Corp. v. The News Corp. Ltd.*, 180 F.R.D. 391, 395 (D. Co. 1998). If the moving party meets its burden of proof, the burden then shifts to the party seeking discovery to show that the requested information is relevant and necessary. *Id.* The court then balances the need for the trade secrets against the claim of injury resulting from disclosure. *Id.* Even if the requested documents are relevant, discovery will not be permitted if the party seeking discovery fails to show need

or if the potential harm caused by production outweighs the benefit. *Mannington Mills, Inc. v. Armstrong World Industries, Inc.*, 206 F.R.D. 525, 529 (D. Del. 2002).

In *Cmedia, LLC v. LifeKey Healthcare, LLC*, 216 F.R.D. 387, 391 (N.D. Tex. 2003), the court applied these rules and found that the third-party's trade secrets and confidential information had to be produced, but "in such a manner as to assure confidentiality. These documents will be produced subject to a protective order which restricts disclosure of privileged documents to the attorneys involved in the litigation and independent experts, and which ensures return of all documents, including copies, to Koepfel within a reasonable time after conclusion of the litigation or certification of destruction thereof."

VIII. KEY MISAPPROPRIATION OF TRADE SECRETS CASES

A. Damages Issues In Trade Secrets Cases

"Damages in misappropriation cases can take several forms: the value of plaintiff's lost profits; the defendant's actual profits from the use of the secret, the value that a reasonably prudent investor would have paid for the trade secret; the development costs the defendant avoided incurring through misappropriation; and a reasonable royalty." *In re Mandel*, 578 Fed. Appx. 376 (5th Cir. 2014) (footnote omitted). For claims accruing on or after September 1, 2013, TUTSA governs. *See* TEX. CIV. PRAC. & REM. CODE § 134A.001–.008. Remedies available under TUTSA include injunctive relief; damages measured by actual loss plus unjust enrichment not included in computing actual loss; a reasonable royalty; and exemplary damages capped at two times actual damages. *Id.* §§ 134A.003, 134A.004. These remedies are largely consistent with those available at common law, although, under TUTSA, attorneys' fees are also available to the plaintiff if wilful and malicious misappropriation exists. *Id.* at 134A.005(3).

In *Wellogix, Inc. v. Accenture, L.L.P.*, 716 F.3d 867, 874 (5th Cir. 2013), the Fifth Circuit U.S. Court of Appeals affirmed a verdict of more than \$40 million in a trade secrets misappropriation case. Wellogix developed software to sell to companies in the oil and gas industry. The software was designed to help them manage complex projects.

Wellogix contracted with Accenture for Accenture to market the software, and shared its source code and other technology with Accenture, subject to a confidentiality agreement. Later, however, Accenture, SAP, and BP worked together to develop a competing software, and accessed Wellogix's technology and source code to do so. Wellogix sued all three companies — BP, SAP, and Accenture. Only Accenture went to trial. After a nine day trial, the jury awarded Wellogix \$26.2 million in actual damages, and \$68.2 million in punitive damages. The district court judge, the Honorable Keith Ellison, entered judgment on the jury verdict, with the exception of remitting the punitive damages award to the amount Wellogix had requested at trial, \$18.2 million. Accenture appealed.

The Fifth Circuit affirmed the judgment against Accenture in all respects. It found that there was sufficient evidence that Accenture had indeed misappropriated Wellogix's trade secrets, and made "use" of them. As the Court observed, "use" is defined broadly under Texas law, to mean:

[A]ny exploitation of the trade secret that is likely to result in injury to the trade secret owner or enrichment to the defendant is a use.... Thus, marketing goods that embody the trade secret, employing the trade secret in manufacturing or production, relying on the trade secret to assist or accelerate research or development, or soliciting customers through the use of information that is a trade secret all constitute use.

Id. at 877 (internal quotation marks and citations omitted).

As for the actual damages award, Wellogix presented proof that venture capital firms had valued Wellogix's worth at approximately \$26.2 million before Accenture's misappropriation, and zero after the misappropriation. Wellogix also presented evidence that Accenture itself had indicated in documents that the BP work alone was worth more than \$20 million, so long as it could keep Wellogix out of it. An expert testified that Wellogix's sole worth was from the technology that had been misappropriated, and evidence showed that during the relevant time, Wellogix was the only company with the

technology at issue. Regarding punitive damages, the court found there was sufficient evidence that Accenture acted with malice, citing to a plethora of e-mails Accenture employees wrote boasting of its ability to “harvest” Wellogix’s technology and its desire to interfere with Wellogix’s business relationships, even though it knew that its conduct was legally questionable.

In *Bohnsack v. Varco, L.P.*, 668 F.3d 262 (5th Cir. 2012), the Fifth Circuit affirmed a \$600,000.00 damages award in a trade secrets misappropriation case, based on what a reasonable investor would have paid for the secrets, observing that:

Damages in misappropriation cases can take several forms: the value of plaintiff’s lost profits, *Jackson v. Fontaine’s Clinics, Inc.*, 499 S.W.2d 87, 89–90 (Tex. 1973); the defendant’s actual profits from the use of the secret, *Elcor Chem. Corp. v. Agri–Sul, Inc.*, 494 S.W.2d 204, 214 (Tex. Civ. App.–1973); the value that a reasonably prudent investor would have paid for the trade secret, *Precision Plating & Metal Finishing Inc. v. Martin–Marietta Corp.*, 435 F.2d 1262, 1263–64 (5th Cir. 1970); the development costs the defendant avoided incurring through misappropriation, *Univ. Computing Co. v. Lykes–Youngstown Corp.*, 504 F.2d 518, 535–36 (5th Cir. 1974) (applying Georgia law); and a “reasonable royalty,” *Elcor Chem. Corp.*, 494 S.W.2d at 214. This variety of approaches demonstrates the “flexible” approach used to calculate damages for claims of misappropriation of trade secrets. *See Univ. Computing*, 504 F.2d at 535.

Id. at 280.

In *Bianco v. Globus Medical, Inc.*, 53 F. Supp. 3d 929, 943 (E.D. Tex. 2014), *aff’d*, 618 Fed.Appx. 1032 (Fed. Cir. 2015), the jury awarded the plaintiff royalty damages of five percent of net sales before trial. The plaintiff’s request for ongoing royalties in lieu of a permanent injunction was granted, but the parties were unable to agree on the post-trial royalty rate. The district court concluded that the post-trial royalty

would continue to be five percent of net sales, with the royalty payment period terminating 15 years after July 1, 2007.

In *Calce v. Dorado Exploration, Inc.*, 309 S.W.3d 719 (Tex. App.–Dallas 2010, no pet.), the court held that the evidence was not legally sufficient to support jury’s award of \$400,000 in reasonable royalty damages to exploration company on its claim for misappropriation of trade secrets. As the court noted, an appropriate measure of damages in a misappropriation of trade secrets case is a “reasonable royalty.” *Id.* at 738 (citing *Univ. Computing Co. v. Lykes-Youngstown Corp.*, 504 F.2d 518, 536 (5th Cir. 1974)). “This does not mean a simple percentage of actual profits; instead, the trier of fact . . . must determine ‘the actual value of what has been appropriated.’” *Metallurgical Indus. Inc. v. Fourtek, Inc.*, 790 F.2d 1195, 1208 (5th Cir. 1986) (quoting *Vitro Corp. v. Hall Chem. Co.*, 292 F.2d 678, 683 (6th Cir. 1961) and citing *Univ. Computing Co.*, 504 F.2d at 537). While every case involving misappropriation of trade secrets requires a “flexible and imaginative approach” to the problem of damages, certain standards have emerged from the cases. *Univ. Computing Co.*, 504 F.2d at 538-39. As stated by the Fifth Circuit,

If the defendant enjoyed actual profits, a type of restitutionary remedy can be afforded the plaintiff—either recovering the full total of defendant’s profits or some apportioned amount designed to correspond to the actual contribution the plaintiff’s trade secret made to the defendant’s commercial success. Because the primary concern in most cases is to measure the value to the defendant of what he actually obtained from the plaintiff, the proper measure is to calculate what the parties would have agreed to as a fair price for licensing the defendant to put the trade secret to the use the defendant intended at the time the misappropriation took place.

Id. at 539.

In calculating what a fair licensing price would have been had the parties agreed, the trier of fact should consider such factors as the resulting and foreseeable changes in the parties’ competitive posture; prices past purchasers or licensees may have paid; the

total value of the secret to the plaintiff, including the plaintiff's development costs and the importance of the secret to the plaintiff's business; the nature and extent of the use the defendant intended for the secret; and whatever other unique factors in the particular case might have been affected by the parties' agreement, such as the ready availability of alternative processes. *Id.* (citing *Metallurgical Indus. Inc.*, 790 F.2d at 1208 (citing *Univ. Computing Co.*, 504 F.2d at 540)). "Estimation of damages, however, should not be based on sheer speculation." *Id.* If too few facts exist to permit the trier of fact to calculate proper damages, then a reasonable remedy in law is unavailable. *Id.* In that instance, a permanent injunction is a proper remedy for the breach of a confidential relationship. *Id.* (citing *Zoecon Indus. v. Am. Stockman Tag Co.*, 713 F.2d 1174, 1180 (5th Cir. 1983) (citing *Hyde Corp. v. Huffines*, 158 Tex. 566, 314 S.W.2d 763, 778 (1958))). In *Calce*, the court concluded there was no evidence to support the jury's \$400,000.00 damages award. *Id.* at 740-41.

In *Rusty's Weigh Scales and Service, Inc. v. North Texas Scales, Inc.*, 314 S.W.3d 105 (Tex. App.—El Paso 2010, no pet.), the court noted that damages to the owner of the trade secret are an element of a claim for damages based on a misappropriation claim. *Id.* at 109. The court held that the evidence was insufficient to support an award of lost profit damages, in an industrial weigh scale company's action against a competitor for misappropriation of trade secrets based on the competitor's alleged use of the company's software. The company's owner asserted that the company lost \$2 million in profits, but did not prove through documentation that such profits were lost, and did not demonstrate that the alleged loss of profits was caused by loss of customers due to the competitor's use of the company's software. *Id.* at 110-11. The court found that such "proof" amounted to mere speculation of lost profits, and was not sufficient to support any award of damages. *Id.* The court also found that the plaintiff had failed to present clear and convincing proof of "malice," so no award of punitive damages was justified. *Id.* at 113.

Likewise, in *Hunter Bldgs. & Mfg., L.P. v. MBI Global, L.L.C.*, 436 S.W.3d 9, 17-22 (Tex. App.—Houston [14th Dist.] 2014, pet. denied), the court of appeals found the

evidence was insufficient to support a jury's finding that the defendants' misappropriation of trade secrets caused the plaintiff-company to suffer past lost profit damages, and thus reversed the jury's \$4.4 million award for such damages.

In *Southwestern Energy Production Co. v. Berry–Helfand*, 491 S.W.3d 699 (Tex. 2016), Tory Berry-Helfand and Gery Muncey brought misappropriation and theft of trade secrets, fraud, conversion, breach of fiduciary duty, and breach of contract claims against Southwestern Energy Production Company (“SEPCO”) relating to SEPCO’s use of drilling techniques and well locations formulated by Helfand and Muncey. These techniques and well locations related to the James Lime reservoir in East Texas and were referred to as the Pearson Prospects. In early 2005, Helfand and Muncey presented their methodology and geological profile to SEPCO pursuant to a confidentiality and noncompete agreement that “required SEPCO to maintain the information’s confidentiality, use it solely to evaluate the Pearson Prospects for purchase from or development with [Helfand and Muncey] and ‘promptly return or upon request by [Helfand and Muncey], destroy the original and all copies of the Confidential Information’ if the parties failed to reach a written agreement for SEPCO to purchase or develop the properties.”

After evaluating the information provided by Helfand and Muncey, SEPCO made no offer, purportedly because it failed SEPCO’s economic criteria. Helfand and Muncey then approached Petrohawk, who entered into a transaction for the Pearson Prospects on the following terms: (i) a \$1.8 million payment, (ii) a sliding-scale overriding royalty interest (which averaged 3% on these leases), and (iii) a 6.25% after-payout working interest. While negotiations with Petrohawk were ongoing, SEPCO embarked on its own James Lime play. In fact, as early as March 11, 2005, SEPCO’s internal drilling documents identified the James Lime as a “primary” drilling objective. Ultimately, SEPCO acquired 1,888 leases and drilled more than 140 wells—88 of them James Lime horizontal wells—in areas clustered around the sweet spots Helfand and Muncey had identified. These wells had a 100% success rate and generated \$381.5 million in revenue

for SEPCO. Helfand and Muncey learned of SEPCO's successful drilling program and sued the company.

At trial, the jury found SEPCO liable on all claims. With respect to damages, the jury rejected the majority of the damages calculations presented by Helfand and Muncey's expert witness, finding instead that the value of the trade secrets was \$11.445 million and that SEPCO's benefits, profits, or advantages from the trade secrets also totaled \$11.445 million in the past (and \$0 in the future). The jury awarded this same \$11.445 million for the breach-of-contract, breach-of-fiduciary duty, theft, and fraud claims. This damages figure was precisely 3% of the \$381.5 million in revenue SEPCO made from the disputed wells. The trial court ordered an accounting and rendered judgment on the jury's verdict, and awarded an additional \$23.89 million in equitable disgorgement of profits. In total, the trial entered a judgment of over \$40 million.

The Texas Supreme Court addressed two key damages issues: (1) the sufficiency of the evidence supporting the \$11.445 million damages finding for misappropriation of trade secrets, and (2) the availability of equitable disgorgement of profits as a remedy. With respect to the former, the Court noted that "[a] 'flexible and imaginative' approach is applied to the calculation of damages in misappropriation-of-trade-secrets cases." Those damages can take many forms, including (i) value of the plaintiff's lost profits, (ii) the defendant's actual profits from the use of the secret, (iii) the value a reasonably prudent person would have paid for the trade secret, (iv) the development costs the defendant avoided by the misappropriation, and (v) a reasonable royalty.

In this case, the \$11.445 million figure was calculated by using the average 3% overriding royalty with Petrohawk. The Petrohawk deal involved the same trade secrets at issue and negotiations in the same general time frame as Helfand's and Muncey's dealings with SEPCO. The Petrohawk transaction also implicated the same geologic area and attributes and included three of the five counties encompassed in Helfand and Muncey's research. Despite these similarities, the Court rejected the \$11.445 million award because the expert's simple use of the fixed 3% overriding royalty was in error.

While the 3% was an average figure based on the Petrohawk agreement and the track record under that agreement, the Petrohawk transaction actually employed a sliding scale for the overriding royalty. Under this sliding scale, the overriding royalty zeroed out at a specified threshold. The expert's failure to consider the sliding-scale and apply it to the SEPCO wells was found by the Court to be a fatal flaw. Applying the 3% figure across the board resulted in an "incomplete and misleading picture"; in contrast, using the actual sliding scale would have resulted in a more certain result. The Court observed, ". . . relying on imagination is not justified when objective evidence is available." While the Court found that there were damages suffered from SEPCO's misappropriation, the case needed to be remanded for a new trial.

With respect to equitable disgorgement of profits, the Court noted that the jury did not make an award of disgorgement of profits; rather the trial court issued that award and the court of appeals rejected that award when it found no fiduciary existed between SEPCO and Helfand and Muncey. Again, the Court remanded the issue to the trial court, stating that "we have not expressly limited the remedy to fiduciary relationships nor foreclosed equitable relief for breach of trust in other types of confidential relationships." Consequently, "whether disgorgement remains equitable must be determined anew on remand and in light of the liability and value determinations following a new trial."

In *GlobeRanger Corp. v. Software AG United States of Am., Inc.*, 836 F.3d 477 (5th Cir. 2016), the developer of a passive radio frequency identification (RFID) system for commercial use brought action against competitor in state court, alleging trade secret misappropriation. The developer recovered \$15 million at trial. The Fifth Circuit affirmed. The court found that GlobeRanger produced sufficient evidence for a jury to reasonably conclude that at least some portion of its system constituted a trade secret. There was testimony explaining how GlobeRanger's "filtering" technology was unique and its ability to filter large amounts of information in real time added value compared to traditional inventory management systems. In addition, both the value and the difficulty

in reproducing the technology were also shown through emails and testimony from Software AG employees.

The court also found that GlobeRanger proved that Software AG “used” its trade secrets, under the Texas Supreme Court’s broad definition of “use” in *Southwestern Energy Production Co.* as “commercial use by which the offending party seeks to profit from the use of the secret” and that such exploitation includes “relying on the trade secret to assist or accelerate research or development.” *Id.* at 499.

Finally, the court also found that the \$15 million award was not excessive, even though Software AG only earned \$860,000 from its project with the Navy it obtained through its misappropriation, and only could have obtained \$140,000 in cost savings as a result of any misappropriation. The court noted that Texas takes a “‘flexible and imaginative’ approach” to damages calculation in trade secret misappropriation cases that allows calculation of damages based on defendant’s avoided costs.” *Id.* at 499 (citing *Sw. Energy Prod. Co.*, 491 S.W.3d at 710–11). The evidence supported the jury’s conclusion that Software AG avoided \$15 million in costs through its misappropriation.

B. Temporary Injunction Standard In Trade Secrets Cases

In *St. Jude Medical S.C., Inc. v. Janssen-Counotte*, No. A–14–CA–877–SS, 2014 WL 7237411, at *14 (W.D. Tex. Dec. 17, 2014), a post-TUTSA case, the district court judge denied the plaintiff’s motion for a preliminary injunction under TUTSA, stating that “there are still far too many open questions and disputed issues of fact to conclude at this juncture St. Jude S.C. has a substantial likelihood of success on the merits of its misappropriation claim.” The district court found that the plaintiff failed to prove what the trade secrets were that the defendant allegedly misappropriated, that it actually owned the alleged trade secrets, that the defendant obtained them through improper means, or that there was an actual or threatened disclosure. *Id.* at 15-16. Significantly, as to the final point, the district court held (contrary to other courts) that “[t]o show a substantial likelihood of threatened disclosure, St. Jude S.C. must establish more than the facts Janssen is the president of a competitor and possesses trade secret information.” *Id.* at

*16. The district court was also apparently put off by the broad injunction the plaintiff sought, stating:

St. Jude S.C. seeks an injunction prohibiting Janssen from working as the U.S. President of Biotronik or undertaking any job duties for Biotronik in the area of strategic planning, pricing, marketing, or product development of CRM devices and products until at least September 1, 2015. The Court declines to impose such a harsh injunction, especially in light of all the ongoing open questions and disputed fact issues described above. While St. Jude S.C. insists this lawsuit is solely about the protection of its trade secrets, the injunction reflects a desire to prohibit competition where there is no non-competition agreement. A sweeping injunction removing Janssen from her current job is not well-tailored to accomplishing the more narrow goal of preventing her from disclosing any of St. Jude S.C.'s trade secrets she may possess.

Id. at *16.

In *INEOS Group Ltd. v. Chevron Phillips Chemical Co., LP*, 312 S.W.3d 843 (Tex. App.–Houston [1st Dist.] 2009, no pet.), a pre-TUTSA case, the Court of Appeals held that the trial court did not abuse its discretion by finding that the plaintiff-manufacturer was sufficiently vigilant in guarding its polyethylene manufacturing technology such that it was entitled to trade secret protection by a temporary injunction pending trial on the merits. In *INEOS Group Ltd.*, the court observed that, on appeal, the scope of review is limited to the validity of the temporary injunction order. *Id.* at 848. The appellate court does not review the merits of the underlying case. *Id.* Instead, the appellate court determines whether there has been an abuse of discretion by the trial court in granting or denying the relief. *Id.* In making this determination, the appellate court may not substitute its judgment for that of the trial court unless its decision was so arbitrary that it exceeded the bounds of reasonableness. *Id.* Abuse of discretion does not exist if the trial court heard conflicting evidence, and evidence appears in the record that

reasonably supports the trial court's decision. *Id.* A trial court abuses its discretion in granting or denying a temporary injunction when it misapplies the law to the established facts. *Id.* Given the abuse-of-discretion-standard, the appellate court reviews the evidence submitted to the trial court in the light most favorable to the court's ruling, draws all legitimate inferences from the evidence, and defers to the trial court's resolution of conflicting evidence. *Id.*

The court noted that "when deciding whether to grant trade-secret protection through a temporary injunction, a trial court does not determine whether the information sought to be protected is, in law and fact, a trade secret; rather, the trial court determines whether the applicant has established that the information is entitled to trade secret protection pending the trial on the merits." *Id.* at 853 (citing *Sharma v. Vinmar Int'l, Ltd.*, 231 S.W.3d 405, 424 (Tex. App.–Houston [14th Dist.] 2007, no pet.)).

In this case, the main issue was whether the plaintiff had taken adequate steps to protect its trade secrets. The defendant argued that the plaintiff had not, and, therefore, its use of the alleged trade secrets was proper and the trial court had erred in enjoining it from using the alleged trade secrets. The appeals court disagreed. The court noted that the plaintiff introduced testimony that it is unaware that any of the expired secrecy obligations cited by the defendant actually resulted in the unauthorized public disclosure of its trade secrets and that the defendant presented no evidence to the contrary. The court observed that the vast majority of the licenses given by the plaintiff over the past 50 years regarding the alleged trade secrets contain perpetual secrecy clauses. The court also found it noteworthy that the plaintiff introduced evidence detailing the strict security measures it had implemented and maintained over the years to keep the at-issue technology confidential, aside from the secrecy agreements. Accordingly, the court found that trade secret protection was warranted at the temporary injunction stage. *Id.* at 854-55. Here are some other trade secrets cases where courts of appeals found that district courts had not erred in granting temporary injunctions:

- *Reliant Hosp. Partners, LLC v. Cornerstone Healthcare Group Holdings, Inc.*, 374 S.W.3d 488 (Tex. App.–Dallas 2012, pet. denied) (affirming trial court’s decision to issue a temporary injunction in a trade secrets case where a departing executive essentially took his employer’s strategic market plans and gave them all to his new employer).
- *IAC, Ltd. v. Bell Helicopter Textron, Inc.*, 160 S.W.3d 191, 203 (Tex. App.–Fort Worth 2005, no pet.) (affirming trial court’s decision to issue an injunction in a trade secrets case).
- *Fox v. Tropical Warehouse, Inc.*, 121 S.W.3d 853, 860 (Tex. App.–Fort Worth 2003, no pet.) (enjoining ex-employee from selling fish to Wal-Mart, his ex-employer’s main customer, because the only way he won the Wal-Mart account was through his misappropriation and use of his ex-employer’s trade secrets).
- *T-N-T Motorsports, Inc. v. Hennessey Motorsports, Inc.*, 965 S.W.2d 18, 21-22 (Tex. App.–Houston [1st Dist.] 1998, pet. dismiss’d) (affirming grant of temporary injunction against former employees who set up competing business based on their knowledge of their former employer’s confidential information; although ex-employees could stay in business, they could not utilize any of their ex-employer’s trade secrets to do business).
- *Rugen v. Interactive Bus. Sys., Inc.*, 864 S.W.2d 548 (Tex. App.–Dallas 1993, no writ) (grant of temporary injunction against former employee prohibiting employee from using any confidential information obtained from former employer to solicit or transact business with employer’s consultants or customers was not abuse of discretion).
- *Collins v. Ryon’s Saddle & Ranch Supplies, Inc.*, 576 S.W.2d 914, 915-16 (Tex. Civ. App.–Fort Worth 1979, no writ) (affirming temporary injunction prohibiting employee from soliciting or contacting all persons who placed

orders with former employer during employee's term of employment so that the employee "could not benefit from breach of the confidential relationship.").

- *Elcor Chem. Corp. v. Agri-Sul, Inc.*, 494 S.W.2d 204, 212 (Tex. Civ. App.—Dallas 1973, writ ref'd n.r.e.) (entering injunction against former employees who left plaintiff's employment and established their own company based on the fruits of their fiduciary breaches and stating that "the equitable cloak of protection must, of necessity, be full and complete so that those who have acted wrongfully and have breached their fiduciary relationship, as well as those who willfully and knowingly have aided them in doing so, will be effectively denied the benefits and profits flowing from the wrongdoing.").

In the following cases, courts of appeals found that the district courts had properly refused to enter temporary injunctions based on alleged trade secret misappropriation:

- *Dallas Anesthesiology Associates, P.A. v. Texas Anesthesia Group, P.A.*, 190 S.W.3d 891 (Tex. App.—Dallas 2006, no pet.) (denial of plaintiff anesthesiology professional association's application for temporary injunction was not an abuse of discretion, where there was conflicting evidence as to whether defendants had breached their fiduciary duties, misappropriated confidential information, or tortiously interfered with business relationships; in light of such conflicting evidence, plaintiff failed to prove a probable right to the relief sought).
- *TMC Worldwide, L.P. v. Gray*, 178 S.W.3d 29 (Tex. App.—Houston [1st Dist.] 2005, no pet.) (district court properly denied application for temporary injunction because the evidence was sufficient to support finding that former employer did not show a probability of success in proving that its customer list was entitled to trade secret protection so as to grant temporary injunction in trade secret action against former employee; there

was no evidence that former employee used the list to obtain 16 customers which were on that list, but rather former employee testified that the 16 customers were obtained through other sources or they sought to continue business with former employee due to his prior relationship with them).

- *Sands v. Estate of Buys*, 160 S.W.3d 684 (Tex. App.–Fort Worth 2005, no pet.) (district court properly denied application for temporary injunction because estate of deceased owner of accounting corporation did not establish a probability of success in proving that clients’ identities deserved trade secret protection, so as to entitle estate to temporary injunction to prohibit former accountant from contacting clients; clients’ identities were known by many people outside the corporation, including other former accountants and the clients themselves, corporation made little effort to guard identities or compile a client list, and information regarding the identities could be acquired by others fairly easily).
- *EMSL Analytical, Inc. v. Younker*, 154 S.W.3d 693 (Tex. App.–Houston [14th Dist.] 2004, no pet.) (district court properly denied application for temporary injunction where there was no evidence former employee was currently violating nondisclosure clause or that there was any likelihood that she would in the future, so as to show a probable, imminent, and irreparable injury necessary to support a temporary injunction; even though she was working for former employer’s customer, evidence only established a theoretical possibility that former employee could take customer away from former employer or that she could divulge confidential information).

C. Permanent Injunctions In Trade Secrets Cases

As noted herein, the appropriateness of granting injunctive relief against those who have misappropriated trade secrets has long been recognized. *See Hyde Corp. v. Huffines*, 158 Tex. 566, 314 S.W.2d 763 (1958); *Elcor Chem. Corp. v. Agri-Sul, Inc.*,

494 S.W.2d 204 (Tex. Civ. App.—Dallas 1973, writ ref'd n.r.e.). The scope of the injunctive relief “must, of necessity, be full and complete so that those who have acted wrongfully and have breached their fiduciary relationship, as well as those who willfully and knowingly aided them in doing so, will be effectively denied the benefits and profits flowing from the wrongdoing.” *Elcor*, 494 S.W.2d at 212. The purpose of an injunction is to remove the advantage created by the misappropriation. *See Bryan v. Kershaw*, 366 F.2d 497, 502 (5th Cir. 1966). Although an injunction should ordinarily operate as a corrective rather than a punitive measure, if a choice must be made between the possible punitive operation of an injunction and the failure to provide adequate protection of a recognized legal right, courts must follow the course that provides adequate protection because “the undoubted tendency of the law has been to recognize and enforce higher standards of commercial morality in the business world.” *Hyde*, 314 S.W.2d at 773.

Historically, the “usual equitable order” in a trade secret misappropriation case is a perpetual injunction against the wrongdoer. *See id.* at 780–81. There has, however, been a recognition that a defendant may, in some cases, provide sufficient proof to show that an injunction of lesser duration than a perpetual injunction is adequate. *See Research Equip. Co. Inc. v. C.H. Galloway & Scientific Cages, Inc.*, 485 S.W.2d 953, 956 (Tex. Civ. App.—Waco 1972, no writ). For example, where a defendant shows at trial that the trade secrets at issue could be reverse engineered by someone with no background in the business or the confidential information was publically disclosed after the misappropriation, a trial court has discretion to grant a limited time injunction. *Id.* (ninety-day injunction upheld where design and construction of product was “based on familiar mechanical means and principles that are quite obvious to and easy to imitate by any reasonably experienced craftsman that might see one.”). But the overriding concern remains the protection of the plaintiff’s recognized legal rights. *See Hyde*, 314 S.W.2d at 773. The burden is on the defendant to show that an injunction for a period of time less than perpetual would be sufficient to achieve that end. *Id.* at 776.

In the case of *Halliburton Energy Services, Inc. v. Axis Technologies, LLC*, 444 S.W.3d 251, 258-61 (Tex. App.–Dallas 2014, n.p.h), the appellate court affirmed the trial court’s decision to grant the plaintiff perpetual injunctive relief. In addition, the appellate court found that, “because the evidence showed Halliburton had a contractual right to exclusive ownership of the property, the trial court abused its discretion in failing to order appellees to destroy all electronic copies of the materials in their possession.” *Id.* at 263.

D. Whether Information Is Truly A “Trade Secret”

In *Texas Integrated Conveyor Systems, Inc. v. Innovative Conveyor*, 300 S.W.3d 348 (Tex. App.–Dallas 2009, pet. denied), the Court of Appeals held that genuine issues of material fact existed on whether former employer’s customer information constituted a “trade secret,” thus precluding traditional summary judgment to the former employees-defendants on the former employer’s claim against them for misappropriation and theft of trade secrets.

As note above, in *GlobeRanger Corp. v. Software AG United States of Am., Inc.*, 836 F.3d 477 (5th Cir. 2016), the developer of a passive radio frequency identification (RFID) system for commercial use brought action against competitor in state court, alleging trade secret misappropriation. The developer recovered \$15 million at trial. The Fifth Circuit affirmed. The court found that GlobeRanger produced sufficient evidence for a jury to reasonably conclude that at least some portion of its system constituted a trade secret. There was testimony explaining how GlobeRanger’s “filtering” technology was unique and its ability to filter large amounts of information in real time added value compared to traditional inventory management systems. In addition, both the value and the difficulty in reproducing the technology were also shown through emails and testimony from Software AG employees.