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Business Torts

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BUSINESS TORTS

Charles M. Hosch*
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TABLE OF CONTENTS

I. DEFAMATION	338
WHAT IF THE PRODUCT <i>Is</i> Bad?	338
II. FRAUD	340
FRAUD AND THE MERGER CLAUSE	340
III. TORTIOUS INTERFERENCE	341
A. BECOMING THE MIDDLEMAN	341
B. SOVEREIGN IMMUNITY LIVES	344
C. HOW LONG MAY THIS ACTIVITY GO ON?	345
IV. NON-COMPETE AGREEMENTS	347
A. WILL UNCLEAN HANDS BAR ENFORCEABILITY?	347
B. STOCK OPTIONS AND “GIVING RISE” TO THE NEED FOR A COVENANT	348
C. TRADEMARKS DO NOT RESTRICT COMPETITION	349
D. ARE NON-SOLICITATION COVENANTS GOVERNED AS NON-COMPETES?	350
E. NON-COMPETE AGREEMENTS AND THE GLOBAL ECONOMY	351
F. IMPLIED PROMISES AND “FORCED SALE” PROVISIONS ..	352
V. BREACH OF FIDUCIARY DUTY	354
A. MIGHT FEES BE FORFEITED? OR MUST THEY BE?	354
VI. TRADE SECRETS AND CONFIDENTIAL INFORMATION	355
A. CRAFTING THE INJUNCTION	355
B. PLEADINGS, SUMMARY JUDGMENT, AND “USE”	356
C. ONE BITE, NOT TWO	357
D. NOT EVERY “STRATEGY” IS A TRADE SECRET	359
E. TRADE SECRETS AND THE AGING PROCESS	360
VII. FALSE ADVERTISING	363
A. PUFFING AGAIN	363
B. WHO IS THE ADVERTISER? AND WHAT IS AN “ADVERTISEMENT”?	364

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VIII. COMPUTER FRAUD AND ABUSE ACT.....	365
WHAT IS "AUTHORIZATION"?	365
IX. CONCLUSION	367

THIS year saw interesting applications and reminders in a number of areas, including noncompetition covenants, trade secrets, tortious interference, and others.

I. DEFAMATION

WHAT IF THE PRODUCT IS BAD?

Turbochargers are serious business, and the respective merits of different makes and models are fiercely debated in the turbocharger community. So it happened in *David Rafes, Inc. v. Huml*,¹ where plaintiff Rafes claimed that Huml and Slowboy Racing, Inc., published defamations about Rafes and the quality of Rafes's turbocharger over the Internet. Rafes claimed Huml and Slowboy had said that "Rafes's turbocharger was a 'poorly manufactured turbo from China' that would 'inevitably fail in a short amount of time,'" was "'a Chinese version us[ing] an inferior stainless in its composition,'" and "was composed of metal, or, 'some type of powdered metal,' that would 'not hold up to the heat and abuse.'"² Rafes also claimed that the pictures published with the article actually showed a turbocharger made by someone else, and that Huml and Slowboy had implied that Rafes's turbocharger had been scientifically tested, when in fact it had not.³

The trial court indicated some uncertainty about "the law of business disparagement" and damages for libel, but it may have been simply cutting to the point at the conclusion of a bench trial when it issued "'preliminary' findings" to the effect that there was indeed something wrong with Rafes's turbocharger, as Rafes's "witnesses or witness" had conceded—"just not anything that Mr. Huml or that the defendants said was wrong with it."⁴ The trial court observed that whether or not Rafes had been slandered, the turbocharger was evidently a "bad product" whose manufacturing problems would have cut deeply into Rafes's damages in any event.⁵ When the plaintiff's counsel questioned whether there was really any evidence that its product was a "bad product," the trial court answered, "Well, it is there. Trust me."⁶

On appeal, the Houston First Court of Appeals noted that "substantial

1. No. 01-08-00856-cv, 2009 WL 3491043 (Tex. App.—Houston [1st Dist.] Oct. 29, 2009, no pet.).

2. *Id.* at *1 (alterations in original).

3. *Id.*

4. *Id.* at *2. Statutory libel is governed by chapter 73 of the Tex. Civ. Prac. & Rem. Code, though common law defenses are maintained under section 73.006. Business (or "commercial") disparagement requires proof of publication of a falsity, malice, and special damages. *Hurlbut v. Gulf Atl. Life Ins. Co.*, 749 S.W.2d 762, 766 (Tex. 1987).

5. *Rafes*, 2009 WL 3491043, at *2.

6. *Id.*

truth” is sufficient to defeat a libel claim.⁷ The court explained that the accused statement need not be “literally true in every detail; substantial truth is sufficient.”⁸ The court of appeals added that in order to determine if the allegedly defamatory statement is “substantially true,” the question to ask is whether it was “more damaging to the plaintiff’s reputation, in the mind of the average person, than a truthful statement would have been.”⁹

The trial court did not enter explicit and final findings or conclusions, but the court of appeals read the trial court’s judgment as “impl[ying] all findings of fact necessary to support it,”¹⁰ and expressly noted that among these implied findings was an affirmative defense of substantial truth.¹¹ And, indeed, the court of appeals found sufficient evidence to support what it described as the trial court’s “blunt[] summar[y]” that the plaintiff’s turbocharger was a “bad product.”¹² The court described at length the testimony of the defendants’ expert on the subject matter of turbochargers, who testified that he had “serious concerns” about “every part” of the plaintiff’s turbocharger, mostly “for the same reasons” as the defendants had observed, and indeed even more concerns about the product than the defendants had identified in their article.¹³ Not surprisingly, Rafes had its own expert who defended the plaintiff’s product and disputed the claims of his counterpart on the other side, but, significantly, the court of appeals accepted the trial court “as the sole judge of the credibility of the witnesses” and therefore “entitled to accept or reject all or any part of the [dueling experts’] testimony.”¹⁴

In these circumstances, it probably would not matter much whether the action was brought as a libel or slander case, as a commercial disparagement case, or even a case under section 43(a) of the Lanham Act.¹⁵ Nor, perhaps, might it have mattered how clearly the defendants had pled their affirmative defenses. If the fact finder finds the plaintiff makes a “bad product,” the defendant can say so, and can say it bluntly and with impunity. In the spirit of what Garry Trudeau once said, this may be an example of “free speech at its most bracing.”¹⁶

7. *Id.* at *4.

8. *Id.* (citing *Gustafson v. City of Austin*, 110 S.W.3d 652, 656 (Tex. App.—Austin 2003, pet. denied); *Howell v. Hecht*, 821 S.W.2d 627, 631-32 (Tex. App.—Dallas 1991, writ denied)).

9. *Id.*

10. *Id.* at *2-3

11. *Id.* at *4 n.3, *7.

12. *Id.* at *5.

13. *Id.* at *5-6.

14. *Id.* at *6.

15. 15 U.S.C. § 1125(a) (2006).

16. See *Cartoonist Trudeau Foresees Protest*, ST. PETERSBURG TIMES, June 10, 1983, at A3 (“free and open society at its most bracing”).

II. FRAUD

FRAUD AND THE MERGER CLAUSE

As a matter of routine, written agreements often say that they contain within them the entirety of the parties' agreement, superseding all earlier discussions, understandings, and agreements, and that there are no other agreements or commitments between the parties except the written ones in the document being signed. These are commonly called "merger" clauses because they seek to "merge" all previous and concurrent discussions between parties into one document in hopes of reducing the risk of surprises later on.

Questions of fraud, particularly fraudulent inducement, sometimes complicate this analysis. This occurred in *LJ Charter, L.L.C. v. Air America Jet Charter, Inc.*,¹⁷ in which the jury found that one air charter company committed common-law fraud against another one in connection with the lease of an aircraft hangar at Hobby Airport.¹⁸ On appeal, one issue involved whether the merger clause in the parties' agreement precluded the plaintiff's claims for common-law fraud.¹⁹

The merger clause in the agreement provided: "This Agreement constitutes the entire agreement of the parties hereto and supercedes any prior understandings or written or oral agreements between the parties respecting the subject matter hereof, and may only be modified in writing executed by all of the parties hereto."²⁰ Citing *Ikon Office Solutions, Inc. v. Eifert*,²¹ the defendant urged that the merger clause must preclude any reasonable reliance by the plaintiff on any commitments outside the terms of the contract—for according to this clause, there were none.²²

The Houston Fourteenth Court of Appeals distinguished *Eifert*, however, finding that the merger clause in the *Eifert* employment agreement included *additional* language besides what the court described as the "standard merger clause language."²³ This additional language provided that "[n]o commitments have been made relative to bonuses, guarantees or any other special provisions, except as specifically identified herein."²⁴ The court of appeals concluded that the expanded merger clause in *Eifert* distinguished it from the one in this case, because bonuses and the like were part of what was at issue in *Eifert*. "[U]nlike the merger clause in *Eifert*," the court explained, "the merger clause [here] does not contain a specific clause disclaiming reliance on representations concerning matters

17. No. 14-08-00534-CV, 2009 WL 4794242 (Tex. App.—Houston [14th Dist.] Dec. 15, 2009, pet. filed).

18. *Id.* at *5.

19. *Id.* at *11.

20. *Id.*

21. 125 S.W.3d 113 (Tex. App.—Houston [14th Dist.] 2003, pet. denied).

22. Among other elements, a plaintiff in a common-law fraud action must show that the defendant made a false representation intending that the other party rely on it, and that the other party did rely on it. *LJ Charter*, 2009 WL 4794242, at *11.

23. *Id.* at *11-12.

24. *Id.* at *11.

in dispute in this litigation.”²⁵ The court did realize that a merger clause “that clearly expresses the parties’ intent to waive fraudulent inducement claims, or one that disclaims reliance on representations about specific matters in dispute, can preclude a claim of fraudulent inducement,”²⁶ but it held that the merger clause in *LJ Charter* was not sufficient in that respect.²⁷

It may not be practicable, or even possible, to anticipate and address every imaginable representation about specific matters that might later come into dispute, and to specifically disclaim reliance on them, but clearly expressing an intent to waive fraudulent inducement claims may be advisable in some circumstances.

III. TORTIOUS INTERFERENCE

A. BECOMING THE MIDDLEMAN

Auditorium chairs may be sold through multiple levels. Manufacturers will sell to distributors, distributors will sell downstream to dealers, and dealers will then sell to end-user customers. Distributors and dealers may each offer their own warranties and other value commitments, and they typically operate on nonexclusive arrangements. In this highly competitive environment, these arrangements can often lead to disputes, as happened in *Smith v. Royal Seating, Ltd.*²⁸

Royal Seating was a nonexclusive distributor of a certain type of auditorium chair made in Mexico. Royal Seating would buy chairs from the manufacturer and resell them to dealers, such as Rock Systems, who would then sell the chairs to consumers.²⁹

In 2006, Royal Seating, acting as the distributor, and Rock Systems, the dealer, were negotiating with three churches in California who joined together to buy 8,700 chairs and installation services. Representatives from both distributor Royal Seating and dealer Rock Systems were involved in these negotiations. Eventually, dealer Rock Systems bought the chairs and sold them to the churches, but it did not buy them from distributor Royal Seating. Instead, it formed its own new company, Lone Star Seating, to act as its own distributor.³⁰ Distributor Royal Seating brought suit for tortious interference with a prospective contract, claiming it would have sold the seats to the churches (presumably through dealer Rock Systems) if the defendants had not intentionally interfered and shoved Royal Seating aside. After a bench trial, the trial court agreed, and entered judgment in favor of plaintiff–distributor Royal Seating.³¹

25. *Id.* at *12.

26. *Id.* at *11 (quoting *Schlumberger Tech. Corp. v. Swanson*, 959 S.W.2d 171, 181 (Tex. 1997)).

27. *Id.* at *12.

28. No. 03-09-00114-CV, 2009 WL 3682644 (Tex. App.—Austin, Nov. 6, 2009, no pet.).

29. *Id.* at *1.

30. Lone Star Seating was formed by Bobby J. Smith, principal of dealer Rock Systems, at the end of 2006. *Id.* at *1.

31. *Id.* at *1-2.

The issues on appeal focused on a fact-intensive study of the evidence, measured against the elements of tortious interference with prospective business relationships. The Austin Court of Appeals outlined those elements as follows:

To establish tortious interference with a prospective business relationship, a plaintiff must prove (i) a reasonable probability that the plaintiff would have entered into a business relationship; (ii) an independently tortious or unlawful act by the defendant that prevented the relationship from occurring; (iii) the defendant did such act with a conscious desire to prevent the relationship from occurring or the defendant knew the interference was certain or substantially certain to occur as a result of the conduct; and (iv) the plaintiff suffered actual harm or damages as a result of the defendant's interference.³²

The court of appeals noted that plaintiffs are not required to show a lack of justification or privilege for the defendant's action.³³

The court examined evidence relating to each of these elements and concluded that it was legally and factually sufficient.³⁴ Much discussion revolved around whether there was a reasonable probability that Royal Seating would have entered into a business relationship.³⁵ The court noted testimony that the churches wanted a warranty that ran from Royal Seating, quoting testimony from one witness that "[t]he determining factor with [one of the churches] was the lengthy warranty [from Royal Seating]."³⁶ There was also a check made payable to "Rock Systems Group/Royal Seating, Ltd." from one of the churches, a purchase order and an "AIA document" between that church and "Rock Systems Group/Royal Seating Ltd." and a "purchase agreement" from another of the churches that was entitled "Rock Systems Group/Royal Seating, Ltd." The court of appeals concluded from all of this "that the evidence was legally and factually sufficient to support the district court's finding" of "a reasonable probability that Royal Seating and the churches would have entered into a business relationship."³⁷ Similarly, the court of appeals found sufficient evidence of a "conscious desire to prevent the business relationship between the churches and Royal Seating from occurring," since Rock Systems' principal had intentionally substituted his own new company as the distributor in the deal.³⁸

Unlike the cause of action for tortious interference with existing contracts, tortious interference with prospective contracts or prospective business relationships requires a showing that the act alleged to constitute an interference be itself "independently tortious or otherwise wrongful" in

32. *Id.* at *3 n.6 (citing *Wal-Mart Stores, Inc. v. Sturges*, 52 S.W.3d 711, 726 (Tex. 2001)).

33. *Id.* at *3 n.7 (citing *Wal-Mart*, 52 S.W.3d at 726-27).

34. *Id.* at *3-9.

35. *Id.* at *3-5.

36. *Id.* at *4-5.

37. *Id.* at *5.

38. *Id.* at *6.

and of itself, separate and apart from the fact that it causes an interference.³⁹ The court of appeals noted the *Wal-Mart Stores, Inc. v. Sturges* standard for “independently tortious” conduct, and addressed whether there was legally and factually sufficient evidence of that conduct in this record.⁴⁰ Royal Seating claimed Rock Systems had committed two such independent torts—fraud and conversion—through its conversion of a check from one of the churches made payable to “Rock Systems Group/Royal Seating, Ltd.” which Rock Systems deposited into its own account without telling Royal Seating.⁴¹ The court of appeals quoted lengthy testimony from the trial record, concluding it was legally and factually sufficient to support a finding that the acts were independently tortious and unlawful.⁴² The court of appeals focused on the claim of conversion “[b]ecause it is dispositive”⁴³ and did not reach Royal Seating’s claim that Rock Systems had also committed fraud “by not disclosing that they planned to divert the sales to the churches from Royal Seating to themselves and that they were secretly negotiating with [the manufacturer] to accomplish this result.”⁴⁴

This was a two-to-one opinion, however, issued over a strong dissent. The dissent viewed the majority as showing “unwarranted and improper deference to the trial court [in affirming] the trial court’s erroneous judgment.”⁴⁵ In the dissent’s view, “Royal Seating did not produce legally sufficient evidence to support” either “a reasonable probability that [it] would have entered into a business relationship with the churches or that Rock Systems’s conduct was independently tortious or wrongful.”⁴⁶ Instead, the dissent characterized Royal Seating’s evidence as “vague and uncertain”⁴⁷ on some points and entirely lacking on others.⁴⁸ *By contrast, the dissent found* “clear, positive, and direct testimony” from Rock Systems that the first contact from the churches came through it, rather than through Royal Seating.⁴⁹ The dissent also found that Royal Seating was never able to show that the churches “had made a final decision” to buy chairs from Royal Seating through Rock Systems.⁵⁰ “At most,” said the dissent, the evidence showed that one Lazarian, “whose authority was never defined or explained, indicated at one point that he planned to buy

39. *Id.* at *3 n.6, *7.

40. *Id.* “By independently tortious we do not mean that the plaintiff must be able to prove an independent tort. Rather, we mean only that the plaintiff must prove that the defendant’s conduct would be actionable under a recognized tort.” *Id.* at *7 (quoting *Wal-Mart Stores, Inc. v. Sturges*, 52 S.W.3d 711, 726 (Tex. 2001)). *See id.* at *7-8 (reviewing the evidence).

41. *Id.* at *6, 7.

42. *Id.* at *6-8.

43. *Id.* at *6.

44. *Id.* at *6 n.12.

45. *Id.* at *9.

46. *Id.*

47. *Id.* at *11.

48. *Id.* at *11-12.

49. *Id.* at *11.

50. *Id.*

Royal Seating's chairs."⁵¹

In particular, the dissent urged that there was insufficient evidence of a reasonable probability that Royal Seating would have gotten the business, because there was no evidence that the churches did not simply change their minds at the last minute—as the dissent noted they were perfectly free to do. “A customer is entitled to solicit bids and conduct in-depth negotiations right up until the moment it enters into a contract. . . . [And it may change] its mind at the last minute.”⁵² The dissent found no fraud because Royal Seating had not shown any duty on Rock Systems' part to disclose its plans.⁵³ The dissent also found no evidence of conversion because Royal Seating did not have any ownership or possession rights to the check, and “[the church's] mistaken use of Royal Seating's name on the check does not give Royal Seating a right to possession of the money.”⁵⁴

Tortious interference cases are heavily fact intensive, which implies that, on appeal, there should be great deference shown to the fact finder. On appeal from this bench trial, the majority held that the trial court is the “sole judge of the credibility of the witnesses and the weight to be given their testimony” . . . [and] may believe one witness, disbelieve others, and resolve inconsistencies in any witness's testimony.”⁵⁵ The dissent, by contrast, urged that “in considering the sufficiency of the evidence, we must also be mindful that in some cases, certain evidence may not be credited just as other evidence may not be disregarded by a reasonable fact-finder.”⁵⁶ The tension between these two principles may be resolved elsewhere. Meanwhile, cutting out the middleman by becoming the middleman proved unsuccessful for this appellant.

B. SOVEREIGN IMMUNITY LIVES

Zoning restrictions often restrict fireworks operators on where they can sell. In *City of Houston v. Guthrie*,⁵⁷ a group of fireworks operators and property owners located outside the city limits of Houston, but inside certain Harris County municipal utility districts (MUDs), challenged the use by Houston and the MUDs of “certain strategic partnership agreements and the Houston City Fire Code” to ban the sale of fireworks where they were located.⁵⁸ Among other claims, the fireworks operators and property owners claimed that these actions constituted a tortious interference (presumably with the fireworks operators' prospective relationships with their customers, and with the property owners' lease

51. *Id.*

52. *Id.* at *12.

53. *Id.* at *13.

54. *Id.* at *14.

55. *Id.* at *3 (citing *McGalliard v. Kuhlmann*, 722 S.W.2d 694, 696-97 (Tex. 1986)).

56. *Id.* at *10 (citing *City of Keller v. Wilson*, 168 S.W.3d 802, 807 (Tex. 2005)).

57. No. 01-08-00712-CV, 2009 WL 5174258 (Tex. App.—Houston [1st Dist.] Dec. 31, 2009, no pet. h.).

58. *Id.* at *1.

agreements with the fireworks operators, though the opinion was not specific on this point).⁵⁹ The City and the MUDs urged that the trial court lacked jurisdiction to consider this claim, however, because tortious interference would not fall within a valid legislative waiver of the City's and the MUDs' sovereign immunity from suit under the Texas Torts Claims Act.⁶⁰

The Houston First Court of Appeals quickly agreed with the City and the MUDs because the Texas Tort Claims Act—which does provide “a limited waiver of immunity for certain tort claims against governmental entities and caps recoverable damages”—does not waive immunity for intentional torts.⁶¹ Tortious interference, of course, is an intentional tort.⁶²

C. HOW LONG MAY THIS ACTIVITY GO ON?

“Equity aids the vigilant,” and the equitable defense of laches may arise if a plaintiff waits too long before seeking a temporary injunction. This was among the issues raised in *Frequent Flyer Depot, Inc. v. American Airlines, Inc.*⁶³

Frequent Flyer was a broker of airline frequent flyer miles and awards, including the AAdvantage™ rewards points issued by American Airlines. American objected to this practice and brought claims “for tortious interference with contract, tortious interference with prospective relations, misappropriation, and fraud,” as well as a breach-of-contract claim against one of Frequent Flyer's principals.⁶⁴ The trial court granted “a temporary injunction prohibiting [Frequent Flyer] from buying, selling, bartering, or soliciting AAdvantage™ rewards [pending trial].”⁶⁵

One issue on appeal was whether the injunction was really preserving the status quo, or instead was changing it. The defendants claimed to have been in business since 2002, and claimed that American had known what they were doing since then, in fact an American Airlines attorney had called the defendants' principal “several times” in 2002 about domain names connected to frequentflyerdepot.com, contending the domain names constituted a trademark infringement. Also, “[s]ince 2005, American ha[d] stopped travel on tickets [brokered through] Frequent Flyer by freezing the accounts of AAdvantage™ members” who sold their miles to third parties.⁶⁶ Frequent Flyer urged that by 2008, the “last peaceable uncontested status” would be for them to carry on in their business.⁶⁷

59. *Id.* at *1-2.

60. *Id.* at *10.

61. *Id.* (citing TEX. CIV. PRAC. & REM. CODE ANN. §§ 101.023, 101.057(2) (Vernon 2005)).

62. *Id.* (citing *Holloway v. Skinner*, 898 S.W.2d 793, 795-96 (Tex. 1995)).

63. 281 S.W.3d 215, 229 (Tex. App.—Fort Worth 2009, pet. denied).

64. *Id.* at 220.

65. *Id.*

66. *Id.* at 222.

67. *Id.* at 223.

American obviously disagreed, contending there was no evidence American knew of Frequent Flyer's brokering activities in 2002 when it contacted Frequent Flyer about the latter's 136 domain names, and no evidence that it knew in 2005 and later that the accounts it was freezing were sold through Frequent Flyer in particular. Further, it claimed it could not have known the full extent of what Frequent Flyer was doing, because Frequent Flyer admitted its transactions were "caught" "only between three to ten percent of the time."⁶⁸ Frequent Flyer's principals testified that it instructed its customers to tell American that the points were a "gift" and that "such representations [were] lies."⁶⁹

In the view of the Fort Worth Court of Appeals, the "last peaceable, noncontested status" would be for Frequent Flyer to stop selling AAdvantageTM rewards points "[i]f, as American claims, appellants' activities are in violation of its agreement with AAdvantageTM members."⁷⁰ Since there was no challenge on appeal as to whether American had "proved a probable right to recover on its causes of action,"⁷¹ this appeared to be the case. But the court of appeals went on to note that American had moved for a temporary injunction "when it learned the full extent of Frequent Flyer's activities" which Frequent Flyer was continuing despite American's objections.⁷² The fact that Frequent Flyer was affirmatively concealing its activity appears to have been very significant, as the court of appeals wrote that "American should not be denied [an injunction] to which it is otherwise entitled simply because it took some time for it to discover Frequent Flyer's admittedly concealed activity."⁷³

The court of appeals did not specifically address many of the elements of the causes of action involved, or why "between three to ten percent" of the defendant's activity—which was being captured, apparently over a period of years, and of which some (though not all) may have been known or readily knowable to have come through Frequent Flyer—was not itself sufficient to trigger an equitable obligation upon American to move against the defendants more promptly.⁷⁴ It may be, however, that where the defendants have been admittedly concealing their activities, and instructing their customers to misrepresent the facts to American, the defendants themselves were simply estopped to make that claim, though that was not expressly stated in the opinion.⁷⁵

68. *Id.* at 222-23.

69. *Id.* at 223 n.3.

70. *Id.* at 223.

71. *Id.* at 223 n.2.

72. *Id.* at 223.

73. *Id.*

74. *See id.*

75. *See id.* at 223 n.3.

IV. NON-COMPETE AGREEMENTS

A. WILL UNCLEAN HANDS BAR ENFORCEABILITY?

The relationship between noncompetition agreements and unclean hands was raised, but ducked, in *Central Texas Orthopedic Products, Inc. v. Espinoza*.⁷⁶ Espinoza had served Central Texas Orthopedics as a sales rep for four years when he resigned to take a sales job with its competitor, Stryker Orthopedics.⁷⁷ Central Texas promptly sued to enforce Espinoza's one-year post-termination noncompetition covenant, and claimed breach of a compensation agreement (for not returning \$485 that Espinoza owed) and breach of fiduciary duty, as well as tortious interference by Stryker. Espinoza counterclaimed for \$12,000 he claimed to be owed in commissions and particularly claimed that Central Texas's withholding of these commissions constituted "unclean hands," precluding equitable enforcement of the noncompetition covenant.⁷⁸

The Covenants Not to Compete Act⁷⁹ does not specifically address the clean hands doctrine, but it does provide that "[t]he criteria for enforceability [of a noncompetition covenant] and the procedures and remedies in an action to enforce [one] are exclusive and preempt any other criteria for enforceability . . . or procedures and remedies . . . under common law or otherwise."⁸⁰ Central Texas argued that as a common law principle, the clean hands doctrine is expressly preempted by the Act.⁸¹ Espinoza disagreed, urging that the clean hands doctrine is an equitable principle, and that the preemptive provision in the Act would not apply.⁸²

The San Antonio Court of Appeals recognized but sidestepped the question, holding that it needed not decide whether the statute preempts the unclean hands doctrine, because the action Espinoza claimed constituted unclean hands was not sufficient in any event.⁸³ The court of appeals held that the unclean hands doctrine would not apply unless "the misconduct at issue is connected to the subject of the litigation and the party asserting the defense has been seriously harmed by the misconduct."⁸⁴ The court of appeals held that the doctrine did not apply in this case because the alleged bad acts—failure to pay the commissions due—did not arise from any obligations in the non-compete agreement, but rather from a compensation agreement, which was different.⁸⁵ These obligations were separate, and the court of appeals held that "the doctrine of unclean hands does not apply when a party is guilty of inequitable

76. No. 04-09-00148-CV, 2009 WL 4670446 (Tex. App.—San Antonio Dec. 9, 2009, pet. filed); *see also infra* Part V.A.

77. *Id.* at *1.

78. *Id.* at *1-2.

79. TEX. BUS. COM. CODE ANN. § 15.52 (Vernon 2002).

80. *Id.*

81. *Espinoza*, 2009 WL 4670446, at *2.

82. *Id.* at *3.

83. *Id.*

84. *Id.*

85. *Id.*

conduct with regard to a transaction *separate* from the one in dispute.”⁸⁶ Since Espinoza did not establish that his former employer had acted with unclean hands, the trial court’s summary judgment in Espinoza’s favor on that point was reversed.⁸⁷

Determination of whether the equitable doctrine of unclean hands is really preempted by section 15.52 of the Covenants Not to Compete Act must await a case which presents unclean hands arising out of those obligations directly.

B. STOCK OPTIONS AND “GIVING RISE” TO THE NEED FOR A COVENANT

It is well known that to be enforceable, covenants not to compete must be “ancillary to or part of an otherwise enforceable agreement at the time the agreement is made” and contain reasonable limitations that “do not impose a greater restraint than is necessary to protect the goodwill or other business interest of the promisee.”⁸⁸ It is also understood that to be “ancillary to or part of an otherwise enforceable agreement,” the “consideration given by the employer in the otherwise enforceable agreement must give rise to the employer’s interest in restraining the employee from competing[, and] the covenant must be designed to enforce the employee’s consideration or return promise in the otherwise enforceable agreement.”⁸⁹

“Giving rise” to an employer’s interest in a noncompetition covenant was the subject of *Marsh USA, Inc. v. Cook*.⁹⁰ Here, defendant Cook was a managing director for Marsh and had worked for the company since 1983. He was included in the 1992 Employee Incentive and Stock Award Plan and was granted stock options in 1996. Before exercising them, however, he had to sign a non-solicitation agreement which contained a covenant not to compete. Cook signed the agreement in 2005 and exercised the stock options, but he left Marsh in 2007 and went to work for one of its competitors. When Marsh sued to enforce the noncompetition covenant, Cook claimed it was unenforceable because it was signed in return for stock options, and stock options in and of themselves did not “give rise” to the need for a noncompetition covenant from him.⁹¹

Marsh urged that “offering a stock option to a valuable employee” like Cook “gives rise to its interest in protecting its goodwill.”⁹² The Dallas Court of Appeals disagreed, however, noting that Marsh “was trying to protect its goodwill by *offering* the stock options to certain valued em-

86. *Id.*

87. *Id.* at *4.

88. TEX. BUS. & COM. CODE ANN. § 15.50(a) (Vernon Supp. 2009).

89. Alex Sheshunoff Mgmt. Servs., L.P. v. Johnson, 209 S.W.3d 644, 648-49 (Tex. 2006).

90. 287 S.W.3d 378 (Tex. App.—Dallas 2009, pet. granted).

91. *Id.* at 378-80.

92. *Id.* at 380.

ployees, including Cook,”⁹³ but that it did not follow that such a stock plan incentive “gives rise to an employer’s interest in restraining the employee from competing.”⁹⁴ Instead, relying on *Olander v. Compass Bank*,⁹⁵ the court of appeals held that “[t]he give rise requirement may be met only if the consideration given by the company creates the interest in restraining competition” and that this would occur only if that interest did not exist before the consideration was extended.⁹⁶ Since Marsh’s interest in Cook’s not competing did not arise or change when it awarded the stock to Cook, the award did not “give rise” to the need or interest in the noncompetition agreement, and consequently the noncompetition agreement could not be enforced.⁹⁷

Note that, as the court of appeals observed, the Texas test for consideration to be provided by the employer is “significantly [more] burdensome” than the test in some other states.⁹⁸ For example, in Indiana, the test would be “whether the covenant and contract have a significant nexus to the ‘employment situation,’” even though these rights “do not arise from the contract to which the covenant is attached.”⁹⁹ Texas requires exactly that.¹⁰⁰

C. TRADEMARKS DO NOT RESTRICT COMPETITION

In *RE/MAX International Inc. v. TrendSetter Realty, LLC*,¹⁰¹ the main issue involved a trademark infringement claim by RE/MAX against a real estate brokerage whose trademarked logo involved a rectangular design with red, white, and blue horizontal stripes. The defendant was ordered to cancel its use of the logo because it stood to be confused with the trademarked logo of RE/MAX.¹⁰²

The brokerage agreement contained a post-termination provision that prevented the brokerage from using RE/MAX’s trademarks, among other things. The defendant argued that the provision amounted to a noncompetition covenant and that it was unreasonable in scope, duration, and geographical reach and thus unenforceable.¹⁰³ In assessing whether the post-termination provision of the contract constituted a “non-compete” covenant, the district court recognized the Fifth Circuit’s holding in *Guy Carpenter & Co., Inc. v. Provenzale*¹⁰⁴ that “a provision need not

93. *Id.*

94. *Id.* at 380-81.

95. 172 F. Supp. 2d 846 (S.D. Tex. 2001), *aff’d*, 44 F. App’x 651 (5th Cir. 2002).

96. *Marsh USA*, 287 S.W.3d at 381.

97. *Id.*

98. *Id.* at 380.

99. *Id.* (emphasis omitted) (quoting *Field v. Alexander & Alexander of Ind., Inc.*, 503 N.E.2d 627, 632 (Ind. Ct. App. 1987)).

100. *Id.* at 380.

101. 655 F. Supp. 2d 679 (S.D. Tex. 2009).

102. *Id.* at 711.

103. *Id.* at 718.

104. 334 F.3d 459 (5th Cir. 2003).

'expressly prohibit' competition to come within its reach."¹⁰⁵ Quoting the Fifth Circuit, the district court stated, "It is enough that the 'practical and economic reality of such a provision is that it inhibits competition virtually the same as a covenant not to compete.'"¹⁰⁶ The district court went on to point out, however, that "Texas law does not treat nondisclosure agreements as covenants not to compete."¹⁰⁷ "A nondisclosure agreement does not prevent [the] former employee from competing," only from using trade secrets or confidential information to compete.¹⁰⁸

Addressing the provision at issue in the RE/MAX contract, the district court said it was "largely a nondisclosure agreement . . . preventing former agents from disclosing or using . . . trademarks, confidential information, or trade secrets, which RE/MAX [was] entitled to protect."¹⁰⁹ The provision prohibiting the former broker from competing using a red, white, and blue sign that could be confusingly similar to RE/MAX marks did not amount to a restriction on competition, because the trademark "is not essential to succeeding in the real estate business."¹¹⁰

D. ARE NONSOLICITATION COVENANTS GOVERNED AS NON-COMPETES?

The question occasionally arises as to whether a "nonsolicitation" covenant is governed by the Covenants Not to Compete Act.¹¹¹ *York v. Hair Club for Men, L.L.C.*¹¹² confirms that they are.

In *York*, two employees of Hair Club for Men (Hair Club) departed its Houston office to open their own hair-replacement salon a mile away, evidently violating their two-year, ten-mile radius (in one agreement, twenty-mile-radius) noncompetition agreement and a nonsolicitation agreement providing that they would not, during that time, solicit from or provide any hair-replacement services to Hair Club customers.¹¹³ The trial court found they also violated a nondisclosure agreement by using the customer information to target and attract forty-one of their former Hair Club customers.¹¹⁴ The trial court granted a temporary injunction, though their nonsolicitation agreement to apply only to customers who had been treated by the local Hair Club in the two years prior to the employees' departure.¹¹⁵

Relying on the new *Mann Frankfort Stein & Lipp Advisors, Inc. v.*

105. *RE/MAX*, 655 F. Supp. 2d at 718.

106. *Id.* at 718-19.

107. *Id.* at 719.

108. *Id.*

109. *Id.*

110. *Id.*

111. TEX. BUS. & COM. CODE ANN. §§ 15.50-.52 (Vernon 2002 & Supp. 2009).

112. No. 01-09-00024-CV, 2009 WL 1840813 (Tex. App.—Houston [1st Dist.] June 25, 2009, no pet.) (mem. op.).

113. *Id.* at *1-2.

114. *Id.* at *2.

115. *Id.* at *3.

*Fielding*¹¹⁶ decision, the Houston First Court of Appeals found that Hair Club did provide the employees with confidential information on its hard-won clients, that this gave rise to Hair Club's interest in keeping that information confidential, and that the covenants were designed to enforce that interest.¹¹⁷ Accordingly, it held both the noncompetition and the nonsolicitation covenants to be enforceable.¹¹⁸ Whether the employees used the "lists" of customers or not, they clearly invited their former Hair Club customers to visit them at the new location, and the court of appeals held that this violated the nonsolicitation covenant in any event.¹¹⁹

The defendants also challenged the trial court's balance of the equities, urging that the Hair Club could have an adequate remedy at law and that the harm the defendants would face from these restrictions would far outweigh any probable injury to Hair Club. The court of appeals observed that the employees were licensed cosmetologists and could find work in cosmetology other than hair replacement.¹²⁰ They could also continue to operate their salon and find new hair-replacement clients other than those they had served at Hair Club.¹²¹ The trial court's order was affirmed.¹²²

Not addressed in this opinion was how the customers themselves might feel about it. Hair-replacement services seem to be quite personal in nature, lasting (according to the opinion) some period of years.¹²³ Might not the goodwill being built up over that time be shared somehow, developing in a seamless whole, among both the Hair Club institution whose reputation and advertising had first attracted the customer, and also the individual cosmetologist who is personally attending to the customer's needs? Might it be the Hair Club institution which draws the customer in for the first visit, but the individual cosmetologist who draws him back for the second?

E. NON-COMPETE AGREEMENTS AND THE GLOBAL ECONOMY

In *Information Services Group, Inc. v. Rawlinson*,¹²⁴ the former employer of Rawlinson, an English citizen and resident, brought suit against him in Houston for purported breach of several restrictive post-termination covenants, including a covenant not to compete. When Rawlinson objected on jurisdictional grounds, the former employer argued that Rawlinson's execution of employment agreements with a Texas limited liability company (including restrictive covenants governed by Texas law),

116. 289 S.W.3d 844 (Tex. 2009); *see infra* Part IV.F.

117. *York*, 2009 WL 1840813, at *4-5.

118. *Id.* at *5.

119. *Id.*

120. *Id.* at *5-6.

121. *Id.* at *6.

122. *Id.*

123. *See id.* at *1.

124. 302 S.W.3d 392 (Tex. App.—Houston [14th Dist.] 2009, pet. denied).

access to job-related confidential information routed through servers located in Texas, and two business trips to Texas for his job, amounted to minimum contacts.¹²⁵ The Houston Fourteenth Court of Appeals applied the customary jurisdictional analysis in concluding that these did not present sufficient minimum contacts,¹²⁶ but there was a particular twist with respect to the noncompetition covenant.

In the former employer's view, Rawlinson was contractually prohibited from competing against it anywhere in the world, including Texas; the covenants thus "require[d] performance in Texas and so personal jurisdiction is proper here."¹²⁷ The court of appeals emphatically disagreed:

[W]e decline to adopt a position that an employee, by agreeing to a non-compete or non-solicitation agreement, is effectively consenting to jurisdiction as far-reaching as the scope of the agreement, which in this case is worldwide. It cannot be enough that Rawlinson simply agreed not to compete or solicit clients in Texas.¹²⁸

Of considerable interest in this age where employees can work online from anywhere—though unnecessary to the decision, since the action was being dismissed for lack of personal jurisdiction—is whether a "worldwide" restriction would have met the Covenant Not to Compete Act's requirement that restrictions be reasonable as to geographic scope.¹²⁹

F. IMPLIED PROMISES AND "FORCED SALE" PROVISIONS

The roller-coaster ride that is the Texas law of noncompetition covenants took another swerve in *Mann Frankfort Stein & Lipp Advisors, Inc. v. Fielding*.¹³⁰ In 2006 the Texas Supreme Court concluded in *Alex Sheshunoff Management Services, L.P. v. Johnson*¹³¹ that the statutory phrase "at the time the agreement is made" should not be read to require an instantaneous delivery of trade secrets, but instead would permit trade secrets to be delivered (and accepted by the promisor/employee) gradually over time. Still, how clearly and definitively an employer must promise to deliver trade secrets (or other confidential information, or other value which would give rise to the need for a noncompetition covenant) remained something of an open issue. In the normal course of business, many employers would not know exactly what information they would want to entrust to new employees, or how much, or how quickly. Much would depend on events and how the employment relationship worked out. Might an employer hedge its bets, requiring a new hire to hold the employer's information in confidence and restrict her competition *if* (and presumably "to the extent that") the employer came to trust her enough,

125. *Id.* at 399-400.

126. *Id.* at 405.

127. *Id.* at 407.

128. *Id.*

129. *See* TEX. BUS. & COM. CODE ANN. § 15.50(a) (Vernon 2009).

130. 289 S.W.3d 844 (Tex. 2009).

131. 209 S.W.3d 644 (Tex. 2006).

over time, to divulge them? Suppose the employer never *expressly* promised to divulge them at all?

That was the situation in *Mann Frankfort*.¹³² Mann Frankfort was a tax, accounting, and consulting firm. Fielding was a new hire, an accountant, and a tax professional. When he joined, he signed Mann Frankfort's standard restrictive covenants, which required him not to compete with Mann Frankfort after his departure, ostensibly in order to protect its proprietary information. But the agreement did not expressly require Mann Frankfort to deliver any proprietary information to Fielding at all.¹³³

The agreement might not have said that in so many words, but the supreme court concluded that the facts did.¹³⁴ Fielding was hired to work as a staff accountant in the firm's tax department. In order to do his job, he would necessarily have to be given access to client files, client accounting information, and other confidential and proprietary information of the firm. Without them he could not work, or at least could not do the work he was obviously hired to do. Accordingly, the supreme court held that an *implied* promise by the firm (to provide such confidential materials) *did* exist, and that this was sufficient consideration to make the non-competition covenant enforceable.¹³⁵ The supreme court realized that Mann Frankfort's implied promise to give Fielding confidential information was "illusory" when it was made, because Mann Frankfort could have fired him immediately before giving him any confidential information.¹³⁶ However, Mann Frankfort did not fire Fielding first. The supreme court concluded that Mann Frankfort "performed its illusory promise by actually providing confidential information."¹³⁷

One other aspect of *Mann Frankfort* which was particularly significant. It concerned a client purchase provision. The restrictive covenants required Fielding not to compete, but added a "what if" provision in case he did. If, within one year after leaving employment, Fielding "directly or indirectly" performed accounting services for anyone who had been a client of Mann Frankfort while he worked there, Fielding would immediately buy from Mann Frankfort (and Mann Frankfort would immediately sell to Fielding) "that portion of [Mann Frankfort's] business associated with [that client]" under terms set out in the agreement.¹³⁸ Without much discussion, the supreme court held that this "client purchase provision was designed to hinder Fielding's ability to use the confidential information to compete against Mann Frankfort," and was therefore "ancillary to or part of" the otherwise enforceable agreement" at the

132. 289 S.W.3d at 846.

133. *Id.*

134. *See id.* at 852.

135. *Id.*

136. *Id.* at 851-52.

137. *Id.* at 852 (citing *Sheshunoff*, 209 S.W.3d at 651). "[A] unilateral contract formed when the employer performs a promise that was illusory when made can satisfy the requirements of the [Covenants Not to Compete] Act." *Sheshunoff*, 209 S.W.3d at 651.

138. *Mann Frankfort*, 289 S.W.3d at 846.

time the agreement was made, and thus fully enforceable.¹³⁹

One might wonder, though, what such a contractual requirement might mean to a court being asked to enjoin preliminarily the competitive use of information whose price had thus been liquidated and was indeed required to be sold to the departing employee. Ordinarily, temporary injunctive relief is available only where there is no adequate remedy at law¹⁴⁰—meaning, typically, that an award of money damages would be difficult to calculate or otherwise inadequate to prevent irreparable harm. Might such provisions be read as calculating a remedy at law rather precisely already?

V. BREACH OF FIDUCIARY DUTY

A. MIGHT FEES BE FORFEITED? OR MUST THEY BE?

The “departing employee” case of *Central Texas Orthopedic Products, Inc. v. Espinoza*¹⁴¹ also raised an issue as to whether a departing employee might forfeit commissions due but unpaid at the time he left. Former employee Espinoza claimed to be owed over \$12,000 in unpaid commissions, but his former employer claimed Espinoza had breached his fiduciary duty by disclosing confidential information to a competitor regarding how much product he was selling, who his customers were, and the fact that his customers preferred using a certain type of product which the plaintiff offered but which was not currently offered by the competitor. His former employer also claimed Espinoza tried to convince another employee to leave with him as well.¹⁴² These breaches of fiduciary duty, the former employer claimed, were sufficient to require Espinoza to forfeit any remaining claims for compensation.

The San Antonio Court of Appeals held that “[f]ee forfeiture is appropriate in cases where an employee breaches his fiduciary duty to his employer,”¹⁴³ whether or not the breach of fiduciary duty causes any damages.¹⁴⁴ But the court of appeals stopped short of concluding that the evidence showed Espinoza breached his fiduciary duty as a matter of law, or even that a breach of fiduciary duty would, necessarily, forfeit that party’s right to earned compensation. Instead, the court of appeals held that “[b]ecause a party’s breach of fiduciary duty *may* forfeit that party’s right to earned compensation,” the plaintiff had “raised a genuine issue of material fact with regard to whether Espinoza breached his fiduciary duty, and therefore whether [he was] entitled to compensation.”¹⁴⁵ The

139. *Id.* at 852.

140. *See* *Brown v. Gulf Television Co.*, 157 Tex. 607, 611, 306 S.W.2d 706, 709 (1957).

141. No. 04-09-00148-CV, 2009 WL 4670446 (Tex. App.—San Antonio Dec. 9, 2009, pet. filed) (mem. op); *see also supra* Part IV.A.

142. *Id.* at *5.

143. *Id.* (citing *Burrow v. Arce*, 997 S.W.2d 229, 239 (Tex. 1999)).

144. *Id.* (citing *Kinzbach Tool Co. v. Corbett-Wallace Corp.*, 138 Tex. 565, 572, 160 S.W.2d 509, 513 (1942)).

145. *Id.* at *6 (emphasis added).

case was remanded.¹⁴⁶

VI. TRADE SECRETS AND CONFIDENTIAL INFORMATION

A. CRAFTING THE INJUNCTION

A common, vexing problem is how to write an enforceable temporary restraining order or temporary injunction involving lists of customers, secret techniques, or other materials which are confidential. To reveal these materials by attaching them to orders would expose them to public view and thus defeat, in many cases, the very point of the orders. Yet defendants must be given clear and adequate notice of what they are enjoined from doing, and for orders granting injunctions to be enforceable, Texas Rule of Civil Procedure 683 provides that they “shall be specific in terms” and “shall describe in reasonable detail and not by reference to the complaint or other document, the act or acts sought to be restrained.”¹⁴⁷

This provision was applied in *Vaughn v. Intrepid Directional Drilling Specialists, Ltd.*¹⁴⁸ Vaughn had been an Intrepid salesman for nine months when he left and formed his own company. Later he sold his company back to Intrepid for millions of dollars and a three-year employment contract containing a noncompetition covenant. The covenant provided that he would not engage in directional drilling within a five-state area for four years or solicit directly or indirectly any customers of Intrepid in that area during that time.¹⁴⁹ Vaughn left Intrepid not long afterwards, however, and Intrepid filed an action against him, his new company, and another former employee with a similar agreement. After a two-day hearing, the trial court entered a temporary injunction.¹⁵⁰

One of the defendants’ principal issues on appeal was whether the temporary injunction complied with Rule 683 in being “specific in terms.”¹⁵¹ The order did not identify any of Intrepid’s customers within the five-state area (except for Chesapeake Gas), or all of its employees for that matter, but rather restrained the defendants from interfering with Intrepid’s customers and business relationships with its customers that were located within the five-state territory.¹⁵²

Significantly, however, Vaughn’s testimony demonstrated that he knew “or could easily determine the identity of the other customers.”¹⁵³ “Under these circumstances,” held the Eastland Court of Appeals, “the trial court’s order sufficiently identified Intrepid’s customers for the pur-

146. *Id.*

147. TEX. R. CIV. P. 683.

148. 288 S.W.3d 931 (Tex. App.—Eastland 2009, no pet.).

149. *Id.* at 933.

150. *Id.* at 934.

151. *Id.* at 938 (quoting TEX. R. CIV. P. 683).

152. *Id.* at 938-39.

153. *Id.* at 939.

poses of Rule 683.”¹⁵⁴

Here, the court of appeals concluded that Vaughn’s knowledge of his former employer’s customer base would allow him to avoid violating the temporary injunction, and hence the order complied with Rule 683.¹⁵⁵ One wonders whether the result might have been different if specific and detailed processes had been at issue in the case, or if the information and materials sought to be protected had been lengthy and detailed.

B. PLEADINGS, SUMMARY JUDGMENT, AND “USE”

The United States Court of Appeals for the Fifth Circuit vacated summary judgment in the Texas trade secret case of *Cudd Pressure Control Inc. v. Roles*, because summary judgment had been granted on grounds that were not pled or argued by the defendants.¹⁵⁶ Cudd Pressure Control Inc. (Cudd) is an oilfield services company. Ronnie Roles, Steve Winters, and four others worked for it until they were enticed by juicy bonuses to join a newly formed, competing business, Great White Pressure Control LLC (Great White). Cudd became “concerned” about its ex-employees’ mass exodus to a new competitor, so it undertook an investigation of their pre-departure conduct. Upon discovering security footage showing Winters loading boxes of materials onto his truck the night before he quit, and an email from Roles to Great White two months before he quit asking for a laptop to transfer information, Cudd filed suit, alleging violations of RICO, conspiracy, breach of fiduciary duty, misappropriation of trade secrets, and common-law unfair competition.¹⁵⁷

The RICO claims were dropped early on, and the case centered on Cudd’s trade secrets misappropriation claims, “focus[ing] on two separate alleged uses of confidential information: (1) [Roles’s] creation of the Great White business plan using Cudd financial data, and (2) design of a mini-snubbing unit that Great White purchased from a [third party], but which was designed, in part,” by Winters while he was at Cudd.¹⁵⁸ The defendants moved for summary judgment on the sole grounds that (1) they did not use the information they took from Cudd, and (2) Cudd had no cognizable damages.¹⁵⁹ The motion did not discuss whether that information constituted trade secrets in the first place. Nonetheless, the district court granted summary judgment for the defendants—former employees on the unpled ground that the disputed information did not

154. *Id.* (citing *Amalgamated Acme Affiliates, Inc. v. Minton*, 33 S.W.3d 387, 397-98 (Tex. App.—Austin 2000, no pet.) (defendant had admitted it could identify the customers and advertisers that were the subject of the order); *Safeguard Bus. Sys., Inc. v. Schaffer*, 822 S.W.2d 640, 644 (Tex. App.—Dallas 1991, no writ) (“Orders generally restraining solicitation of customers and not specifically listing the individual customers have not been found to be overbroad.”)).

155. *Id.*

156. 328 F. App’x 961, 965 (5th Cir. 2009).

157. *Id.* at 962.

158. *Id.*

159. *Id.* at 965.

constitute trade secrets at all.¹⁶⁰

The Fifth Circuit reversed the summary judgment, holding as a procedural matter that the district court could not grant summary judgment *sua sponte* on a ground not requested by the moving party.¹⁶¹ It then examined whether summary judgment was proper on the grounds advanced by the former employees and concluded that it was not.¹⁶² Viewing the evidence in the light most favorable to the non-movant, the Fifth Circuit was prepared to assume Cudd's information constituted trade secrets. Summary judgment could not be sustained on the ground that the former employees did not "use" the information, because evidence indicated that they did "use" the information to lure investors and to build a business plan.¹⁶³ By "use," the Fifth Circuit meant "commercial use," and it recited its previously derived definitions as "whenever 'a person seeks to profit from the use of the secret'"¹⁶⁴ and "[a]ny misappropriation . . . followed by an exercise of control and domination."¹⁶⁵ The evidence showed at least a fact issue as to whether the defendants' use met that definition.¹⁶⁶

Summary judgment based on Cudd's failure to show damages was also improper, because Cudd had not had sufficient opportunity to gather evidence on that point.¹⁶⁷ Thus, the Fifth Circuit vacated the summary judgment award and remanded the case.¹⁶⁸

C. ONE BITE, NOT TWO

Weddings are big business all over the U.S., but in Texas, where "everything is bigger," the bridal industry wars rival the Great War. This was the case in *Bridal Expo, Inc. v. Van Florestein*.¹⁶⁹

Bridal Expo is a powerhouse in the industry. For twenty-five years it has hosted the Bridal Extravaganza Show, one of the largest bridal shows in the country. The show is attended by hundreds of exhibitors and thousands of prospective brides who travel from all over Texas to peruse gowns, floral arrangements, photography, music, catering, and a myriad of other bridal services, so after twenty-five years, Bridal Expo has acquired an extensive database of vendors, attendees, and potential clients.¹⁷⁰

160. *Id.*

161. *Id.*

162. *Id.* at 965-66.

163. *Id.*

164. *Id.* at 965 (quoting *Gen. Universal Sys., Inc. v. HAL, Inc.*, 500 F.3d 444, 450 (5th Cir. 2007)).

165. *Id.* at 965-66 (quoting *Carbo Ceramics v. Keefe*, 166 F. App'x 714, 721 (5th Cir. 2006)).

166. *Id.* at 966.

167. *Id.*

168. *Id.* at 967.

169. No. 4:08-cv-03777, 2009 WL 255862 (S.D. Tex. Feb. 3, 2009); *see also infra* Parts VII.A, VIII.

170. *Id.* at *1.

Defendants Sonja van Florestein and Tiffany Moore left their employ at Bridal Expo in July 2008, but not before Moore downloaded Bridal Expo's databases and other information. A few months later, van Florestein and Moore surfaced, now working for the newly formed company Wedding Showcase, which scheduled its first "Houston Wedding Showcase" event for February 2009, a few weeks after the Bridal Extravaganza at the same location.¹⁷¹ They admitted they used the information they downloaded from Bridal Expo's database to mail ads to vendors for their new company's seminar, held in November 2008. They also used Google to advertise their Wedding Showcase as "Houston's #1 Bridal Show" and mailed a brochure to vendors using "quotations, attributed to 'our' vendors and 'our' brides, that [actually] originated from vendors and brides at other bridal shows on the East Coast, produced by another company."¹⁷²

In a state court suit, Bridal Expo brought claims for trade secret misappropriation, unfair competition, and related business torts. The trial court denied its request for a temporary restraining order, however, and also denied its application for a temporary injunction after a hearing. Bridal Expo decided to cut its losses and nonsuited the state case.¹⁷³ It turned around and sued in federal court, asserting the same common-law claims and requesting the same relief, but adding federal causes of action, such as a Lanham Act Section 43(a) false advertising claim and a Computer Fraud and Abuse Act claim.¹⁷⁴

On the state claims, the federal district court held that all the elements of collateral estoppel were present, and it refused to disturb the state court's ruling on the temporary injunction.¹⁷⁵ The district court found no reason to revisit the state court's decision because only a month had passed since the state court's denial of preliminary relief, and furthermore, Bridal Expo's February 2009 Bridal Extravaganza, held in the interim, had been successful, thus suggesting a lack of tangible harm to Bridal Expo.¹⁷⁶ What appeared not to be addressed was whether intangible harm was occurring to Bridal Expo's marks and goodwill, or whether, regardless of harm to Bridal Expo, the defendants were being unjustly enriched by their acts.

Also not reported was why the state courts denied Bridal Expo's applications for interim relief. A hint appears in the federal opinion's discussion of the Computer Fraud and Abuse Act claims noting that the defendants had not signed confidentiality or other restrictive agreements while in the employ of Bridal Expo.¹⁷⁷

171. *Id.*

172. *Id.* at *2.

173. *Id.*

174. *Id.*

175. *Id.* at *3.

176. *Id.* at *5.

177. *Id.* at *11.

D. NOT EVERY “STRATEGY” IS A TRADE SECRET

Not every “strategy” is a trade secret, as the Fifth Circuit explained in *CQ, Inc. v. TXU Mining Co., L.P.*¹⁷⁸ TXU mines lignite (low-grade coal) for commercial fuel. In 2004, TXU sent a request for bids to CQ and several other companies that specialized in cleaning lignite to participate through a “Key Alliance Agreement” in building and operating lignite-cleaning facilities at two of TXU’s lignite mines for five years. TXU required bidders to sign a “Confidentiality Agreement,” preventing either party from using confidential information disclosed during negotiations for any purpose, “except the analysis, investigation, and evaluation of the proposed business relationship.”¹⁷⁹

In early 2005, TXU notified CQ that it had been selected as a contractor. The parties had different understandings, however, of the significance of the selection. CQ understood that TXU agreed at that point to the five-year Alliance Agreement discussed in the bid documents, but TXU contended that it merely selected CQ to continue further negotiations. The parties never came to terms or reduced their agreement to writing, but CQ did spend the next few months advising TXU on the proposed lignite-cleaning operation. When CQ inquired about reducing the arrangement to writing, TXU responded that it had not made a final decision, but that it would compensate CQ even if it ultimately did not go forward with the project. TXU ultimately decided against the project, and in July 2005, TXU terminated its relationship with CQ. TXU later built and operated its own lignite-cleaning facility.¹⁸⁰

CQ sued TXU for breach of the five-year Alliance Agreement, breach of the Confidentiality Agreement, quantum meruit, and misappropriation of trade secrets for using CQ’s “ROM” strategy to clean lignite. On cross-motions for summary judgment, the district court found that questions of material fact precluded summary judgment for CQ, but it granted summary judgment for TXU on breach of the purported Alliance Agreement under the statute of frauds, and on most of the trade secret claims, on the grounds that CQ failed to provide any evidence that TXU used CQ’s confidential information.¹⁸¹ Prior to trial, the district court excluded the report and opinions of CQ’s damages expert. The parties then entered into a settlement agreement whereby TXU paid CQ’s legal fees, and CQ withdrew its claims for promissory estoppel and injunctive relief. TXU then moved for a “take-nothing” judgment on CQ’s remaining claims.¹⁸²

CQ raised several challenges on appeal, but the Fifth Circuit affirmed the district court’s judgment and interim rulings, including the exclusion

178. 565 F.3d 268 (5th Cir. 2009).

179. *Id.* at 271.

180. *Id.* at 271-72.

181. *Id.* at 272.

182. *Id.*

of reports by CQ's damages expert.¹⁸³ The Fifth Circuit found CQ's expert report on lost profits for misappropriation properly excluded as irrelevant and untimely; following the initial release of the report, the district court dismissed CQ's contract and trade secret claims that "provided the substantial basis for the report."¹⁸⁴ The Fifth Circuit also held that the district court had properly excluded the expert's supplemental report based on recovery of a hypothetical royalty under a hypothetical licensing agreement, as prohibited by Texas law.¹⁸⁵

The Fifth Circuit also upheld the district court's dismissal of CQ's trade secret claims.¹⁸⁶ In addition to the lack of evidence that TXU had used such information, the Fifth Circuit analyzed whether the "ROM" strategy constituted a trade secret at all. The "ROM" strategy was CQ's recommendation that TXU focus on cleaning lignite at the mine. There were no allegations that the strategy involved any "previously unknown process or method for cleaning lignite."¹⁸⁷ To the contrary, the evidence suggested that TXU had already contemplated cleaning the lignite when it sent its original request for bids. The "strategy" was just a recommendation between two generally known alternatives of how to do it. The Fifth Circuit reasoned that "[w]hile [the] recommendation may have been based on CQ's valuable experience and effort, it was not a 'process or device for continuous use' that offered TXU an advantage over its competitors," and consequently did not meet the definition of a trade secret.¹⁸⁸

E. TRADE SECRETS AND THE AGING PROCESS

Many nondisclosure agreements are open-ended in their terms, requiring the obligees not to use or disclose the information "at any time"; but many others are expressly limited in time and expire by their own terms in two, five, ten, or some other term of years. Trade secrets and confidential information can be protected only so long as their owners take reasonable precautions to protect their confidentiality. What happens when nondisclosure agreements expire?

This question was addressed and at least partly answered in *INEOS Group Ltd. v. Chevron Phillips Chemical Co.*¹⁸⁹ Here, Chevron Phillips Chemical (CPChem) obtained a temporary injunction prohibiting INEOS from soliciting, negotiating, or licensing high-density polyethylene made by using the "loop slurry" process which CPChem claimed was derived from its trade secrets. The principal issue on appeal was whether this technology was still entitled to trade secret protection or whether

183. *Id.* at 277, 280.

184. *Id.* at 277.

185. *Id.* at 278.

186. *Id.* at 274.

187. *Id.*

188. *Id.* at 274-75.

189. No. 01-09-00504-CV, 2009 WL 4854349 (Tex. App.—Houston [1st Dist.] Dec. 17, 2009, no pet.).

CPChem had errantly disclosed it to third parties who were no longer bound to hold it in confidence.¹⁹⁰

It seems that Phillips's engineers developed the "loop slurry" process in 1958. Over the following years, the process was further improved and was licensed out by Phillips and its successors (including CPChem) to allow other companies to build their own "loop slurry" plants through over a hundred different licensing agreements. In time, INEOS acquired the assets of a joint venture which included some of the plants built under authority of these licenses, together with the related information regarding the "loop slurry" process, and it began licensing the "loop slurry" technology to third parties. CPChem brought suit against INEOS, claiming misappropriation of trade secrets and breach of contract.¹⁹¹

INEOS defended, in part, by examining exactly how the secrecy of the "loop slurry" process had been treated since 1958. Its own licensing agreements with CPChem—or more precisely, the ones to which it had acceded when it acquired the relevant assets—were perpetual in nature. But INEOS found several agreements under which Phillips had disclosed the technology under confidentiality agreements which had long since expired.¹⁹²

INEOS argued that a "trade secret must be a secret," that "[v]igilance in guarding the trade secret is required," and that its owner may disclose it to a third party if it takes steps to insure the secrecy, but that "the unrestricted disclosure of trade-secret information to third parties, outside . . . a confidential relationship, destroys the trade-secret status of the information."¹⁹³ Most of the license agreements contained "perpetual" secrecy clauses, but INEOS took CPChem to task for a number of such agreements that had expired by their own terms, such as a 1979 agreement with a fifteen-year term indicating that Phillips had been paid \$1.5 million "specifically for the shortened secrecy term"¹⁹⁴ and several from 1976 with twenty-five-year secrecy terms.¹⁹⁵

In INEOS's view, these agreements had clearly expired with the full knowledge of CPChem's predecessor in interest; hence, the "loop slurry" technology could no longer enjoy trade secret protection, if it ever had. CPChem, of course, disagreed, and presented an explanation with respect to each instance. In one instance of an expired confidentiality agreement, CPChem explained that the licensee was *itself* owned by a parent company bound by a "perpetual" confidentiality requirement. In another, the licensee had subsequently agreed not to license the technology to third parties. As to another (with a government ministry in Iraq), CPChem objected that the time limits should not be deemed to have ever started running because of force majeure issues with respect to enforce-

190. *Id.* at *1.

191. *Id.* at *1-2.

192. *Id.* at *2.

193. *Id.* at *7-8.

194. *Id.* at *5.

195. *Id.* at *6-7.

ment inside Iraq. CPChem claimed to have renegotiated other agreements. In any event, CPChem urged that in fact the secrecy had not really been lost. And it objected that in the 1979 agreement there was no evidence that the funds were paid "specifically for the shortened secrecy requirement."¹⁹⁶ (Perhaps the various licensees preferred to keep it to themselves rather than reveal the technology to others, but if so, the opinion made no mention of it.)

The issue in *INEOS* seemed to turn on the exact nature of what CPChem was required to prove to qualify for a temporary injunction—which, it appears, is a fairly low threshold. At the temporary injunction stage, movant CPChem was required only to prove "a probable right of relief on its misappropriation of trade secrets claim."¹⁹⁷ However accurately *INEOS* may have recited the legal principles applicable to trade secrets, the Houston First Court of Appeals concluded that it could *not* apply them to determine whether the "loop slurry" technology was actually a trade secret.¹⁹⁸ "To the contrary," the court of appeals held, "when deciding whether to grant trade-secret protection through a temporary injunction, a trial court does not determine whether the information . . . is, in law and fact, a trade secret; rather, [it merely] determines whether the [movant has shown it] is entitled to trade secret protection pending . . . trial on the merits."¹⁹⁹

Further, in order to make this showing, all CPChem was required to show was "some evidence . . . tending to show that it possessed a trade secret," and more specifically in this case, "some evidence tending to show [it had been] sufficiently vigilant."²⁰⁰ After noting that it was to "view[] the evidence . . . in the light most favorable to the [trial] court's ruling, draw[] all legitimate inferences [favorable to the trial court's ruling], and defer[] to the trial court's resolution of conflicting evidence," the court of appeals had no trouble finding CPChem had presented "some evidence" of vigilance in maintaining the secrecy of the technology.²⁰¹ The court of appeals cited to the familiar cases of *Rugen v. Interactive Business Systems, Inc.*²⁰² and *Gonzales v. Zamora*²⁰³ for the proposition that "[w]hen an effort is made to keep material important to a particular business from competitors, trade secret protection is warranted."²⁰⁴

In practical terms, "some evidence" of making "an effort"²⁰⁵ to maintain confidentiality should not be read to minimize the need for secrecy precautions. Absolute secrecy is not required, but reasonable precau-

196. *Id.* at *5-9.

197. *Id.* at *4.

198. *Id.* at *8.

199. *Id.*

200. *Id.*

201. *Id.* at *9.

202. 864 S.W.2d 548, 552 (Tex. App.—Dallas 1993, writ denied).

203. 791 S.W.2d 258, 265 (Tex. App.—Corpus Christi 1990, no writ).

204. *Id.* at *9.

205. *See id.*

tions are,²⁰⁶ and a court can rarely be persuaded to protect property more strenuously than its owner has protected it. *INEOS v. Chevron Phillips* also suggests that confidentiality agreements with term limits might profitably be re-examined and considered from time to time. Two years may seem like a long time in a fast-moving industry like communications technology, but as *INEOS* shows, even twenty-five years can go by very quickly.

VII. FALSE ADVERTISING

A. PUFFING AGAIN

The *Bridal Expo* court also addressed the federal claims raised by the plaintiff, starting with the plaintiff's likelihood of success on the merits of its false advertising claim.²⁰⁷

A prima facie case under § 43(a) requires the plaintiff to establish: (1) the defendant made a false statement of fact about its product; (2) the statements deceived or had the capacity to deceive a substantial segment of potential customers; (3) the deception is material, in that it is likely to influence the purchasing decision; (4) . . . interstate commerce [is involved;] and (5) the plaintiff has been . . . injured as a result.²⁰⁸

If the plaintiff proves the commercial message at issue is "literally false," the second and third elements will be presumed.²⁰⁹ Otherwise, the plaintiff has to show that the message had a tendency to deceive potential customers and that it actually affected their purchasing decision. Also, the statement has to amount to more than "puffery"; in other words, it must be more than a general statement of opinion or claim of superiority.²¹⁰

Defendants called the Google ads puffery and argued that their use of "our" in the brochures "refer[red] to the principals of Wedding Showcase, who have produced many shows." Moreover, the brochures said "several times that the Houston Wedding Showcase is a new show."²¹¹

The district court agreed. Based on the Fifth Circuit's holding in *Pizza Hut, Inc. v. Papa John's International, Inc.*,²¹² the court held that the Google ads were too ambiguous to be considered literally false, the assertion that the defendant was "#1" was not empirically verifiable, and anyway, such a statement was the kind of "bald assertion" or "general

206. See *In re Bass*, 113 S.W.3d 735, 739 (Tex. 2003) (extent of measures taken to guard the secrecy of the information is a factor to be considered); see also RESTATEMENT OF TORTS § 757 cmt. b (1939); RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 39 reporter's note cmt. d (1995).

207. *Bridal Expo, Inc. v. Van Florestein*, No. 4:08-cv-03777, 2009 WL 255862, at *5 (S.D. Tex. Feb. 3, 2009); see also *supra* Part VI.C; *infra* Part VIII.

208. *Bridal Expo*, 2009 WL 255862, at *5.

209. *Id.* at *6.

210. *Id.* at *6-7.

211. *Id.* at *6.

212. 227 F.3d 489 (5th Cir. 2000).

statement of superiority” on which no reasonable consumer would rely.²¹³ In any event, the defendants stopped running the ad, so injunctive relief was not necessary.²¹⁴

As for the brochure, where defendants used the pronoun, “our,” to describe vendors and brides even before they had held their first event, the court found no literal falsity. “Our” likely referred to the show’s owners, it felt, one of whom ran the shows on the East Coast from which the “our” statements came.²¹⁵ The brochure explained that the Houston Wedding Showcase *would* be “a new show . . . with a long history.”²¹⁶ The court concluded that it was unlikely that a sophisticated vendor audience, familiar with the Houston wedding market, would be misled into thinking that the quoted brides and vendors were previously affiliated with the Wedding Showcase, or that it would affect their decision to attend the defendants’ event.²¹⁷

B. WHO IS THE ADVERTISER? AND WHAT IS AN “ADVERTISEMENT”?

*Heartbrand Beef, Inc. v. Lobel’s of New York, LLC*²¹⁸ illustrates the occasional difficulty of assessing advertising claims in close competition. Heartbrand sells Akaushi beef, the South Texas breeder’s equivalent to the very popular and very expensive Japanese Kobe beef. Heartbrand brought an enforcement action against several defendants, including Yahoo!, for false designation of origin under section 43(a) of the Lanham Act. When a user typed the keyword, “Akaushi,” into the Yahoo! search engine, the first sponsored site that appeared was for the website, www.akaushisteaks.com. This link contained no actual content but instead was a collection of links. When a user clicked one of the links containing the word, “akaushi,” they were directed to lobels.com. Lobel’s sells high-quality beef, but it does not sell Akaushi beef. Heartbrand alleged that Yahoo!’s display of the ad constituted common-law unfair competition²¹⁹ and false designation of origin in violation of section 43(a) of the Lanham Act.²²⁰

The district court recited the elements of a false designation of origin claim under section 43(a) which are identical to those for false advertising.²²¹ The court preliminarily acknowledged that Heartbrand’s section 43(a) claim against Yahoo! seemed confusing, since “Yahoo! obviously does not fit into these classic models [of false designation of origin] because Yahoo! is not in the business of selling beef.”²²² The court went on

213. *Bridal Expo*, 2009 WL 255862, at *6-7.

214. *Id.* at *7.

215. *Id.* at *8.

216. *Id.*

217. *Id.*

218. No. V-08-62, 2009 WL 311087 (S.D. Tex. Feb. 5, 2009).

219. *Id.* at *1.

220. 15 U.S.C. § 1125(a) (2006).

221. *Heartbrand Beef*, 2009 WL 311087, at *2; *supra* Part VII.A (listing the elements); see *Pizza Hut v. Papa John’s Int’l, Inc.*, 227 F.3d 489, 495 (5th Cir. 2000).

222. *Heartbrand Beef*, 2009 WL 311087, at *2.

to analyze the complaint using the section 43(a) elements anyway and rejected Heartland's claim first, because Yahoo! did not make a "statement" by placing an advertisement—the advertiser made the statement—and second, even if Yahoo! did make a statement, the statement was not about Yahoo!'s own products and services.²²³ It is not clear what unfair competition claim remained—since Heartland and Yahoo! weren't competitors—but Yahoo! did not address it in its motion to dismiss.

Use of "keywords" in Internet search engines has led to considerable dispute for some years now, primarily in the trademark (designation of origin) context, with some courts holding that "use" of another company's trademark in metatags or keywords constitutes "use" for purposes of trademark infringement and others holding that it does not. Geographic regions known for their production of fine qualities of a certain product (e.g., Champagne), particularly but not exclusively in Europe, often claim it is deceptive to use the names of those regions to identify types of products not sourced from there. In this case, however, the word "Akaushi" seems not to be used to designate a particular producer, or a region of the country, but rather a generic type of beef. It would seem, therefore, that the appropriate section 43(a) analysis would have been under 15 U.S.C. § 1125(a)(1)(B)—the "false advertising" prong—rather than the § 1125 (a)(1)(A) prong of "false designation of origin." Probably the court would have arrived at the same conclusion either way, but it might have had an easier journey and left a clearer trail to follow.

VIII. COMPUTER FRAUD AND ABUSE ACT

WHAT IS "AUTHORIZATION"?

In *Bridal Expo*, the plaintiff also brought claims under the Computer Fraud and Abuse Act (CFAA),²²⁴ which creates liability for a person who "knowingly and with intent to defraud, accesses a protected computer *without authorization*, or *exceeds authorized access*, and by means of such conduct furthers the intended fraud and obtains anything of value."²²⁵ To establish a civil violation, there are extra requirements; here, the relevant additional factor was "loss to 1 or more persons during any 1-year period . . . aggregating at least \$5,000 in value."²²⁶ The term "loss" includes costs of responding to an offense, such as restoring any information that was disturbed or interrupted as a result of the offense, and conducting a damage assessment.²²⁷

Bridal Expo claimed its former employees van Florestein and Moore acted without authorization when they accessed its files on the day they resigned, after they had turned in their office keys (and another em-

223. *Id.* at *2-3.

224. *Bridal Expo, Inc. v. Van Florestein*, No. 4:08-cv-03777, 2009 WL255862, at *2 (S.D. Tex. Feb. 3, 2009); *see also supra* Parts VI.C., VII.A (discussing *Bridal Expo*).

225. 18 U.S.C. § 1030(a)(4) (2006) (emphasis added).

226. *Bridal Expo*, 2009 WL 255862, at *9.

227. *Id.*

ployee had let them back into the office), and that the corresponding loss plaintiff suffered was its confidential trade secrets. Defendants responded that there is a marked and significant difference between access to computers and use or disclosure of information obtained through that access.²²⁸

The district court pointed out a split among the circuits over the meaning of “authorization.” Some courts conclude that authorization focuses on the alleged violator’s intent, as when an employee accesses files to use them in harming the employer, even if the employee technically has authorization to access the files in the scope of her duties. Other courts have noted that if Congress had intended to include all wrongdoers, it would have eliminated the “authorization” language. The Fifth Circuit has not yet ruled on the issue. The district court determined that, given the statutory construction argument and the rule of lenity (since the CFAA is also a criminal statute), it would not “equate ‘authorization’ with a duty of loyalty to an employer,” and thus “authorization” is not exceeded just because the employee intends to or ultimately does misuse the acquired information.²²⁹

The district court found that van Florestein and Moore had not signed a confidentiality agreement or any other agreement restricting access to the files they worked on at Bridal Expo. Further, they accessed the files on the last day of their employment (even though they had already turned in their keys), and it was “within the nature of their [employment] relationship” to use their computers and access the files at issue.²³⁰ Thus, the court held that van Florestein and Moore did not exceed their authorization to access the information, and Bridal Expo was unlikely to succeed on the merits of its CFAA claim.²³¹ Even had there been a likelihood of success, the court said injunctive relief would not be warranted, based on the Fifth Circuit’s hesitance to grant injunctive relief against the use of information “obtained through a past violation of the CFAA” where there was no potential for ongoing access.²³²

This seems to leave the nature of “authority” less than entirely clear. It is understandable that, based upon an interpretation of less-than-clear statutory language, the court might not wish to automatically expose the former employees to a higher degree of culpability than Congress may have intended. But in this case, it is not readily apparent what “authority”—however it is defined—the former employees might still have to access their former employer’s databases once they had resigned, turned in their keys, and left the building. Coming back in to retrieve personal items would be one thing, but coming back in to retrieve information held in the company’s databases would seem to be quite another.

228. *Id.*

229. *Id.*

230. *Id.* at *11.

231. *Id.*

232. *Id.*

IX. CONCLUSION

No startling, new principles of competition burst into view this year. Instead, Texas continued its steady course of common law development in this area, clarifying points here, reminding practitioners there, addressing (among many others) the following:

- Where a product *is* bad, saying so will rarely be actionable;²³³
- “Merger clauses” may forestall fraud claims only where they clearly anticipate them;²³⁴
- Political subdivisions still enjoy sovereign immunity from tortious interference claims;²³⁵
- Necessarily implied promises to deliver confidential information may support a non-competition agreement;²³⁶ and
- “Authorization” under the Computer Fraud and Abuse Act is less than certain.²³⁷

233. *See supra* Part I (discussing *David Rafes, Inc. v. Huml*, No. 01-08-00856-CV, 2009 WL 3491043 (Tex. App.—Houston [1st Dist.] Oct. 29, 2009, no pet.)).

234. *See supra* Part II (discussing *LJ Charter, L.L.C. v. Air. Am. Jet Charter, Inc.*, No. 14-08-00534-CV, 2009 WL 4794242 (Tex. App.—Houston [14th Dist.] Dec. 15, 2009, pet. filed)).

235. *See supra* Part III.B (discussing *City of Houston v. Guthrie*, No. 01-08-00712-CV, 2009 WL 5174258 (Tex. App.—Houston [1st Dist.] Dec. 31, 2009, no pet.)).

236. *See supra* Part IV.F. (discussing *Mann Frankfort Stein & Lipp Advisors, Inc. v. Fielding*, 289 S.W.3d 844 (Tex. 2009)).

237. *See supra* Part VIII (discussing *Bridal Expo, Inc. v. Van Florestein*, No. 4:08-c-03777, 2009 WL 255862 (S.D. Tex. Feb. 3, 2009)).

