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## TEXAS SUPREME COURT CLARIFIES ENFORCEABILITY OF NONCOMPETES

The September 13, 2006 edition of Health Industry Online discussed covenants not to compete ("noncompetes") under Texas law in relation to physician employment and physician investment in competing interests or ventures. One of the aspects of noncompetes discussed therein was the requirement that the noncompete be ancillary to or part of an otherwise enforceable agreement "at the time the agreement is made."

This Texas Supreme Court discussed this requirement in its 1994 *Light v. Cellular* decision. As construed by the various Texas appellate courts, the *Light* decision mandated that consideration to support a noncompete must be of a certain type (confidential information, trade secrets, etc.) and the employer's promise to provide the consideration must be enforceable at the same time the employee gives his or her return promise not to disclose the information or compete. Based upon this construction, most of the Texas appellate courts endorsed a noncompete enforceability test which essentially required an employer to simultaneously exchange appropriate confidential information with the employee at the time the employee signs the noncompete agreement.

Practically speaking, this approach was usually burdensome for employers and oftentimes simply impossible. Moreover, this approach failed to acknowledge employers' needs to protect the valuable confidential and proprietary information that employees ultimately received during their employment, even if they did not do so the very day that they signed the noncompete. Legally speaking, this approach provided employees an easy way avoid noncompetes – if the noncompete did not recite that consideration would be simultaneously exchanged, the noncompete as written was unenforceable.

On Friday, October 20, 2006, the Texas Supreme Court re-entered the noncompete arena in *Sheshunoff Mgmt Servs., LP v. Johnson, et. al*, holding that:

An at-will employee's non-compete covenant becomes enforceable when the employer performs the promises it made in exchange for the covenant. In so holding, we disagree with the language in *Light* stating that the Covenants Not to Compete Act requires the agreement containing the covenant to be enforceable the instant the agreement is made.

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Thus, a noncompete will become enforceable once the employer actually provides confidential information to the employee in accordance with its promise to do so.

In addition, the Court also emphasized the following:

- An employer cannot create an enforceable noncompete by promising to give notice before termination, or by paying monetary consideration. Instead, as before, only promises related to the provision, receipt and non-disclosure of confidential information can support a noncompete. Therefore, the employer's promise must be to provide confidential information to the employee and the employee must, in turn, promise to maintain the confidentiality of the information and refrain from disclosing it.
- Employers cannot obtain enforceable noncompetes with existing employees simply by having them sign an agreement. The employer must, instead, promise to and actually provide the existing employee with new confidential information.
- The enforceability of noncompetes under Texas law was never intended to depend upon "overly technical disputes." Rather, the "core inquiry" is whether the noncompete's restrictions as to time, geographical area, and scope of activity are reasonable and are not greater than necessary to protect the employer's goodwill or business interests.

What does this mean for entities such as employers and physician groups who want enforceable noncompetes? Noncompetes should affirmatively state that the employer promises to provide confidential information and the employee promises to maintain confidentiality and not disclose the information. The Court's opinion emphasized the employer's "promise" to the employee; consequently, nothing in the opinion provided direct or implied approval of agreements stating that an employee "may have access to" confidential information. After making the promise in writing, employers need to give employees confidential information, the sooner the better. The Court noted that undue delay in providing the information – such as waiting until the employee's termination – would weigh against the noncompete being reasonable. When confidential information is provided, it would be prudent for employers to document that the information was given at that time. Employers still need to draft reasonable noncompetes which do not overly restrict an employee's post-employment efforts. Finally, physician groups need to remain mindful of the special requirements imposed upon physician noncompetes (access to patient list and medical records, buy-out option, continuing care during course of acute illness) and incorporate these requirements into the noncompete.