



**Texas Supreme Court Significantly Changes Law on Covenants Not to Compete—
*Marsh USA, Inc. and Marsh & McLennan Companies v. Cook***

By: Jim McInerney

In June 2011, the Texas Supreme Court took another large step toward helping Texas employers protect their relationships with customers, by holding that a company's provision of stock options to employees was adequate consideration for a non-compete agreement. *Marsh USA, Inc. and Marsh & McLennan Companies, Inc. v. Cook*, No. 09-0558 (Tex. June 24, 2011).

A covenant not to compete is an agreement between an employer and an employee restricting the employee's ability to solicit customers and employees of his or her employer in the event that the employee leaves employment. If this sounds like a restriction on an employee's ability to seek new work, it is. In the past, Texas courts routinely struck down non-compete agreements as invalid restraints on an employee's ability to contract for new employment.

In an effort to balance an employee's right to find new work with an employer's interest in protecting its business from unfair competition, the Texas legislature passed the Covenants Not to Compete Act (CNCA), which attempted to impose reasonable restrictions on an employee's ability to compete with a former employer. The goal of this legislation was to encourage employers to entrust confidential information and important client relationships to key employees, without the fear that an employee would quit and immediately begin competing against their former employer.

In interpreting the CNCA, the Texas Supreme Court held that, because covenants not to compete are contracts, they must be supported by adequate consideration—that is, the employer must give the employee something of value in exchange for the agreement not to compete. In *Light v. Centel Cellular of Texas*, 883 S.W.2d 643 (Tex. 1994), the supreme court held that the consideration for a non-compete agreement must give rise to the employer's interest in keeping the employee from competing. *Light's* restrictive interpretation of the CNCA prevented many non-competes from being enforced. However, in recent years, the Texas Supreme Court has expanded the enforceability of covenants not to compete.

The *Marsh* decision continues that trend. Rex Cook, a managing director of Marsh USA, Inc., signed a non-compete agreement that he would not solicit Marsh's clients, recruit its employees, or disclose confidential information in exchange for exercising stock options at a discounted price. Less than three years after signing the agreement, Cook resigned his employment and went to work for a direct competitor. Marsh then sued him for breaching the agreement. The trial court found the non-compete agreement unenforceable. The Texas Court of Appeals agreed, holding that the transfer of stock did not give rise to Marsh's interest in restraining its former employer from competing.

The Texas Supreme Court reversed the judgment of the Court of Appeals, and held that the business interest being protected (Marsh's goodwill) was reasonably related to the consideration given (stock options) and the covenant not to compete was enforceable against Cook. The supreme court noted that Texas law has long held that a company's goodwill, though intangible, is property, and an integral part of the business.

The significance of this ruling is that the supreme court found a non-compete agreement supported by financial incentive to be enforceable, a departure from previous decisions. Not surprisingly, there was a vigorous dissent to the majority opinion. One dissenter expressed concern that *any* financial incentive, including a raise, a bonus or even a salary could support an enforceable covenant not to compete, effectively allowing an employer to *buy* a covenant not to compete, something Texas courts have never allowed.

Whether or not the *Marsh* decision goes as far as the dissenting justices fear, its effect will allow employers in Texas to include covenants not to compete in many more employment-related contracts than before.

ABOUT THE AUTHOR

Jim McInerny has over 20 years' experience representing clients in employment matters. He is Board Certified in Labor and Employment Law by the Texas Board of Legal Specialization. Jim's practice focuses on defending employers from claims of discrimination and wrongful termination in state and federal court. He also advises clients on all aspects of employment law, including immigration issues, OSHA citations, wage and hour matters, hiring and termination decisions, employee handbooks, and non-compete agreements.

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