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The Uncertain Status of Post-Employment Non-Compete Covenants in Texas

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THE UNCERTAIN STATUS OF POST-EMPLOYMENT NON-COMPETE COVENANTS IN TEXAS*

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INTRODUCTION

A post-employment non-compete covenant is an agreement by an employee that, after termination of employment he or she will not compete with his or her former employer—usually within a specified geographic area and for a specified period of time. Such covenants are standard parts of many employment contracts.[1]

Under the long standing common law of contracts, non-compete covenants are generally suspect as restraints of trade.[2] Post-employment non-compete covenants also bear a strong presumption of unfairness because of the superior bargaining power almost invariably wielded by the employer.[3] Nevertheless most jurisdictions, including Texas, have traditionally enforced post-employment non-compete covenants within the constraints of the reasonableness test described below.

Recently, however, courts in several jurisdictions have begun to view non-compete covenants with increasing disfavor.[4] Indeed, the opinions in two recent cases decided by the Supreme Court of Texas cast serious doubt upon the continuing viability of such covenants in Texas.[5] Unfortunately, both opinions are flawed in their reasoning and confused in their application of the law. Therefore, their predictive value is unclear.

The purpose of this article is to (1) identify the policy issues and conflicting interests; (2) describe the common law rules generally applied in most U.S. jurisdictions and examples of some statutory efforts to resolve the dilemma; (3) describe and critique the relevant Texas law as it existed prior to the two most recent cases; and (4) discuss these cases against the above-described background.

II. BACKGROUND: THE DILEMMA; THE "SOLUTIONS"

A. *Policy Issues*

The basic dilemma is the confrontation between two interests so

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at Texas Southern University in Houston and a Visiting Professor at Loyola Law School in Los Angeles.

1. Closius and Schaffer, *Involuntary Nonservitude: The Current Judicial Enforcement of Employee Covenants Not to Compete*, 57 So. CAL. REV. 531, 532 (1984).

2. Restatement (Second) of Contracts, Sec. 186 (1979).

3. *Id.* at Sec. 188 comment g.

4. *See*, "Courts Skeptical of 'Non-Compete' Pacts", *Wall Street Journal*, Jan. 11, 1989, page B1.

5. *Martin v. Credit Protecting Association*, 31 TEXAS SUPREME COURT J. 626 (No. C-7339, June 13, 1988) *DeSantis v. Wackenhut*, 31 TEXAS SUPREME COURT J. 616 (No. C-6617, June 13, 1988).

widely acknowledged that they are often regarded as "rights": (1) an employee's interest in having the freedom to accept employment in his or her chosen field; and (2) an employer's interest in protecting its business by agreeing with an employee that the latter will not compete with the employer for a stated time, within a specified geographic area, after employment ceases.[6] Ironically, each of these interests might generally be thought protected by "freedom of contract."

1. *Individual Rights*

"Freedom of contract", while clearly a relevant notion, is perfectly ambiguous in this context. The slogan alone will not resolve the dilemma presented by the contradiction between *sanctity* of contract (*pacta sunt servanda*) and freedom *to* contract (*e.g.*, for the sale of one's personal services). Indeed, freedom of contract is almost certainly a misnomer if what is meant is that parties should be free to agree to whatever terms they like and the state, through its judicial apparatus, should enforce those agreements. In reality freedom of contract is neither so simple nor so absolute.

Judicial refusal to enforce contracts involving fraud, duress or incapacity, for example, is at once an exception to and a prerequisite of freedom of contract.[7] It is a prerequisite because freedom of contract is generally thought meaningful only when parties with contractual capacity act voluntarily.[8] Even when these conditions are met, however, the parties are not entirely free to do as they please, for the doctrines of undue influence and unconscionability give courts broad lattitude to adjust or avoid otherwise valid agreements.[9]

The doctrine of unconscionability is most often invoked in situations said to involve unequal bargaining power.[10] The real issue, however, may be protection of the employee/covenantor from his or her own willingness to enter an ill-advised and detrimental "bargain".[11]

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6. Kniffin, *Employee Non-competition Covenants: The Perils of Performing Unique Services*, 10 RUT. CAM. L.J. 25 (1978).

7. Professor Duncan Kennedy describes this as "the constitutive character of the exceptions to enforcement." Kennedy, *Distributive and Paternalist Motives in Contract and Tort Law, With Special Reference to Compulsory Terms and Unequal Bargaining Power*, 41 MD. L. REV. 563, 569-70 (1982).

8. *Id.*

9. *Id.*

10. *Id.* at 614; see also, Uniform Commercial Code Sec. 2-302 comment. "The principle is one of the prevention of oppression . . ." *Id.*

11. Kennedy, *supra* note 7, at 634. "Courts using the doctrine of unconscionability like to put their decisions on grounds of unequal bargaining power . . . [b]ut its often obvious that they are concerned not with power but with naivete." *Id.*

The question is whether the prospective freedom to sell one's services is an interest whose alienation the law should regulate or even forbid.[12] The idea that freedom to apply one's (legal) trade is an interest "owned" by each individual is neither radical nor new.[13] To conclude that this interest should be inalienable, however, requires a second, more difficult step. The unenforceability of a contract by which one agrees to be murdered is scarcely controversial, but the analogy to an agreement not to do a particular kind of work in a particular area during a particular period of time seems altogether theoretical and attenuated.[14] There would be little basis for objection if, during the period of the restraint, the covenantor was paid not to work, but this differs from the typical situation only because in the typical situation the covenantor is, arguably, paid in advance not to work during the period of the restraint.

2. *Economic Issues*

The policy arguments against post-employment non-compete covenants would seem especially persuasive when an employer has terminated an employee, or when an employer is using a post-employment restriction to pressure an employee not to quit. With respect to the latter situation, one court has observed that:

> A covenant that serves primarily to bar an employee from working for others or for himself in the same competitive field so as to discourage him from terminating his employment is a form of industrial peonage without redeeming virtue in the American economic order.[15]

The court's reference to the "economic order" shifts the focus

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12. *See generally*, Calebresi and Melamed, *Property Rules, Liability Rules, and Inalienability*," 85 HARV. L. REV. 1089 (1972). There are three types of "entitlements": those protected by property rules, those protected by liability rules, and those that are inalienable. "An entitlement is inalienable to the extent that its transfer is not permitted between a willing buyer and a willing seller." *Id.* at 1092-93.

13. J. Locke, *Second Treatise of Government* (New York 1952) (6th Ed. London 1764) "every man has a *Property* in his own *Person* . . . the *Labour* of his Body and the Work of his hands . . . are properly his." *Id.* at ch. V, sec. 27. J. Bentham, *Theory of Legislation* (R. Hildreth trans. 1840) (1st ed. 1802). "The idea of property consists in an established expectation." *Id.*; *Lynch v. Household Finance Corp.* 405 U.S. 538 (1972). "[T]he dichotomy between personal liberties and property rights in a false one . . . In fact, a fundamental interdependence exists between the personal right to liberty and the personal right to property. Neither could have meaning without the other." *Id.* at 552. *See generally*, Radin, *Property and Personhood* 34 STANFORD L. REV. 957 (1982).

14. *See generally*, Calabresi and Melamed, *supra* note 12, at notes 45-51 and associated text.

15. *Josten's Inc. v. Cuquet*, 383 F. Supp. 295, 299 (E.D. Md. 1974).

away from fairness to the individual, and toward a distinct policy issue. This second issue is social utility and/or efficiency and the question is whether society is better off with or without the enforcement of restrictive covenants in a given industry or business context. It can be argued, in general, that the public interest is best served by enforcing at least some post-employment non-compete covenants because they protect and, therefore, encourage, employer investment and such investment results in better products and services.[16]

The social utility argument *against* enforcement is also largely economic. The court in *Reed Roberts Assocs. v. Shauman*[17] described the economic system's need for "the uninhibited flow of services, talent and ideas"[18] and went on to state that "no restrictions should fetter an employee's right to apply to his own best advantage the skills and knowledge acquired by . . . his previous employment."[19]

The potentially significant collective economic impact of post-employment non-compete restraints has led some authors to advocate application of the rules and principles of antitrust law.[20] The Sherman Act proscribes "every contract in restraint of trade or commerce among the several states."[21] But this seemingly absolute prohibition has long been tempered by the "rule of reason."[22] As a result, every post-employment restraint tested under the rule has survived.[23]

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16. *See generally* R. Posner, *Economic Analysis of Law*, Sec. 3.1, at 30 (2d ed. 1977); Rubin & Shedd, Human Capital and Covenants Not to Compete, 10 J. LEGAL STUD. 93, 96-97 (1981).

17. 353 N.E.2d 590 (1976).

18. *Id.* at 593.

19. *Id.*

20. *See, e.g.*, Goldschmid, *Antitrust's Neglected Step-child: A Proposal for Dealing with Restrictive Covenants Under Federal Law*, 73 COLUM. L. REV. 1193, 1204 (1973); Sullivan, *Revisiting the "Neglected Stepchild": Antitrust Treatment of Post-Employment Restraints of Trade*, 1977 U. ILL. L.F. 621.

21. 15 U.S.C. Sec. 1 (1976). The commerce clause of the U.S. Constitution has long been construed as giving Congress significant power over not only interstate activities, but intrastate labor-management relations. *See e.g., U.S. v. Darby*, 312 U.S. 100, 117-24 (1941); *N.L.R.B. v. Jones & Laughlin Steel Corp.*, 301 U.S. 1, 29-32 (1937). Also, although Sec. 6 of the Clayton Act stipulates that human labor is not a commodity or article of commence, this definition was developed to create room (within the antitrust arena) for labor unions to operate legally. *Nichols v. Spencer Int'l. Press, Inc.* 371 F.2d 332, 335 (7th Cir. 1967).

22. See *Standard Oil Co. v. U.S.* 221 U.S. 1, 57-60 (1910), (acknowledging that every contract restrains trade and, therefore, the prohibition cannot be absolute).

23. *See e.g., Bradford v. New York Times Co.*, 501 F.2d 51, 59 (2d Cir. 1974); *Frackowiak v. Framer Ins. Co.* 411 F. Supp. 1309, 1318-19 (D. Kan. 1976); *Alders v. A.F.A. Corp. of Fla.* 353 F. Supp. 654, 656 (S.D. Fla. 1973); *Miller v. Kimberly-Clark Corp.* 339 F. Supp. 1296, 1297 (E.D. Wis. 1971).

At least one author has argued that the survival of the restrictions under antitrust analysis results from the courts' failure to consider labor market impact, as opposed to product market impact. Product market analysis is the traditional approach, but labor market analysis has been employed in some sports cases. Note, *The Antitrust Implications of Employee Non-compete*

In *Newburger, Loeb & Co. v. Gross*,[24] for example, the Court of Appeals for the Second Circuit observed that:

> employment agreements not to compete are proper subjects for scrutiny under section 1 of the Sherman Act. When a company interferes with free competition for one of its former employee's services, the market's ability to achieve the most economically efficient allocation of labor is impaired . . . Restraints on post-employment competition that serve no legitimate purpose at the time they are adopted would be *per se* invalid . . . Even if the clause is not overbroad *per se*, it might still be scrutinized for unreasonableness: Are the restrictions so burdensome that their anti-competitive purposes and effect outweighed their justifications? Restraints that fail this balancing test might be struck down under a rule of reason.[25]

However, in concluding that the restriction at issue was reasonable and, therefore, enforceable, the court cited the covenantee's "legitimate interest" in preventing the covenantor from competing for customers of the covenantee.[26]

B. *The Common Law Approach*

Post-employment restrictive covenants, having their origins in an era when apprenticeships approximated indentured servitude, were initially subject to extreme judicial disfavor.[27] A strong belief that such

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Agreements: A Labor Market Analysis, 66 MINN. L. REV. 519 (1982), citing: *Radovich v. N.F.L.* 352 U.S. 445, 453-4 (1957); *Mackey v. N.F.L.* 543 F.2d 606, 616-18 (8th Cir. 1975) cert. dismissed 434 U.S. 801 (1977).

24. 563 F.2d 1057 (2d Cir. 1977).

25. *Id.* at 1082.

26. *Id. Newburger*, involving a securities brokerage firm, demonstrates the circularity of embarking upon an antitrust analysis and ultimately testing the covenant against a standard not appreciably different from the one that would have applied in the absence of the antitrust rhetoric. See *infra*, notes 31-34 and associated text. Arguing that the economic issues remain relevant, however, Professor Sullivan has suggested that "the courts should take into account market impact in a more explicit and serious manner than they have so far." Sullivan, *supra* note 20 at 647. He advocates consideration of five factors in evaluating post-employment non-compete covenants: (1) the totality of the anti-competitive restraints imposed by the employer involved; (2) extent to which there is a pattern of such restraints in the relevant industry; (3) the state of competition in the industry, and, more specifically, in the relevant geographic market; (4) the scope of the restraint's prohibition and the remedy provided for violations; and (5) the nature of the employee restrained, with special disfavor for restraints on employees who are particularly valuable to competitors. Finally, Professor Sullivan suggests that courts subject proffered employer justifications to a higher degree of scrutiny. *Id.* at 647-49.

27. The earliest recorded case concerning a post employment restrictive convenant was decided in 1414. The case involved an agreement by a dyer to refrain from practicing his trade for a

covenants constituted restraints of trade and were inherently repugnant to public policy dominated the first two centuries of English case law on the topic.[28] In the 16th century, however, courts gradually diminished the prohibition against such restraints, allowing enforcement if the covenant was reasonable with respect to duration, geographic area, and benefit to the covenantee, and there was no violation of public policy.[29]

The general common law rule today is that a post-employment non-compete covenant is enforceable if it is supported by consideration and reasonable as to geographic scope, duration, and range of activities prohibited.[30] "Reasonableness" is determined against the backdrop of an ostensibly independent determination regarding the legitimacy of the business interests for which the former employer seeks protection.[31]

Many courts apply stricter standards to test the enforceability of non-compete covenants associated with employment contracts as distinguished from those for sales of businesses or dissolutions of partnerships.[32] In a further effort to discourage employer attempts to obtain unjustifiably broad protection, some courts refuse to enforce non-compete covenants that appear to have been drafted or included in bad faith.[33]

1. *Consideration for Employee's Covenant*

If a non-compete covenant is executed simultaneously with and as part of an employment contract, the employment itself constitutes

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period of six months after the termination of his employment by the covenantee. The court judge refused to issue the injunction sought by the covenantee and was so incensed he declared that, if the plaintiff had been present in court, he would imprison him until the plaintiff paid a fine to the king. *The Dyer's Case*, Y.B. Mich. 2 Hen. 5 f, pl. 26 (C.P. 1414).

28. Patterson, *The Law of Contracts in Restraint of Trade* at 34 (1891).

29. *Id.*

30. Restatement (Second) of Contracts (1979) provides, at Sec. 188(1), that a non-compete covenant is unreasonable if

> (a) the restraint is greater than is needed to protect the promisee's legitimate interest, or (b) the promisee's need is outweighed by the hardship to the promisor and the likely injury to the public.

See e.g., Weatherford Oil Tool Co. v. Campbell, 340 S.W.2d 950, 951 (Tex. 1960); *Hill v. Mobile Auto Trim, Inc.*, 725 S.W.2d 168 (Tex. 1987).

31. *Id., See also*, Restatement (Second) of Contracts, *supra*, Section 188, comment d.

32. *See e.g., American Hot Rod Assoc. v. Carrier* 500 F.2d 1269 (4th Cir. 1974), *Accord, C.G. Caster Co. v. Regan* 357 N.E.2d 162 (Ill. 1976). The differentiated standard dates back at least to *Mitchell v. Reynolds*, 1 P.W.ms. 181, 24 Eng. Rep. 347 (Q.B. 1711).

33. E. Farnsworth, *Contracts*, Sec. 5.8, at 363.

consideration for the covenant.[34] In most jurisdictions mere continuation of employment does not constitute consideration for a covenant entered into *after* inception of employment.[35] In these jurisdictions there must be new consideration through the provision of additional benefits (*e.g.*, a promotion, a salary increase, or an annuity) to the employee.[36]

Texas has been among the minority of jurisdictions following the alternate view that continued employment is sufficient consideration for the enforcement of a post-employment non-compete covenant. In *McAnnally v. Person*[37] a Texas court ruled that although the employee had worked three months before execution of the covenant, the covenant was supported by consideration.[38] More recently, in *Martin v. Credit Protection Association*,[39] the Supreme Court of Texas did not dispute the finding of the trial court and the court of appeals that continued employment constituted consideration for Martin's covenant.[40]

2. *Reasonableness*

It is generally held that in order to be enforceable, a non-compete covenant should be limited to a reasonable period of time.[41] Some courts have further specified that the duration must be limited to the period during which the covenantee remains in business.[42]

A host of subsidiary issues attend the basic requirement of geographic reasonableness. For example, Texas courts, among others, have held that where an express territorial restriction is unreasonably broad in scope, it can be modified by limiting the restriction to the area in which the former employee performed duties for his or her former employer.[43] A prohibition without express geographic boundaries can be similarly limited to the territory where the former employee

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34. Annotation, *Sufficiency of Consideration For Employee's Covenant Not To Compete, Entered into after Inception of Employment*, 51 A.L.R.3d 825, 828 (1973).

35. *Id.* at 830.

36. *Id.*

37. 57 S.W.2d 945 (Tex. Civ. App. 1933).

38. *Id.* at 948.

39. *Supra* note 5.

40. *Id.* at 626.

41. *See e.g., Bob Pagan Ford, Inc. v. Smith*, 638 S.W.2d 176 (Tex. Ct. App. 1982); *Schmidt v. Central*, 13 N.Y.S.2d 817 (1939); *Justin Belt Co. v. Yost*, 502 S.W.2d 681 (Tex. 1973).

42. *See e.g., Campbell v. Bd. of Trustees of Leland Stanford Junior University*, 817 F.2d 499 (9th Cir. 1987).

43. *See Eubank v. Puritan Chemical Co.*, 353 S.W.2d 90 *error ref. nre* (Tex. Civ. App. 1962); *Plating, Inc. v. Hutchinson*, 201 N.E.2d 239 (Ill. 1965); *All Stainless, Inc. v. Colby*, 308 N.E.2d 481 (Mass); *Martin v. Kiddle Sales and Services* 496 S.W.2d 714 (Tex. Civ. App. 1973).

carried out his or her duties for her employer,[44] or to the former employer's business area,[45] or to the former employer's customers.[46]

The third element of the reasonableness test requires an examination of the range of activities the covenant purports to ban.[47] In light of the strong public policy opposing restraints of trade, the basic rule is that a narrower ban is more likely to be held enforceable than a broader one.[48] A covenant purporting to ban a former employee's pursuit of an entire occupation, even within a limited geographical area, is most objectionable.[49]

3. *Employer's Business Interest*

The generally prevailing reasonableness test also provides that post-employment restrictive covenants are enforceable only if and to the extent that they seek to protect a legitimate business interest of the former employer.[50] Traditionally, such interests comprised only proprietary information, notably, trade secrets and customer lists.[51] This requirement is sometimes ignored, however, by courts that seem to enforce restrictive covenants on the most rudimentary of contract law principles, *i.e.*, that the covenant is part of a bargained-for-exchange.[52]

Alternatively, courts have relied increasingly upon "uniqueness of employee services" as a legitimate and, therefore, protectable interest of the employer.[53] *Purchasing Assocs. Inc. v. Weitz*[54] illustrates the

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44. *See Wrentham Co. v. Cann*, 189 N.E.2d 559 (Mass. 1963); *McAnally v. Person*, 57 S.W.2d 945 *error ref.* (Tex. Civ. App. 1973).

45. *See Brannen v. Bouley*, 172 N.E. 104 (1930); *New England Tree Expert Co. v. Russell*, 28 N.E.2d 997 (Mass. 1940); *Grace v. Orkin Exterminating Co.*, 255 S.W.2d 279 (Tex. 1953), *error ref. nre*; and *Thames v. Rotary Engineering Co.*, 315 S.W.2d 589 (Tex. Civ. App. 1958).

46. *See Edgecomb v. Edmunston*, 153 N.E. 99 (Mass. 1926); *Martin v. Kiddle Sales and Service*, 296 S.W.2d 714 (Tex. Civ. App. 1973); *and Career Placement of White Plains, Inc. v. Vaus*, 77 Misc. 2d 788, 354 N.Y.S.2d 764 (1974).

47. *See Whiting Milk Co. v. O'Connell*, 179 N.E. 169 (Mass. 1931).

48. *See e.g., Barnes Group, Inc. v. Harper*, 653 F.2d 175, 180 (5th Cir. 1981); *Pemco Corp. v. Rose*, 257 S.E.2d 885, 891 (W. Va. 1979); *Karpinski v. Ingrasci*, 268 N.E.2d 751, 754 (1971).

49. *See generally*, Closius and Schaffer, *supra* note 1.

50. *See* Blake, *Employee Agreements Not To Compete*, 73 HARV. L. REV. 625, 653 (1960).

51. *See Id.*; 6A Corbin, *Corbin on Contracts* Sec. 1394, at 100 n.83 (1962); *Meeker v. Stuart*, 188 F. Supp. 272, 275 (D.D.C. 1960). Some authors have gone further and argued that "*only* trade secrets or confidential information constitute a protectable interest sufficient to justify any form of post associational restraint". Closius and Schaffer, *supra*, note 1 at 551.

52. *See e.g., Foster & Co. v. Snodgrass*, 330 So. 2d 521, 522 (Fla. Dist. Ct. App. 1976); *Continental Group, Inc. v. Kinsley*, 422 F. SUpp. 838, 844 (D. Conn. 1976).

53. Kniffin, *supra* note 6 at 26; Tannenbaum, *Enforcement of Personal Services Contract in the Entertainment Industry* at 21.

54. 196 N.E.2d 245 (N.Y. 1963).

emergence of the "uniqueness of employee services" standard as an independent basis for enforcement of a post-employment restrictive covenant, rather than merely an additional factor to be considered while seeking to protect trade secrets and customer lists.[55] The *Purchasing Assocs.* court enunciated a standard, explaining that it is not enough to show that the individual excels at his work or that his or her services are of great value to the employer.[56] "[T]here must be a finding that his services are of such character as to make [the employee's] replacement impossible or that the loss of [the employee's] services would cause the employer irreparable injury."[57]

Other jurisdictions, including Texas, generally claim to follow this standard.[58] Unfortunately, the standard has at least two problems. First, it is not clear, in practice, whether the employee's services must be truly unique or just very important.[59] Secondly, and more importantly, even if the services are unique, "there is no significant correlation between uniqueness of the employee's services and the reasonableness of restraining him from accepting employment with another employer."[60] The former employee's skills and abilities, even if developed and/or enhanced while working for the former employer, belong to the employee and should not, therefore, constitute a legitimate basis for the restraint.[61] Moreover, even if the employee's departure causes irreparable harm to the former employer, enforcement of the negative covenant will not make the covenantee whole, but only punish the covenantor. Punishment is not generally considered a proper ob-

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55. Id. at 248.

56. Id.

57. Id. at 250.

58. Annotation, *Enforceability of Covenant Not To Compete Involving Radio or Television Personality*, 36 A.L.R.3d 1139 (1985).

59. The ambiguity of the standard is illustrated by the opinion in *Bradford v. New York Times Co.*, a suit contesting the enforceability of a post-employment restrictive covenant stipulating the forfeiture of retirement benefits as liquidated damages. Bradford had worked for the *Times* for 16 years, during which time he had served in capacities including General Manager, Vice President, and Director. After leaving the *Times*, Bradford violated the covenant by going to work for a competitor. The *Times* terminated his retirement benefits amounting to approximately one half million dollars. Bradford sued. The United States Court of Appeals upheld the restrictive covenant on the basis of Bradford's "uniqueness", which it found to be inherent in his "broad and vital corporate responsibilities" and his having been the "number two man" at the *Times*. The court's position has intuitive appeal, but probably only because we assume he "number two man" must have had virtually unfettered access to proprietary information (*e.g.*, trade secrets and customer lists). If the court is protecting proprietary information, it does not need the uniqueness standard. If it is protecting something else, that should be made clear. 501 F.2d 51 (2d Cir. 1974).

60. Kniffin, *supra* note 6, at 27.

61. C. Kaufman, *Corbin on Contracts* Sec. 1391B (Supp. 1982); *Hallmark Personnel of Texas v. Franks*, 562 S.W.2d 933, 936 (Tex. Civ. App. 1978); *Club Aluminum Co. v. Young*, 160 N.E. 804, 806 (Mass. 1928).

jective of contract law, even in the event of breach.[62] *A fortiori*, it is an improper objective when there has been no breach but only a termination of employment pursuant to the terms of the contract.

C. *Statutory Solutions*

Legislatures in several jurisdictions have statutorily addressed the enforceability of post-employment non-compete covenants.[63] The resulting legislation falls generally into two categories: prohibition and limitation. An example of each approach is discussed briefly below.

1. *Prohibition*

California courts have not adhered to the reasonableness test since 1872.[64] The California legislature enacted a statute which provides that "every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void."[65]

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62. E. Farnsworth, *supra* note 34, sec. 12.8 at 842.

63. ALA. CODE Sec. 8-1-1 (1984 Repl.); ALASKA STAT. Sec. 45.50.562, 45.50.574 (1986); ARIZ. REV. STAT. ANN. Sec. 44-1401 (1967 & Supp. 1986); ARK. STAT. Sec. 8-2-113(2) (1986 Repl.); CONN. GEN. STAT. ANN. Sec. 35-26 (1981 rev.); FLA. STAT. ANN. Sec. 542.33 (West Supp. 1987); GA. CODE ANN. Sec. 13-8-2 (1982); HAWAII REV. STAT. Sec. 480-4(c) (1976 Repl.); IDAHO CODE Sec. 48-101 (1977); IND. CODE ANN. Sec. 24-1-1-1 (Burns Supp. 1986); IOWA CODE ANN. Sec. 553-4 (West Supp. 1986); KAN. STAT. ANN. Sec. 50-112 (1983); LA. REV. STAT. Sec. 23:921 (West 1985); MASS. GEN. LAWS ANN. ch. 93, Sec. 4 (West 1984); MICH. COMP. LAWS ANN. Sec. 445-772 (West Supp. 1986); MINN. STAT. ANN. Sec. 325D.51 (West 1981); MISS. CODE ANN. Sec. 75-21-1 (1972)); MO. ANN. STAT. Sec. 416.031 (Vernon 1979); MONT. CODE ANN. Sec. 28-2-703 (1985); NEB. REV. STAT. Sec. 59-801 (Reissue 1984); N.J. REV. STAT. Sec. 56:9-3 (Supp. 1986); N.M. STAT. ANN. Sec. 57-1-1 (Supp. 1985); N.Y. GEN. BUS. LAW Sec. 340 (McKinney 1968 & Supp. 1987); N.C. GEN. STAT. Sec. 75-4 (Repl. 1985); N.D. CENT. CODE Sec. 9-08-06 (1975 Repl.); OHIO REV. CODE ANN. Sec. 1331.06 (Anderson 1979); OKLA. STAT. ANN. tit. 15 Sec. 217 (West 1966); S.C. CODE ANN. Sec. 39-3-10 (Law Co-op. 1976); S.D. CODIFIED LAWS ANN. Sec. 53-9-11 (Supp. 1986); TENN. CODE ANN. Sec. 47-25-101 (1984 Repl.); VA. CODE ANN. Sec. 591-9.5 (1982 Repl.); WASH. REV. CODE ANN. Sec. 19.86.030 (1978); W. VA. CODE Sec. 47-18-3 (1986 Repl.); WIS. STAT. ANN. Sec. 133.03 (West Supp. 1986).

64. *See Bosley Med. Group v. Abramson*, 207 CAL. RPTR. 477, 480 (1984).

65. CAL. BUS. & PROF. CODE Sec. 16600 (West 1987). Former California Civil Code Section 1673 was the predecessor to the present Section. It was adopted in 1872 following the introduction, by Senator Pendegrast of Napa County, of Senate Bill 430 entitled "An Act to Establish a Civil Code." The Measure passed the Senate on March 15, 1872, and the Assembly on March 16, 1872. A review of the 1871 annotations indicates that Sec. 1673 was taken verbatim from Sec. 833 of the 1865 draft of a Civil Code for the State of New York. The New York Civil Code was primarily a codification of prior common law. *See, The Journal of The Senate*, 19th Session: Legislature of the State of California (1871-72) at 575; *Revised Laws of the State of California*; in four codes, Political, Civil, Civil Procedure and Penal, at 329-30. Compare, The Civil Code of the State of New York by the Commissioners of the Code (1865) at 255-56.

The statute's applicability to personal services contracts is settled.[66]

If a post-employment non-compete covenant only prohibits the former employee from revealing trade secrets or confidential information such as customer lists, California courts will generally enforce the covenant.[67] However, if a post-employment covenant has territorial and/or durational restrictions, it is generally unenforceable.[68] The rationale behind the courts' rulings is that non-compete covenants are repugnant to California's public policy.[69]

Statutory exceptions exempt sales of businesses[70] and dissolutions of partnerships[71] from the general prohibition. Post-employment non-compete clauses in employment contracts, however, are not covered by these exceptions and hence, are void in California.[72] Trade secret, customer lists and other proprietary information are protected by other legal principles, including those of agency.[73]

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66. *Frame v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.* 97 CAL. RPTR. 811 (1971); *Buskuhl v. Family Life Ins. Co.* 76 CAL. RPTR. 602 (1969).

67. *See Loral Corp. v. Moyes*, 219 CAL. RPTR. 836, 174 Cal. App. 3d 268 (App. 6 Dist. 1985); *Rigging Intern. Maintenance Co. v. Gwin*, 180 CAL. RPTR. 451, 128 C.A.3d 594 (1982).

68. *See Loew's Inc. v. Cole*, 185 F.2d 641, cert. denied, 71 S. Ct. 570, 340 U.S. 954; see also *KGB, Inc. v. Giannoulas*, 164 CAL. RPTR. 571, 104 C.A.3d 844 (1980).

69. *See Fidelity Credit Assur. Co. of California v. Cosby*, 265 P. 372, 90 C.A. 22; *Frame, Inc. v. Merrill Lynch, Pierce, Fenner & Smith, Inc.* 97 CAL. RPTR. 811, 20 C.A.3d 668 (1971).

70. The specific language of the statutory exception provides: "Any person who sells the good will of a business, or any shareholder of a corporation selling or otherwise disposing of all his shares in said corporation, or any shareholder of a corporation which sells (a) all or substantially all of its operating assets together with the goodwill of the corporation, (b) all or substantially all of the operating assets of a division or a subsidiary of the corporation together with the goodwill of such division or subsidiary, or (c) all of the share of any subsidiary, may agree with the buyer to refrain from carrying on a similar business within a specified county or counties, city or cities, or a part thereof, in which the business so sold, or that of said corporation, division, or subsidiary has been carried on, so long as the buyer, or any person deriving title to the goodwill or shares from him, carries on like business therein. For the purposes of this section, subsidiary shall mean any corporation, a majority of whose voting shares are owned by the selling corporation." CAL. BUS. & PROF. CODE Sec. 16601 (West 1987).

71. *Id.* The specific language provides: "Any partner may, upon or in anticipation of dissolution of the partnership, agree that he will not carry on a similar business within a specified county or counties, city or cities, or a part thereof, where the partnership business has been transacted, so long as any other member of the partnership, or any person deriving title to the business or its goodwill from any such other member of the partnership, carries on a like business therein." CAL. BUS. & PROF. CODE Sec. 16602 (West 1987).

72. *See Loral Corp. v. Moyes*, 219 CAL. RPTR. 836, 174 Cal. App. 3d 268 (App. 6 Dist. 1985); *Campbell v. Bd. of Trustees of Trustees of Leland Stanford Junior University*, 817 F.2d 499, 502 (9th Cir. 1987); But *see Rigging Intern. Maintenance Co. v. Gwin*, 180 CAL. RPTR. 451 (1982).

73. *See* Restatement (Second) of Agency, Sec. 396(a)-(d) (1957).

2. *Limitation*

A Louisiana statute declares void any non-compete agreement which the employer may "require or direct any employee to enter into."[74] However, such a restriction may be enforceable if it does not exceed two years, and "the employer incurs an expense in the training of the employee or incurs an expense in the advertisement of the business. . ."[75] Louisiana courts have made it clear that the expense must be substantial and the referenced advertisement must connect the employee-covenantor with the business.[76]

III. THE TEXAS TRADITION, *MARTIN* AND *DESANTIS*

Texas courts have generally followed the prevailing common law approach as outlined above, and held specifically that a non-compete covenant is (1) a restraint of trade and enforceable only if reasonable;[77] (2) unreasonable "if it is greater than is required for the protection of the person for whose benefit the restraint is imposed or imposes undue hardship upon the person restricted;"[78] (3) unenforceable unless reasonable as to duration, geographic scope and range of activities prohibited;[79] and (4) unenforceable if injurious to the public interest.[80] Reasonableness is a question of law for the court,[81] and a Texas court can modify a restriction to make it reasonable or, without formally modifying the covenant, enforce it only to a reasonable extent.[82] In addition, an employer/covenantee who seeks injunctive relief has the burden of proving reasonableness.[83]

Weatherford Oil Tool Co. v. Campbell[84] is the root of contemporary Texas case law regarding post-employment non-compete

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74. LA. REV. STAT. ANN. Sec. 23:291 (West 1985).

75. *Id.*

76. See, *Nalco Chemical Co. v. Hall*, 237 F. Supp. 678, 681 (E.D. La. 1965) aff'd 347 F.2d 90 (5th Cir. 1965).

77. *Weatherford Oil Tool Co. v. Campbell*, 340 S.W.2d 950, 951 (1960).

78. *Id.*; *Henshaw v. Kroenecke*, 656 S.W.2d 416, 418 (1983).

79. *Frankiewicz v. National Comp. Assocs.*, 633 S.W.2d 505, 507 (1982).

80. *Matlock v. Data Processing Sec., Inc.*, 618 S.W.2d at 329 (1981).

81. *Henshaw v. Kroenecke*, 656 S.W.2d at 418.

82. *See, e.g., Matlock v. Data Processing Sec. Inc.*, 618 S.W.2d at 329; *Justin Belt Co. v. Yost*, 502 S.W.2d at 685; *Spinks v. Riebold*, 310 S.W.2d 668, 69 (Tex. Civ. App.—El Paso 1958, writ ref'd).

83. *Custom Drapery Co. v. Hardwick*, 531 S.W.2d 160, 164 (Tex. Civ. App.—Houston [1st Dist.] 1975, no writ).

84. 340 S.W.2d 950 (1960).

covenants. *Weatherford* was a suit to enforce non-compete covenants against three former employees of a company involved in manufacturing and selling oil field equipment.[85] Upon commencement of employment, each of the defendant employees (two salesmen and an office worker) signed covenants not to compete with Weatherford for one year after termination of employment.[86] Soon after termination of employment, they violated these covenants by organizing a company that competed with Weatherford.[87] Weatherford sought and was denied an injunction and the court of appeals affirmed.[88]

Weatherford appealed and the Supreme Court of Texas, in affirming the court of appeals, adopted the reasonableness test generally described in Part II of this article.[89] Applying the test, the court found that the absence of any territorial limitation in the covenant meant enforcement would preclude covenantors from operating their new business anywhere in the world.[90] The court found this result unreasonable;[91] and while modification might be appropriate when equitable relief was sought, Weatherford's prayer for an injunction had become moot and "an action for damages . . . must stand or fall on the contract as written."[92] Thus, the court refused to award damages.[93]

The court reaffirmed and clarified *Weatherford* 21 years later in *Matlock v. Data Processing Security, Inc.*[94] *Matlock* involved efforts by Data Processing Services, Inc. ("DPS") to prevent competition by Matlock and two other former DPS employees who quit their jobs with DPS, established another company, and began to compete with DPS in violation of non-compete covenants signed by the employees. The covenantors sought a declaratory judgment that the covenants were

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85. *Id.* at 951.

86. *Id.* The covenant stated: "I hereby contract and agree that for a period of one year from the date of the termination of my employment, for any reason, I will neither enter into a business offering like merchandise to that offered by Weatherford Oil Tool Company, Inc., nor assist either directly or indirectly any competitor of Weatherford Oil Tool Company, Inc., or any other person, company or organization in offering like mechandise to that offered by Weatherford Oil Tool Company, Inc., in any area where Weatherford Oil Tool Company, Inc. may be operating or carrying on business during said one year period." *Id.*

87. *Id.*

88. 327 S.W.2d 76.

89. 340 S.W.2d 950, 951. Lacking Texas precedent, the court cited the Restatement of Contracts and A.L.R. Annotations.

90. *Id.* at 152.

91. *Id.*

92. *Id.* at 953.

93. *Id.*

94. 618 S.W.2d 327 (1981).

void.[95] DPS sought and was granted a temporary injunction pending trial on the merits, and Matlock appealed.[96]

The Supreme Court of Texas upheld that portion of the injunction that prohibited covenantors' use or disclosure of trade secrets or confidential business information of DPS,[97] but found the prohibitions regarding use of "know-how" and information pertaining to "prospective customers of DPS" too vague to be enforced.[98] The court also found the covenants' geographic scope (the whole of the United States) unreasonable because DPS had no protectable interest that reached throughout the U.S.[99] The court affirmed the temporary injunction as modified, after citing *Weatherford* and restating the general proposition that:

> A determination of the reasonableness of territorial restraints upon non-competition contracts requires a balance of the interests of the employer, the employee, and the public while being "mindful of the basic policies of individual liberty, freedom of contract, freedom of trade, protection of business, encouragement of competition and discouragement of monopoly."[100]

The current formulation of the Texas rule was set forth in a 1987 case styled *Hill v. Mobile Auto Trim, Inc.*[101] A brief analysis of the Hill case is necessary to a discussion of the Texas Supreme Court's recent opinions in *Martin* and *DeSantis*.

A. *Hill*

Hill involved a non-compete covenant included in a franchise agreement between Mobile Auto Trim, Inc. ("Mobile") as franchisor and Joel Hill as franchisee. The essence of the agreement was that Hill would pay approximately $42,000 and five percent of his gross revenue from a mobile automobile trim and repair business in exchange for the use of Mobile's name and good will and an equipped van provided

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95. *Id.* at 328.
96. *Id.*
97. *Id.* at 329.
98. *Id.*
99. *Id.* DPS had done business with less than two percent of the potential U.S. Market. *Id.* at 328.
100. *Id.* at 329, quoting, in part, from *Fidelity Union Life Co. v. Protective Life Ins. Co.* 356 F. Supp. 1199, 1203 (N.D. Tex. 1972).
101. 725 S.W.2d 168 (Tex. 1987).

by Mobile.[102] The lengthy and detailed non-compete covenant provided that after termination of the franchise agreement, Hill would not compete with Mobile, directly or indirectly, for a period of three years.[103] The prohibition covered seven counties, including the two within which Hill's franchise areas were located.[104] After approximately two and one half years, Mobile terminated the agreement because of Hill's delinquency in the payment of his franchise fees.[105] Hill violated the non-compete covenant by soliciting a Mobile customer almost immediately.[106] Mobile sought and was granted a temporary injunction.[107]

On appeal to the state Supreme Court, Hill argued that the non-compete agreement was a restraint of trade and unreasonable.[108] The court set forth a four part test for reasonableness, indicating that a non-compete covenant is unenforceable in Texas unless it is:

(1) necessary for the protection of the promisee;
(2) reasonable as to time, territory and activity and not oprressive to the promisor;
(3) not injurious to the community; and
(4) supported by consideration.[109]

The court announced its conclusion that the Hill covenant was

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102. *Id.* at 169.

103. *Id.* at 170. The provision read as follows:

> Franchisee (Hill) agrees that upon termination of this Franchise Agreement, for whatever reason, Franchisee shall not directly or indirectly, as an officer, director, shareholder, proprietor, partner, consultant, employee or in any other individual or representative capacity, engage, participate or become involved in any business that is in competition in any manner whatsoever with the business of the Company or its franchisees. Furthermore, it is understood between the parties that substantial goodwill will exist [sic] between the Company and the managers of the various car dealerships serviced by the Company and the Company's franchisees. Because said managers are transient and frequently change employment among car dealerships, Franchisee further agrees that upon termination of this Franchise Agreement, for whatever reason, Franchisee will not directly or indirectly in any manner whatsoever, contact said managers (irrespective of the car dealerships that employ them) regarding business in competition with the Company. This covenant shall extend for a period of three (3) years following the termination of this Franchise Agreement or any renewal hereof. Further, this covenant shall cover the following geographic area during said period: The following Texas Counties: Dallas, Tarrant, Ellis, Denton, Rockwall, Kaufman, and Collin.

104. *Id.* at 169.

105. *Id.* at 170.

106. *Id.*

107. 704 S.W.2d 384.

108. 725 S.W.2d at 169.

109. *Id.* at 170-71.

"plagued by a lack of reasonableness,"[110] then proceeded to identify three general problems with the restraint.[111]

1. *Consideration*

First, the court said, the covenant was not supported by consideration.[112] However, in attempting to support this conclusion with a discussion of training and trade secrets,[113] the court demonstrated its confusion regarding a simple point: the covenant was part of the franchise agreement and supported by the same consideration that made the agreement enforceable.[114]

The court distinguished post-employment non-compete covenants from non-compete covenants associated with sales of businesses, thereby implying recognition that restrictive covenants in different business contexts might be subject to different analyses.[115] Next, however, the court proceeded to analyze the Hill covenant as though it was part of a simple employment agreement rather than a franchisor-franchisee relationship.[116] This choice (or oversight) should have made the consideration issue an easy one, as the law across U.S. jurisdictions is uniform on this point: if a non-compete covenant is executed simultaneously with and as part of an employment contract, the employment itself constitutes consideration for the covenant.[117] Texas is in accord.[118] Moreover, Texas is among a minority of jurisdictions that take a more liberal view of the consideration requirement in the context of post-employment non-compete covenants.[119]

Thus, the majority opinion in Hill seems clearly to reflect a misunderstanding of the consideration requirement and how it is met.

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110. *Id.* at 170.

111. It would appear, although the court did not state, that any one of the problems cited would have been fatal to the covenant.

112. 725 S.W.2d at 171.

113. *Id.*

114. See *supra* note 35 and associated text.

115. 725 S.W.2d at 170.

116. See *infra* note 128 and associated text.

117. See *supra* note 35 and associated text.

118. *See, e.g., Garcia v. Laredo Collections, Inc.*, 601 S.W.2d 97, 98-99 (Tex. Civ. App.—San Antonio 1980, no writ).

119. When the execution of a covenant not to compete is contemporaneous with the acceptance of employment, the latter becomes the consideration for the covenant. A question has arisen, however, whether an agreement not to compete executed after employment has commenced is supported by consideration . . . Texas courts have held that continued employment is sufficient consideration for a covenant not to compete. *Id.*

2. *Employer's Interest*

Secondly, the court said Mobile had no legitimate business interest to protect.[120] In most jurisdictions, this requirement would be met readily by Mobile's customer lists and Hill's contacts on behalf of Mobile, *i.e.*, by Mobile's goodwill.[121]

In Texas, "goodwill" has been defined as "that value which inheres in fixed and favorable consideration of customers arising from established and well conducted business."[122] Traditionally, Texas courts have had no difficulty attaching value to business goodwill.[123] One Texas court held that a restrictive covenant was enforceable

> where the good will of the employer's customers had attached to the employee during the latter's employment and the employee thus had acquired during his employment a special influence which gave him an advantage over the employer in competition for the customer's business.[124]

Another concluded that

> most courts recognize that an employer has a sufficient interest in retaining his customers to support an employee's covenant whenever the employee's relationship with customers is such that there is a substantial risk that he may be able to divert all or part of their business.[125]

And just four years prior to *Hill*, Texas law still provided that a covenantee

> had a right to protect himself from the possibility that [covenantor] would establish a rapport with the clients of the business and upon termination take a segment of that clientele with him.[126]

In *Hill*, however, the Texas Supreme Court not only refused to

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120. 725 S.W.2d at 171.

121. See *supra* note 51 and associated text.

122. *Texas & Pacific Ry. Co. v. Mercer*, 58 S.W.2d 896, 900 (Tex. Civ. App.—Dallas 1933) rev'd on other grounds, 90 S.W.2d 557 (1936).

123. "Such value is based necessarily upon prospective profits to result from voluntarily continued patronage of the public." *Id.*

124. *Kidde Sales & Service, Inc. v. Pearson*, 493 S.W.2d 326, 329-30 (Tex. Civ. App.—Houston [1st Dist.] 1973, no writ).

125. *Hospital Consultants, Inc. v. Potyka*, 531 S.W.2d 657 (Tex. Civ. App.—San Antonio 1975).

126. *Henshaw v. Kroenecke*, 656 S.W.2d 416, 418 (Tex. 1983).

recognize Mobile's protectable interest in such goodwill but, amazingly, declared that the goodwill actually belonged to Hill.[127] It is noteworthy that the court did not limit this conclusion to situations involving franchise agreements, as opposed to employment. Indeed, the court appeared to use the terms "employee" and "franchisee" interchangeably and even melded them into one: "employee/franchisee".[128]

3. *The "Common Calling" Issue*

Third, and potentially most troublesome for the future, the court's majority adopted a new rule, concluding that no restrictive covenant should be enforced against anyone engaged in a "common calling."[129] The court did not define "common calling,"[130] but introduced the rule in discussing the question whether the covenant was "oppressive to the promissor."[131] The court concluded the enforcement of the covenant was oppressive to Hill, stating

> [n]ot only has he lost his franchise and investment therein, he is now prevented from using his previously acquired skills and talent to support him and his family in the county of their residence.[132]

If the *Hill* majority's "common calling" rule is a sub-issue in the "oppression" part of the four-pronged test of enforceability,[133] the *Hill* opinion signaled a significant policy shift away from recent Texas cases upholding restrictive covenants even when convenantors would clearly be required to seek work in a different field,[134] or in a different area of the same field.[135]

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127. 725 S.W.2d at 171.

128. *Id.* at 171-72.

129. *Id.* at 172.

130. Neither did the Utah case to which the Texas court attributed the rule: *Robbins v. Finlay*, 645 P.2d 623, 627 (1982), but a subsequent Texas case establishes that a hairdresser is engaged in a common calling—even if designated "shop manager". *Bergman v. Norris of Houston*, 734 S.W.2d 673, 674 (1987). Meanwhile, the Utah court seems to have backed away from the "common calling" issue and returned to a reasonableness standard. *See, e.g., System Concepts, Inc. v. Dixon*, 669 P.2d 421, 426 (Utah 1983). (Post-employment non-compete covenant enforceable against national sales manager of cable television equipment company where covenant was reasonable in time and area and necessary to protect covenantee's good will).

131. See *supra* note 109 and associated text.

132. 725 S.W.2d at 172.

133. See *supra* note 109 and associated text.

134. *Orkin Exterminating Co. v. Wilson*, 501 S.W.2d 408 (Tex. Civ. App.—Tyler 1973, writ dism'd w.o.j.).

135. *Electronic Data Systems v. Powell*, 524 S.W.2d 393 (Tex. Civ. App.—Dallas 1975, writ ref.'d n.r.e.).

Alternatively, the "common calling" test may be a part of the inquiry into the employer's protectable interest. *I.e.*, an employee engaged in a common calling, perhaps definitionally, does not provide unique services and, therefore, the employer/covenantee is necessarily deprived of the "unique services" rationale for enforcement of the covenant.[136] This seems to be the approach taken by the Supreme Court of Utah, from which the *Hill* court borrowed the common calling rule.[137] Within two years of adopting the common calling rule, the Utah court backed away from that formulation, reverting to the more common (arguably inverse) statement of the proposition:

> to justify enforcement of a restrictive covenant by injunctive relief the employer must show not only goodwill, but that the services rendered by the employee were special, unique or extra-ordinary.[138]

This approach would be consistent with prior Texas case law.[139]

Whatever the current position in Utah, it seems the *Hill* majority left an important gap in the protection available to an employer/covenantee. By flatly refusing to enforce post-employment non-compete covenants against employees engaged in common callings, the Texas court left employers with no protection against "common calling" convenantors who would misuse customer lists.[140] It is against this extremely problematic doctrinal background that *Martin* and *DeSantis* must be assessed.[142]

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136. See *supra* notes 53-62 and associated text.

137. See *supra* note 130.

138. *System Concepts Inc. v. Dixon*, 669 P.2d 421 (Utah 1983). For the quoted proposition, the Utah court cited *Robbins v. Finlay* 645 P.2d 623, 627-8 (Utah 1982) the case in which it established the common calling rule. The words "common calling", however, are conspicuously absent from the more recent opinion.

139. See *supra* note 58; *Matuszak v. Houston Oilers*, 515 S.W.2d 725 (Tex. Civ. App. Houston [14th Dist.] 1974, no writ).

140. The Utah court *upheld* the portion of the covenant that prohibited misuse of customer leads, even as it established the common calling rule. 646 P.2d at 627. This point seems to have escaped the *Hill* majority. Customer leads are not readily protectable by trade secrets law. *Crouch v. Swing Mach. Co.*, 468 S.W.2d 604 (Tex. Civ. App. San Antonio 1971, no writ).

141. 725 S.W.2d at 172.

142. Justice Gonzalez's dissent comprises a thorough critique of the majority opinion in *Hill*. *Id.* See also, White, " 'Common Callings' and the Enforcement of Post-employment Covenants in Texas" 19 ST. MARY'S L.J. 3, 589-619 (1988); Note, "*Hill v. Mobile Auto Trim, Inc.*: The Common Calling Standard," 40 BAYLOR L. REV. 2, 297-320 (1988).

B. *Martin*

The Martin case involved a three year non-compete covenant signed by an employee three years after the commencement of employment with a collection agency, upon the condition that he would be terminated if he did not sign the covenant.[143] Two years after signing the covenant, Martin quit his job at Credit Protection Association ("CPA"), joined with others to organize a new business, and began competing with CPA.[144] This competition included solicitation of CPA customers with whom Martin had dealt while employed at CPA.[145] CPA sought an injunction and damages.[146]

The trial court found that CPA's collection process comprised neither trade secrets nor confidential information, and held, on that basis, that CPA had not met its burden of showing a protectable employer interest.[147] The trial court went on to hold, however, that CPA had a protectable interest in a list of 1200 customers with whom Martin had dealt on CPA's behalf and that CPA was entitled to limited injunctive protection.[148]

The court of appeals affirmed.[149] In finding the four-part *Hill* test satisfied,[150] the court of appeals held that (1) Martin's "customer contact" was a legitimate interest of CPA, (2) that Martin was not "oppressed" by the three year restriction, (3) the restraint was not injurious to the public and (4) the training and salary received by Martin comprised consideration to make the covenant enforceable.[151] Additionally, the court of appeals concluded that Martin was not engaged in a "common calling, such as a barber, but, to the contrary. . . [was] unique to all CPA customers."[152]

The Texas Supreme Court, in a brief opinion, confirmed the continuing viability of the *Hill* test but did not comment on the manner in which the court of appeals had applied the test in the *Martin* case.[153]

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143. *Martin v. Credit Protection Assoc.*, 757 S.W.2d 24 (Tex. App. 1988).

144. *Id.* at 26.

145. *Id.*

146. *Id.*

147. *Id.* at 26-7.

148. *Id.* at 27. The trial court also awarded plaintiff reasonable attorneys' fees, but denied CPA's prayer for exemplary damages. *Id.*

149. *Id.* at 31.

150. See *supra*, note 91, and associated text.

151. *Martin v. Credit Protection Assoc.*, *supra*, note 5 at 29.

152. *Id.*

153. *Id.*

Instead, the Supreme Court rested its decision on the common calling issue, stating that:

> Martin was and is a salesman, a "common calling" occupation. We will not restrain the right of any individual to engage in a common calling.[154]

The Supreme Court therefore reversed the judgment of the court of appeals, dissolved the injunction, and held the restrictive covenant void.[155]

The court's brief opinion and terse conclusion with respect to the pivotal issue shed little light on the obvious question: what is a "common calling" occupation in Texas? It would seem, however, that in rejecting the court of appeals' conclusion that Martin's was not a common calling, the Supreme Court rejected the rationale upon which that conclusion was based, *i.e.*, that Martin had become "unique to all CPA customers."[156]

Employee "uniqueness", as a factor to be considered in enforcing non-compete covenants, is problematic.[157] It is clear, however, that the court of appeals' reliance on the "uniqueness" concept is misplaced. Unique employee services may comprise a protectable employer interest and may serve, by mutual exclusion, to define "common calling", but the court of appeals broke new ground in using employee's uniqueness to *convenatee's customers* as a basis for concluding that the employee was not engaged in a common calling. The appeals court's concept of uniqueness seems dangerously close to the truism that each of us is unique. (*i.e.*, one of a kind). Whatever "uniqueness" means in this context, it must mean more than that no two people are exactly alike. Otherwise, no one can be engaged in a common calling or, at most, a common calling situation could arise only when multiple salespeople were assigned to the same clients and/or territory—and the clients considered those sales people fungible. The state supreme court's opinion arrested movement in this direction, but did nothing to define "common calling".

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154. *Id.*
155. *Id.*
156. *Id.*
157. See *supra*, notes 59-62 and associated text.

C. *DeSantis*

The opinion in *Desantis* is considerably more detailed than that in *Martin*. In 1981, as a condition of the commencement his employment by the Wackenhut Corporation, DeSantis signed an agreement that he would not compete with Wackenhut, within a 40 county area, for a period of two years following the termination of his employment.[158] The agreement provided that its interpretation and enforcement would be governed by Florida law.[159] In 1984, DeSantis resigned, established a competing business and began soliciting customers, including some Wackenhut customers with whom he had dealt while employed by Wackenhut.[160]

Wackenhut sought an injunction and monetary damages, alleging breach of contract and tortious interference with contract and business relations.[161] The trial court issued an injunction, after reducing the geographic area of the proscription from 40 counties to 13.[162] The court of appeals affirmed and DeSantis appealed.[163]

1. *Choice of Law*

The Supreme Court of Texas first considered the parties' choice of Florida law. The court adopted the rule of Section 187 of the Restatement (Second) of Conflict of Laws, providing, *inter alia*, that (1) there must be a reasonable relationship between the parties and the state whose law is chosen and (2) the law of that state must not be contrary to any fundamental public policy of the forum state.[164] The court found the "reasonable relationship" aspect of the test satisfied.[165]

Turning to the public policy question, the court cited several differences between the relevant laws of Texas and Florida. In Florida, the court said, non-compete covenants are made enforceable by statute and courts are not empowered to refuse enforcement even when the covenant "would produce an unjust result in the form of an overly

158. *DeSantis, supra* note 5 at 617.
159. *Id.*
160. *Id.*
161. *Id.*
162. *Id.*
163. 732 S.W.2d 29.
164. Restatement (Second) of Conflicts of Laws (1971), Section 187.
165. *DeSantis, supra* note 5 at 618.

burdensome effect upon the employee."[166] Additionally, the Texas court asserted, Florida courts relax their normal standards for granting injunctive relief by *presuming* irreparable injury in the context of non-compete covenants.[167] Finally, the Texas court found that Florida courts "give no consideration to the type of work done by the employee. Thus, Florida courts have enforced convenants not to compete against hairstylists, telephone salespersons, and secretaries."[168] The Texas court found these considerations, taken together, sufficient to nullify the partie's choice of Florida law on the grounds that Flordia law regarding non-compete covenants is "contrary to the fundamental Texas public policy of promoting free movement of workers in the job market."[169]

2. *What is Reasonable?*

Testing the DeSantis covenant under Texas law, the court first determined that DeSantis, as an established professional in the security field and an office manager handling millions of dollars in gross annual revenues for Wackenhut, was not engaged in a common calling.[170] The court then proceeded to apply the *Hill* test, finding that the covenant failed two of the test's four parts. First, the jury had failed to find that Wackenhut would be irreparably harmed by DeSantis' competition. This failure, the Texas Supreme Court held, was "essentially equivalent to a failure to find that the covenant was necessary to protect Wackenhut."[171] This conclusion is unjustified, however, because the jury did not need to find irreparable harm under Florida Law, which *presumes* such harm.[172]

Secondly, the court held that the covenant was not supported by consideration, since "DeSantis had more than fourteen years as an established professional in the security business before he joined Wackenhut" and there was "no evidence that DeSantis obtained any special knowledge or training from Wackenhut."[173]

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166. *Id.*, citing *Twenty Four Collection, Inc. v. Keller*, 389 So.2d 1062, 1063 (Fla. Dist. Ct. App. 1980) rev. den. 419 So.2d 1048 (Fla. 1982).

167. *Id.*, citing *Cordis Corp. v. Prooslin*, 482 So.2d 486, 490 (Fla. Dist. Ct. App. 1986).

168. *Id.* citing, *Tiffany Sands, Inc. v. Mezhibousky*, 463 So.2d 349 (Fla. Dist. Ct. App. 1985); *Channell v. Applied Research, Inc.* 472 So.2d 1260 (Fla. Dist. Ct. App. 1985); *Rollins Protective Services Co. v. Lammons*, 472 So.2d 812 (Fla. Dist. Ct. App. 1985).

169. *Id.* at 620.

170. *Id.*

171. *Id.*

172. See *supra*, note 167 and associated text.

173. *DeSantis, supra* note 5 at 620.

On this point the court is simply incorrect in its application of the law. Consideration for an employee's non-compete covenant entered into at the inception of employment is found in the employment itself, *i.e.*, in the compensation the employee is promised and paid.[174] Although jurisdictions differ on the question whether mere continuation of employment is consideration for a covenant signed after an employee has begun work,[175] there is broad judicial consensus that a non-compete covenant included in an initial employment agreement (as was DeSantis') is supported by the same consideration that makes the rest of the agreement enforceable, *i.e.*, the promise of compensation.[176] The issue mislabeled "consideration" by the Texas Supreme Court should properly have been considered in connection with the question of whether Wackenhut, as covenantee, had a protectable interest (*e.g.*, trade secrets or customer lists) at stake. Here, the court has further compounded the confusion evident in its discussion of the consideration issue in the *Hill* case.

Nevertheless, on the basis of these two conclusions, the court found the covenant unreasonable and, therefore, unenforceable.[177] The court then turned its attention to DeSantis' counterclaims.

3. *Covenantor's Counterclaims*

At the trial level, DeSantis and RDI (DeSantis' newly formed company) brought counterclaims for monetary damages, fraud and tortious interference with Contractual relations.[178] Before the Supreme Court of Texas, they contested the denial of their damages claim, the grant of summary judgment for Wackenhut on the tortious interference claim, and the grant of a directed verdict for Wackenhut on the fraud claim.[179]

The claim for monetary damages was based on alternative theories: (1) a common law cause of action based on wrongful issuance of an injunction, and (2) a statutory claim that the covenant was an illegal restraint of trade, violating the Texas Free Enterprise and Antitrust Act.[180] The court held that because it had found the covenant unenforceable, DeSantis and RDI were entitled to damages.[181] RDI was

174. See *supra*, note 35.
175. See *supra* notes 36-37 and associated text.
176. *Id.*
177. *Id.*
178. *DeSantis, supra.*
179. *Id.*
180. TEXAS BUS. & COM. CODE Sec. 15.21(a)(1).
181. *Id.* at 621.

awarded $18,000 actual damages as found by the jury, prejudgment interest and costs, and reasonable attorney's fees.[182] DeSantis recovered only attorney's fees and costs as the jury had found that he sustained no actual damage.[183] Ominously, the court also stated that although there had been no showing of willfulness or flagrant misconduct by Wackenhut, the presence of these elements would have made treble damages appropriate.[184]

IV. Conclusion

While the Martin and DeSantis cases appear to cast serious doubt upon the continuing viability of post-employment non-compete covenants in Texas, they are not clear and logical steps towards an articulated policy objective. Instead, they compound and may tend to institutionalize the confusion created by the majority opinion in *Hill*. Thus, although the Supreme Court of Texas would appear to be at the forefront of efforts to reign in restrictive covenants, recent Texas case law provides inadequate footing for a successful attack on such restraints.

182. *Id.*
183. *Id.*
184. *Id.*