

Resources

Texas Supreme Court Opens the Door for a New Option to Restrict Post-Employment Conduct

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On August 29, 2014, the Texas Supreme Court issued its long-awaited decision in *Exxon Mobil Corporation v. Drennen*. The court ruled that Drennen, a former ExxonMobil executive, could be stripped of approximately \$5 million in unvested restricted stock for taking a position with a competitor in violation of the detrimental-activity provisions of the incentive programs under which he had received the restricted stock awards.

Importantly, this case was not decided under Texas law as the contracts in question had choice of law provisions calling for New York law to apply. Nonetheless, this decision may have major implications for Texas corporations wishing to reward valuable employees and encourage retention.

Even though Texas had a close relationship to the issue – Drennen lived in Texas, ExxonMobil is based in Texas and the suit was filed here – the Court found that the detrimental activity provision was not a covenant not to compete and that, therefore, the enforcement of New York law would not contravene any fundamental public policy of Texas. Under New York law, the court determined that ExxonMobil had lawfully terminated the outstanding awards upon Drennen's breach of the restrictive covenants in the incentive programs.

The Court signaled that such provisions may be enforceable under Texas law rather than unenforceable non-competition agreements, stating that:

There is a difference, although a narrow one, between an employer's desire to protect an investment and an employer's desire to reward loyalty. Non-competes protect the investment an employer has made in an employee, ensuring that the costs incurred to develop human capital are protected against competitors who, having not made such expenditures, might appropriate the employer's investment. Forfeiture provisions conditioned on loyalty, however, do not restrict or prohibit the employees' future employment opportunities. Instead, they reward employees for continued employment and loyalty. . . . [E]mployee stock-ownership plans have a purpose that is unrelated to restraining competition—linking the interest of key employees with the employer's long-term success. Under a noncompete, the former employer can bring a breach of contract suit to enforce the clause. But under a forfeiture provision, the former employer does not need to take legal action because the profit sharing plan belongs to the employer.

The Court did not give employers certainty that these provisions would be enforceable under Texas law. It noted that it had not considered whether such provisions in non-contributory employee incentive programs were unenforceable under Texas law as unreasonable restraints on trade. That question was reserved for another day.

What does this mean for employers?

Employers who provide similar stock incentive plans to their key executives should review those agreements and determine if adding a detrimental-activity clause makes sense for their organizations, or if they have such provisions, that they are consistent with this ruling. While enforceability of such provisions is not certain, the Texas Supreme Court has clearly indicated a willingness to consider this possibility.

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