

TADC EMPLOYMENT LAW NEWSLETTER

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I. TEXAS SUPREME COURT DECISIONS.

A. COVENANTS NOT TO COMPETE - A promise not to compete may be implied and thus, a covenant not to compete may be enforceable, if the nature of the employment for which the employee is hired reasonably requires the employer to provide confidential information to the employee.

Three years ago, in *Alex Sheshunoff Management Services, L.P. v. Johnson*, 209 S.W.3d 644 (Tex. 2006), the Texas Supreme Court strengthened the enforceability of non-compete agreements by rejecting the requirement that an employer contemporaneously provide an employee with confidential information at the signing of the non-compete agreement in order for the agreement to be enforceable. In so doing, the Texas Supreme Court held that an employer's promise to share confidential information could be consideration for a covenant not to compete even though the promise is made in connection with employment at will. The employee's covenant, however, only becomes binding once the employer actually provides confidential information. The *Sheshunoff* Court, nevertheless, left open the issue of whether or not the promise to share had to be expressly made in order to be considered adequate consideration. Earlier this year, in *Mann Frankfort Stein & Lipp Advisors Inc. v. Fielding*, __S.W.3d__, 2009 WL 1028051 (Tex. 2009), the Texas Supreme Court answered this question and held that the promise to share confidential information might be implied in an appropriate case.

In *Mann Frankfort*, the Texas Supreme Court determined whether a covenant not to compete in an at-will employment agreement was enforceable when the employee expressly promised not to disclose confidential information, but the employer made no express return promise to provide confidential information.

The facts of this case involved an employee who signed an employment agreement that contained a client purchase provision¹ and in which the employee promised he would "not disclose or use at any time...any secret or confidential information or knowledge obtained by while employed..." The employee subsequently resigned and filed a declaratory judgment action seeking to have the client purchase provisions declared unenforceable. The lower court granted the employee's motion. On appeal, the court of appeals held that the client purchase provision was unenforceable because it was not ancillary to or part of an otherwise enforceable agreement as required under the Covenant Not to Compete Act (TEX. BUS. & COM. CODE §15.50(a)). The court of appeals explained that because the employee never acknowledged that he received confidential information, and the employer had not expressly promised to provide confidential information, there was no "otherwise enforceable agreement" to which the employee's covenant could be "ancillary."

The Texas Supreme Court disagreed. The Court found the client purchase provision to be enforceable because it held there was an implied employer promise to provide confidential information. The Court reasoned that even if there is not an express promise by the employer to provide confidential information, there might be an implied promise to do so if the nature of the work for which the employee is hired reasonably required confidential information to be provided to the employee. The facts of the case showed that the employer had fulfilled his implied promise by providing confidential information to the employee, and as such, the Court held the employee was bound to the provisions of the employment agreement.

The significance of this holding is that some noncompeting agreements that were previously unenforceable will now be enforceable.

¹ The "client purchase provision" read as follows:

"If at any time within one (1) year after the termination or expiration hereof, Employee directly or indirectly performs accounting services for remuneration for any party who is a client of Employer during the term of this Agreement, Employee shall immediately purchase from Employer and Employer shall sell to employee that portion of Employer's business associated with each such client."

B. NON-SIGNATORIES AND ARBITRATION AGREEMENTS – An arbitration agreement between a decedent and his employer requires the employee’s wrongful death beneficiaries to arbitrate their claims against the employer.

In re Jindal Saw Ltd., ___ S.W.3d___, 2009 WL 490082 (Tex. 2009) the Texas Supreme Court reaffirmed its recent decision in *In re Labatt Food Service*, 279 S.W.3d 640 (Tex. 2009), holding that an arbitration agreement between a decedent and his employer requires the employee’s wrongful death beneficiaries to arbitrate their claims against the employer.

The employer in this case did not provide worker’s compensation insurance to cover its employees, but rather, it provided an optional benefit plan. The employee had elected to participate in the plan which contained an arbitration agreement, requiring all disputes related either to the benefit plan, the arbitration agreement, or the employee’s employment to be submitted to arbitration. The employee subsequently died from work-related injuries. The nonsubscriber employer moved to compel arbitration when the wife and children of the deceased employee filed a wrongful death action.

The lower court held that the family member’s were bound to the arbitration agreement with respect to the deceased employee’s survival action but not with respect to the wrongful death action. The Texas Supreme Court saw no distinction and followed the prior precedent of *Labatt*, holding that the pre-death arbitration agreement bound family members because the wrongful death action was entirely derivative of the decedent’s rights.

II. TEXAS APPELLATE COURT DECISIONS

A. GOVERNMENTAL IMMUNITY – A statute is not a contract by a local government, but a municipal ordinance and collective bargaining agreements are contracts by that local government.

In City of Houston v. Williams, 290 S.W.3d 260 (Tex. App.—Houston [14th] 2009), retired firefighters brought action against the city, alleging that the city had failed to pay certain compensation, including termination benefits, as was required by local statutes, ordinances, and collective bargaining agreements. The city alleged that the court lacked jurisdiction on the basis of governmental immunity. The firefighters argued that the city had waived its governmental

immunity under Texas Local Government Code §§271.151 – 271.160, but they did not otherwise refer to a written contract.

The lower court denied the city’s plea to jurisdiction and granted a partial summary judgment in favor of the firefighters. The Houston Court of Appeals, 14th District, affirmed. The Texas Supreme Court reversed and remanded the case for consideration of whether the firefighter’s claims fell within the Local Government Code sections.

The provisions of the Texas Local Government Code allow for a local government entity that enters into a contract for goods or services to be sued. The provisions at issue define a contract to be a “written contract stating the essential terms of the agreement for providing goods and services to the local government entity.” The firefighter’s claims in this case, however, were not based on contracts in the traditional sense. The firefighters were relying on state statutes, local ordinances, and collective bargaining agreements. The court held: (1) the state statutes were not contracts between the city and the firefighters; (2) municipal ordinances constituted a written contract subject to the waiver of sovereign immunity; and (3) the collective bargaining agreements were contracts between the city and the firefighters association, but the firefighters lacked standing to sue the city for breach of the agreement because they were not parties to the agreements.

B. GOVERNMENTAL IMMUNITY – A requested declaration and injunction did not require the payment of money, and as such, these claims did not implicate governmental immunity.

In Lowell v. City of Baytown, Texas, 264 S.W.3d 31 (Tex. App.—Houston [1st] 2007), firefighters sued the city, alleging that they had not been paid their seniority pay when serving temporarily in higher classifications. Under the Civil Service Act, a firefighter, while filing in a higher position, is entitled to the base salary of the higher position as well as the employee’s own seniority pay. The firefighters sought a declaratory judgment and injunction.

The city filed a plea to the jurisdiction, asserting that the city’s governmental immunity from suit had not been waived and that the firefighters had not exhausted their administrative remedies. The trial court granted the city’s plea and dismissed the case for lack of subject matter jurisdiction.

On appeal, the firefighters argued that the trial court had jurisdiction under the Declaratory Judgment Act to construe the Civil Service Act. The court of appeals explained that a suit to construe a statute or ordinance pursuant to the Declaratory Judgment Act does not implicate governmental immunity from suit. The court held: (1) because the firefighters' requested declaration and injunction did not require the payment of money damages, the firefighters' claims did not implicate governmental immunity; and (2) the firefighters' claims were not governed by the collective bargaining agreement, and thus, the administrative remedies within the collective bargaining agreement did not apply.

III. FEDERAL FIFTH CIRCUIT COURT DECISIONS

A. ARBITRATION – The right to arbitration can be waived by substantial invocation of the judicial process.

While not overtly an employment law decision, the Fifth Circuit's opinion in *Nicholas v. KBR*, 565 F.3d 904 (5th Cir. 2009) will likely have an impact on employment litigation. In *Nicholas*, the plaintiff appealed the district court's denial of her motion to compel arbitration of her contract dispute with the defendant. The district court had ruled that the plaintiff had waived her right to arbitrate.

On appeal, the Fifth Circuit narrowed its analysis of whether a party waived its right to invoke an arbitration provision to a two-step process: (1) a substantial invocation of judicial process; and (2) prejudice to the other party. The facts of the case are convoluted, but in pertinent part, the plaintiff filed the lawsuit without asserting a request for arbitration and then waited ten-months before moving to compel arbitration. In reviewing the facts, the court concluded that the act of a plaintiff filing suit without asserting a right to arbitrate constitutes substantial invocation of the judicial process, unless an exception applies. Although the court acknowledged that the party normally seeking to invoke is the party being sued, the court explained that the legal standard for waiver is the same regardless of which party is alleged to have waived arbitration.

The court discussed a number of exceptions that might apply to the substantial invocation of judicial process. One such exception could be where a lawsuit was filed that was not inconsistent with seeking arbitration. For example, a plaintiff might file a suit seeking a declaration of a valid arbitration agreement.

The court's list of exceptions was not exhaustive, but it held that one did not exist in the case at hand.

In addition to finding substantial invocation of judicial process, the court found that the significant litigation activity before the plaintiff's demand for arbitration had caused prejudice to the defendant. The court explained that prejudice in the context of waiver refers to "delay, expense, and damage to a party's legal position." The court held that delay alone will not constitute waiver, but it may combine with other activities, such as pretrial activity, to result in prejudice.

In conclusion, the court held that (1) the plaintiff had substantially invoked judicial process by bringing suit without also seeking arbitration, and (2) delayed invocation of the arbitration process prejudiced the defendant, also supporting a finding of waiver of arbitration.