

## **Texas Supreme Court Makes Enforcement of Noncompete Agreements Easier for Employers**

**June 28, 2011**

On June 24, the Texas Supreme Court issued a long-awaited decision clarifying the standards for enforcement of noncompete agreements under the Texas Business and Commerce Code. In *Marsh USA Inc. and Marsh & McLennan Cos. v. Rex Cook*, the court considered whether an employee's receipt of stock options could sustain an agreement that prohibited the employee from soliciting or accepting business from certain customers of Marsh McLennan (Marsh).

Noncompete agreements, which include prohibitions on working for a competitor and limitations on an employee's ability to solicit customers, are governed in Texas by the Texas Business and Commerce Code. Under that statute, such agreements may be enforced only if they contain reasonable limitations with respect to geography, time, and scope of activity to be prohibited and only if they are "ancillary to or part of an otherwise enforceable agreement." Texas courts, as well as practitioners and employers, have struggled with this latter requirement. The *Cook* case represents a significant change in Texas law and a departure from the Texas Supreme Court's previous analysis of noncompete agreements.

Under previous court decisions, the analytical focus was on the type of consideration provided by the employer in exchange for the employee's promise to refrain from competing. Specifically, a Texas employer seeking to enforce a noncompete agreement must have been able to show that the consideration it provided to the employee "gave rise to an interest" in restraining competition. For example, an employer's promise of trade secrets or confidential information was deemed sufficient consideration to support a noncompete agreement whereas simple cash consideration was not.

In *Cook*, the Texas Supreme Court considered whether an employer's grant of stock options satisfied the "ancillary" prong of the Texas Business and Commerce Code. Cook joined Marsh in 1983 and signed an agreement under which he could exercise certain stock options in exchange for signing an agreement limiting his ability to solicit or accept business from clients of Marsh with whom he had business dealings during his employment. Cook thus signed the noncompete agreement not when he was provided the original grant of stock options, but rather when he chose to exercise the options.

After his separation from employment with Marsh, Cook went to work for a competitor. He thereafter was sued by Marsh for breach of his contract and for breach of fiduciary duty. Cook filed a motion for summary judgment in the district court on the grounds that the agreement was unenforceable under the Texas Business and Commerce Code. The trial court granted Cook's motion and an appellate court affirmed that ruling.

The Texas Supreme Court, in a 6-3 opinion, disagreed with the lower courts and reversed the grant of summary judgment. Significantly, the court overruled previous authority that focused on the type of consideration provided by the employer and the assessment of whether or not that consideration “gives rise” to an interest in restraining competition. Rather, the court construed the Texas Business and Commerce Code as requiring simply that there be a nexus between the noncompete agreement and the employer’s interests, holding that the noncompete agreement “must be reasonably related to the [employer’s] interest worthy of protection.” The court emphasized Cook’s high-level executive position with the company and found that, by providing an ownership interest in the company, the stock options provided to Cook were “reasonably related to the company’s interest in protecting its goodwill, a business interest the [Texas Business and Commerce Code] recognizes as worthy of protection.” The noncompete was thus enforceable on that basis.

As a practical matter, *Cook* should make enforcement of noncompete agreements easier in Texas. The decision represents a shift from the previous, more technical focus on the type of consideration provided in the noncompete agreement to a more generalized assessment of the employer’s interests in restraining competition. *Cook* follows a trend of other recent Texas Supreme Court cases that have found that the enforcement of noncompete agreements should be decided in the context of the overall purpose of the Texas Business and Commerce Code, which is to provide for reasonable restrictions that protect legitimate business interests.

If you have any questions or would like more information on the issues discussed in this LawFlash, please contact any of the following Morgan Lewis attorneys:

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