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The Case of the Moonlighting Employee

Allison L. Bowers
Brenna Holmes Nava

Authors Contact Information:

Allison L. Bowers
Hutcheson Bowers LLLP
Austin, TX

allison@hutchesonbowers.com
512.777.4449

Brenna Holmes Nava
Rackspace Hosting, Inc.
San Antonio, TX

brenna.nava@rackspace.com
210.312.9316

MOONLIGHT

noun moon·light \-ˌlīt\

Simple Definition: the light of the moon

Also an intransitive verb meaning to hold a second job in addition to a regular one

moon·lights, moon·light·ed, moon·light·ing

Example: She is a secretary who *moonlights* as a waitress on weekends.

First Known Use: 1957

MERRIAM-WEBSTER DICTIONARY

http://www.merriam-webster.com/dictionary/moonlighting

I. INTRODUCTION

Although the word moonlighting has been used for nearly 60 years to describe an employee working a second job during their off hours, the ramifications of these secondary employment situations have grown exponentially over the decades. Today, in the fast-paced, high-tech industry, a company's employees often take on consulting projects for other companies, work on their own passion projects and startup ideas both during and after their primary work hours, and even develop applications and programs for their employer's platform for which the employer allows the employee to retain the resulting intellectual property and much of the ensuing revenue, all with the employer's blessing.

Unfortunately for employers, not all employees undertake side work with the best of intentions. The past two decades have been fraught with litigation in the high tech world resulting from employees who unfairly compete with their prior employer, who breach their fiduciary duties, who disclose, consciously or unconsciously, protected proprietary and confidential information and who unlawfully claim that inventions and intellectual property developed by them actually belongs to them and not their employer despite the fact that they had contractually agreed otherwise.

This paper will present dilemmas taken from the ever-shifting landscape of supplemental employment in the technology field and how those situations implicate state and federal contractual and common law obligations for both employers and their moonlighting employees. This paper also provides up-to-date model agreement language designed for technology employers so that they can best protect their business should an employee (or employees) act in a manner that unfair competes with or unlawfully damages a company or diverts away corporate opportunities for that employee's benefit.

II. THE CASE SCENARIOS OF THE MOONLIGHTING EMPLOYEES

- ***The Off-Hours, Self-Taught Game Designers***

  Two employees work as artists for an online gaming website. They decide that they want to design their own games and to form their own startup. On their off-hours, they both learn how to code and how to game design using their own equipment and facilities. Neither employee informs their employer of this new endeavor despite the fact that they are both bound by a written contractual obligation to do so. The employees finally design a successful game of their own. The employer claims ownership of the game and intellectual property and informs the employees that it is entitled to all rights and revenue based on the inventions assignment provision in the would-be game designers' employment agreements. The employees, of course, disagree and claim ownership on the basis that it was created off-hours and with no assistance from the employer.

- ***The IT Professional Who Consults on the Sly***

  An IT manager's supervisor calls her in for an unscheduled meeting. The supervisor informs the manager that it has come to his attention from another employee that the IT manager is moonlighting as a consultant in addition to handling her full time duties as IT manager for their employer. The IT manager does not deny consulting on the side. She informs her supervisor that she began consulting for clients—some of whom she gained through her work as IT manager—two months ago and assures her boss that she only does this consulting before work, at lunch and after work. The IT manager is not bound by an exclusivity provision or other contractual arrangement that forbids her from moonlighting; however, the IT manager did sign a noncompetition agreement at the onset of her employment that forbids her from working for a competitor during her employment and for one year following the termination of her employment as well as prohibiting her from soliciting the company's customers. Her supervisor informs her that he is going to consult with the company president and the human resources manager about the situation as he does not believe she is capable of maintaining her current level of productivity as an IT manager while she also works her part-time consulting gig.

- ***The Group of Employees Who Decide to Start their Own Company, which Becomes a Direct Competitor with their Employer***

  Three software engineers each separately and independently inform their respective group leaders that they would like to pursue discrete side "passion" projects after hours. The company does not outright ban moonlighting, but each software engineer signed an employment agreement, which contains provisions for nondisclosure, non-solicitation of employees and customers and noncompetition. Additionally, the company's Code of Conduct contains a conflict of interest policy. When viewed individually, it does not appear to the employees that their after-work activities breach any contractual provision or common law duties. Around the same time as these employees start their separate moonlighting gigs, their division manager, who is also a corporate officer, discretely prepares to form a competing entity. He scouts new office space and looks into equipment leasing options. He also starts to notify the employer's vendors and customers of his intent to form a new startup. Ultimately, following the division manager's lead, each of the software engineers leave the company

> because, in actuality, they were involved with and critical to the division manager's startup—a business that in no uncertain terms competes with their former employer and slowly siphons off its customer base. The employees maintain they have disclosed none of their former employer's proprietary information and have breached no contractual provision. Their former employer disagrees and retains counsel to represent it in a lawsuit for immediate injunctive relief against the new startup and each of the individuals.

Each of the three scenarios above presents a myriad of employment issues, some with clear-cut outcomes and some with results that are likely fact specific because no bright line rule to predetermine their outcome exists. Although these situations are fictitious, the issues raised are becoming more and more commonplace in the technology sector as the definitions and parameters of employment begin to change and blur respectively. In today's environment, both employee and employer loyalty are sometimes fleeting and as transitory as the employees and employers themselves. Employees jump from company to company and rarely retire after staying with a company for 25 years.

III. COMMON LAW ISSUES THAT ARISE BECAUSE OF A MOONLIGHTING EMPLOYEE

Employers often ask employees to sign contractual, restrictive provisions designed to prevent employee competition and disclosure of confidential information and to ensure adequate assignment of rights to ideas and inventions developed during employment. In addition to these contractual protections, multiple common law safeguards also exist to ensure that the moonlighting employee does not overstep her boundaries and engage in extracurricular employment that unlawfully encroaches upon her employer's business.

A. FIDUCIARY DUTIES OWED TO AN EMPLOYER

Certain employees—in most circumstances, officers and directors—owe fiduciary duties to their employers. For example, the division manager who is a corporate officer and who forms his own startup while still employed by his primary employer in the fictitious scenario above, owes a duty of loyalty to his employer because of the special relationship that exists between a company and its officers.

1. ELEMENTS NECESSARY TO ESTABLISH A BREACH OF FIDUCIARY DUTY

There are four elements to an employer's claim against its employee for breach of fiduciary duty: (i) existence of a fiduciary duty; (ii) breach of the duty; (iii) causation and (iv) damages." *Abetter Trucking Co. v. Arizpe*, 113 S.W.3d 503, 508 (Tex. App.—Houston [1st Dist.] 2003, no pet.); *Homoki v. Conversion Servs., Inc.*, 717 F.3d 388, 403 (5th Cir. 2013).

a. When is someone a fiduciary?

The existence of a fiduciary duty is a question of law. *Nat'l Plan Admin., Inc. v. Nat'l Health Ins. Co.*, 235 S.W.3d 695, 700 (Tex. 2007). Fiduciary duties are imposed on parties to certain relationships based on the special nature of those relationships. *Id.* Although there are various relationships leading to a fiduciary duty, qualifying employees typically fall into a "formal" category, due to a principal–agent relationship with their employer. *See Abetter*, 113 S.W.3d at 508. The Texas Supreme Court has broadly stated that an "agreement to act on behalf of the principal causes the agent to be a fiduciary, that is, a person having a duty, created by his undertaking, to act primarily for the benefit of another in matters connected with his undertaking." *Johnson v. Brewer & Pritchard, P.C.*, 73 S.W. 3d 193, 200 (Tex. 2002), *quoting* THE RESTATEMENT (SECOND) OF AGENCY. The Court has qualified that, "even in an agency relationship such as employer–employee, courts take all aspects of the relationship into consideration when determining the nature of fiduciary duties flowing between the parties." *Nat'l Plan Admin.*, 235 S.W.3d at 700–03 (taking into account contractual agreements between two companies in determining scope of relationship).

While Texas law does not usually find a formal fiduciary duty when the relationship is simply between employee and employer, an "informal" fiduciary relationship may exist. *See, e.g., Merritt Hawkins & Assocs., LLC, MHA v. Gresham*, 79 F.Supp. 3d 625, 637 (N.D. Tex. 2015) (stating that an "employee's fiduciary duty still prohibits him from appropriating his employer's trade secrets or carrying away information such as customer lists"). Courts have found an employee-employer fiduciary relationship under the "informal" category, arising when "one person trusts in and relies upon another . . . ." *Navigant Consulting, Inc. v. Wilkinson*, 508 F.3d 277, 283 (5th Cir. 2007) (quoting *Jones v. Blume*, 196 S.W.3d 440, 447 (Tex. App.—Dallas 2006, pet. denied); *see, e.g., Molex, Inc. v. Nolen*, 759 F.2d 474, 479 (5th Cir. 1985) (finding a fiduciary relationship because the employer "obviously trusted and relied on Nolen, as the sales representative responsible for the Tandy account, in its dealings with Tandy"). One Texas court has noted that the parties' subjective feelings of trust are not enough to create such a relationship. *Cf. Gregan v. Kelly*, 355 S.W.3d 223, 229 (Tex. App.—Houston [1st Dist.] 2011 no pet.) (concluding that *employer* did not owe *employee* fiduciary relationship despite testimony by employer that the parties trusted and placed confidence in each other).

The Houston Court of Appeals concluded that an employee was a fiduciary simply because of his employee status—without any in-depth analysis. *See Gaal v. BASF Wyandotte Corp.*, 533 S.W.2d 152, 154 (Tex. App.—Houston [14th Dist.] 1976, no writ) (stating that an employer claiming breach of fiduciary duty "had a contractual and common-law right to require [employee] to act in good faith towards its customers during [his] term of employment"). Another recent opinion simply applied the Court's broad language from *Brewer & Pritchard*, reasoning an employee owed a fiduciary duty to the extent he "agreed to act on behalf of" the employer "in matters connected with his employment." *Speedemissions, Inc. v. Capital C Enterprises, Ltd.*, 01-07-00400-CV, 2008 WL 4006748 at *7 (Tex. App.—Houston [1st Dist.] Aug. 28, 2008, no writ) (mem. op). The opinions that have more critically analyzed the issue tend to focus on the level of responsibility, discretion, and importance of the role given to the employee in deciding whether the duty exists. *See SP Midtown, Ltd. v. Urban Storage, L.P.*, 14-07-00717-CV, 2008 WL 1991747, at *12 (Tex. App.—Houston [14th Dist.] May 8, 2008, pet. denied) (mem. op); *Daniel v. Falcon Interest Realty Corp.*, 190 S.W.3d 177, 185–86 (Tex. App.—Houston [1st Dist.] 2005, no pet.).

For example, where an employee occupied "the most important day-to-day position at the facility," a supervisory role over clients and marketing, and possessed confidential pricing and marketing information, there was more than a scintilla of evidence of his fiduciary role. *SP Midtown, Ltd.*, 2008 WL 1991747 at *12. That the employee "was in charge of all daily financial transactions and had the authority to transact business on behalf of [the employer] without daily supervision" supported this conclusion. *Id.*

Also, the Houston appellate court held that a project manager and on-site superintendent for a construction project owed a fiduciary duty as to his role of subcontracting the work out for the project. *Daniel*, 190 S.W.3d at 185–86. The court considered that his responsibilities included soliciting bids, setting the scope of work for each subcontractor, reviewing the bids and overseeing workers and that he also "occupied a position of peculiar confidence towards" the employer. *Id.*

In *Navigant*, supra, an informal fiduciary duty was found by the jury because the two head employees of the company's Dallas office had a "relationship of trust and confidence" with the company. 508 F.3d at 283. The employees did not challenge the jury's finding, though the court specifically noted in support of the finding that the employees "enjoyed broad discretion over almost all aspects of the Claims Practice" that they were secretly planning to compete against. *Id.*

b. Breaching a fiduciary duty

The Texas Supreme Court has explained that an employee bound by the fiduciary duty must (i) account for profits arising out of the employment; (ii) not act as, or on account of, an adverse party without the principal's consent; (iii) not compete with the principal on his own account or for another in matters relating to the subject matter of the agency; and (iv) deal fairly with the principal in all transactions between them. *Johnson v. Brewer & Pritchard, PC*, 73 S.W.3d at 200. Taking customer lists or other proprietary information is also a breach of fiduciary duty. *Id.; Cuidado Casero Home Health of El Paso, Inc. v. Ayuda Home Health Care Svcs, LLC*, 404 S.W.3d 737, 752 (Tex. App.—El Paso 2013, no pet.).

Whether an employee's acts during employment rise to the level of competition is a fact issue to be determined by the jury. *See Abetter*, 113 S.W.3d at 513. An employee who solicits business from the employer's existing client breaches his fiduciary duty to his employer, as this is direct competition. *See id*. In *Abetter*, however, the court upheld the jury's no-breach finding where the employee "mentioned he would like to start his own company" and "just briefly broached the subject" of "some day" working for the client. *Id*. at 512 (concluding that jury could have found employee "acted in [employer]'s best interests"); *compare with Gaal*, 533 S.W.2d at 154 (concluding employee breached duty by "soliciting and capturing business from approximately thirty of appellee's customers while still employed by appellee"). Also, referring a customer to a competitor is not a breach of fiduciary duty unless the employee "accept[s] or agree[s] to accept profit, gain, or any benefit from" the referral. *Brewer & Pritchard*, 73 S.W.3d at 203.

When an employee is disloyal and takes steps to divert wrongfully corporate opportunities from his employer, the mistake can be a costly one. Just last month, the Sixth Circuit Court of Appeals upheld a district court decision granting summary judgment against two former employees in addition to affirming an award of $3,680,3454.18 in damages and a permanent injunction. In *Nedschroef Detroit Corp. v. Bemas Enters. LLC*, Case No. 15-1728, (6th Cir. April 22, 2016), Marc Rigole and Bernard LePage, the manager and highest ranking employee of Nedschroef Detroit and a project/service engineer, respectively, covertly formed a competitive business in 2011 that engaged in the same work as Nedschroef Detroit—servicing and providing replacement parts for Nedschroef fastener machines. *Id.* at *2. Two years later, Nedschroef Detroit fired the two employees after learning of their competing business, Bemas Enterprises. *Id.*

The Nedschroef Plaintiffs sued Rigole, LePage and their company, Bemas, for, among other things, breach of the duty of loyalty, breach of fiduciary duty and misappropriation of corporate opportunities. *Id.* at *2. The district court granted summary judgment for the Nedschroef Plaintiffs on all claims, awarded nearly $3.7 million dollars and permanently enjoined the defendants from providing replacement parts or services to Nedschroef machines in North America. *Id.*

On appeal, the Sixth Circuit was "satisfied" that the district court properly had granted summary judgment and issued a permanent injunction. *Id.* at *5. The appellate court based its decision on the undisputed facts presented that Rigole and LePage created and ran Bemas as a competitive business with Nedschroef while they were still Nedschroef employees. *Id.* at *3. The court also found that the defendants had misappropriated proprietary information despite their claim that Bemas's customer supplied them with Nedschroef's proprietary information. *Id.* The court stated that expert testimony proved that claim wrong in addition to the fact that Bemas's document production showed they received Nedschroef's information directly from Bemas, but with all references to Nedschroef removed. *Id.*

The Sixth Circuit stated that the trial court correctly had concluded "that regardless of the source from which Defendant obtained the drawings, Defendants in fact acquired Nedschroef's confidential drawings through breach of a duty to maintain their secrecy, then used those drawings to manufacture and sell parts in direct competition with Nedschroef." *Id.* at *4-5.

c. Causation and Damages

Although causation and damages are purportedly elements of the claim, courts have held the employer need *not* show actual damages caused by the breach if the employer is seeking only profit disgorgement—courts have upheld awards to the employer in the amount that the employee profited. *See Kinzbach Tool Co. v. Corbett-Wallace Corp.*, 138 Tex. 565, 573 (Tex. 1942) (stating "[i]t is beside the point . . . to say that [the employer] suffered no damages because it received full value for what it has paid and agreed to pay"). Instead, "if the fiduciary takes any . . . benefit in violation of his duty, or acquires any interest adverse to his principal, without a full disclosure, it is a betrayal of his trust and a breach of confidence, and he must account to his principal for all he has received." *Id.* For example, in *Daniel v. Falcon Interest Realty Corp.*, an employee project manager responsible for subcontracting out a project conspired with his family members to form a business to which the manager could channel the work at a profit for both

him and his family. 190 S.W.3d at 186 177, 186. The court concluded the employee must disgorge his profits from those insider deals, despite the employer's admission that the family's company performed satisfactory work at a price that was less costly than other bidders. *Id.* at 187.

A loss at trial for a moonlighting-on-the-sly, self-dealing employee, much like the division manager/corporate officer in the third scenario of this paper, can be costly. Take *Advanced Nano Coatings, Inc. v. Hanafin*, 556 Fed. Appx. 316, 319 (5th Cir. Feb. 19, 2014), for example. In *Advanced Nano Coatings*, the Fifth Circuit ruled that a former employee who breached his fiduciary obligations to his former employers by self-dealing with their customers was required "to repay everything he gained by virtue of his position, including payments for his salary and any expenses he may have incurred." *Id.* The appellate court also affirmed the district court's award of $417,688.44 in attorney's fees and expenses and $57,000.00 in appellate attorney's fees in the event the former employers were ultimately the prevailing parties. *Id.* at 320.

2. RECENT CASE LAW

a. ***Sisoian v. International Bus. Machs., Corp.*, No. A-14-CA-565-SS, 2014 WL 4161577 (W.D. Tex. Aug. 18, 2014)**

Sisoian stands for the proposition that an employee's fiduciary duties to his former employer do not necessary die with the termination of his employment with that company. Thomas Sisoian developed the "Objectiva Architecture" for his company, Objectiva Innovations, Inc. *Id.* at *1. He hired two employees, Francis Anderson and James Hartmann, both of whom signed employment agreements, which included a nondisclosure of proprietary information provision. *Id.* Sisoian ultimately dissolved his company and entrusted Hartmann to retain the digital source images and data files for the Objectiva Architecture. *Id.* Prior to the dissolution, IBM hired Sisoian and then Anderson as a project architect. Both signed agreements in which they agreed to assign to IBM all rights to works of authorship developed during their IBM employment. *Id.* The Objectiva Software was excluded from these agreements, and Anderson returned his copy of the architecture to Sisoian. A few years later, Anderson requested a copy of the architecture from Hartmann, his former coworker at Objectiva, under the false auspice that he was asking on Objectiva company business. *Id.* Anderson obtained and then disclosed the architecture to IBM, which then used it to covertly create Websphere Telco Content Pack and from which it made substantial revenue. *Id.*

Sisoian learned of IBM's use of the Objectiva Software and sued IBM claiming, among other things, that Anderson breached his fiduciary duty to Objectiva by disclosing the architecture. IBM argued that the breach of fiduciary duty claim should be dismissed for failure to state a claim because Anderson's alleged breach happened when he no longer had a fiduciary relationship with Objectiva (*i.e.* after his employment with Objectiva had ended). *Id.* at *5.

Federal District Court Judge Sam Sparks disagreed and sided with Sisoian. Judge Sparks determined that Sisoian had sufficiently alleged a breach of fiduciary duty claim. In the opinion, the judge wrote:

> While the fiduciary relationship might have ended, Anderson still owed a duty not to disclose confidential information after he no longer worked for Objectiva. According to Sisoian's allegations, Anderson, as part of his employment with Objectiva, signed a Confidentiality, Proprietary Information, and Trade Secrets agreement, requiring employees not to disclose Objectiva's proprietary information to any third party without prior written consent from Objectiva. Therefore, even though Anderson returned his copy of the Objectiva Architecture and his Objectiva-issued laptop when his employment with Objectiva ended in September 1999, he still could not disclose proprietary information to third parties.

Id. at *5.

b. *Frisco Med. Ctr d/b/a Baylor Med. Ctr.at Frisco v. Bledsoe*, No. 4:12-CV-37/4:15-CV-105, 2015 WL 7734108 (E.D. Tex. Nov. 30, 2015)

In *Frisco Medical Center*, a husband and wife team were caught absconding with a litany of confidential and proprietary information via, among other things, Dropbox—a web-based file hosting service that uses cloud storage—over a one-week time period between the wife's acceptance of a job at another medical center and her resignation date. Cynthia Bledsoe was employed by Baylor Medical Center at Frisco ("Baylor Frisco") as Chief Operating Officer and her husband was the Information Systems Administrator when she resigned in late 2011. *Id.* at *1-2. After Ms. Bledsoe had commented that she "knew where too many bodies were buried," Baylor Frisco hired Hewlett-Packard IT Security Investigations to conduct a forensic investigation of the Bledsoe's computer equipment. *Id.* at *2. The investigation revealed that the Bledsoes had engaged in many subversive acts, including using Dropbox to take confidential and proprietary business information, peer review materials and privacy protected patient information, and that Mr. Bledsoe had wiped clean a company Ipad to prevent its contents from being viewed. Mr. Bledsoe also modifying the Ipad's permissions to impede the investigation. *Id.* at *3.

The court granted summary judgment against Mr. and Mrs. Bledsoe on Baylor Frisco's breach of fiduciary duty claims for misappropriating thousands of confidential files pertaining to "peer review activities, business strategies, employee counseling and supervision, and proprietary programs" to their personal desktop computer via Dropbox and against the husband for his intentional deletion of the Ipad data. *Id.* at *11-12. The court noted that Baylor Frisco had been damaged as a result of their actions because it had incurred $218,000.00 in forensic investigation costs alone. *Id.* The court also ruled that the Bledsoes would not be able to discharge any indebtedness to Baylor Frisco by virtue of their eve-of-trial bankruptcy filings because their actions were fraudulent and malicious. *Id.* at *12. Finally, the court found that Baylor Frisco was entitled to reasonable attorney's fees and costs. *Id.* From January 1, 2012

through July 31, 2015, the medical center had incurred $1,142,979.00 in attorney's fees alone. *Id.* at *11.

B. RAMPING UP OR RIPPING OFF: THE RIGHT TO BEGIN PREPARATION TO COMPETE VS. UNLAWFUL USURPATION OF CORPORATE OPPORTUNITY.

Although an employee may not breach fiduciary duties to her employer, that same employer cannot prevent an employee from lawfully beginning to prepare a competing business. The simple fact that a moonlighting employee or a group of moonlighting employees, as in this paper's third scenario above, leaves a company and goes to work for the employer for which they were moonlighting or starting up their own competing business does not automatically give rise to unlawful activity.

1. WHAT CONSTITUTES PROPER PLANNING?

It is black letter law in Texas that it is permissible for an employee to prepare to go into direct competition with his employer prior to resigning from his soon-to-be former employer without breaching his fiduciary duty. *Rimkus Consulting Group, Inc. v. Cammarata*, 688 F.Supp. 2d 598, 669 (S.D. Tex. 2010). The Texas Supreme Court has suggested an employee owes no absolute duty of loyalty to an employer. *Johnson*, 73 S.W.3d at 201; *Harding Co. v. Sendero Res., Inc.*, 365 S.W.3d 732, 744 n26 (Tex. App.—Texarkana 2012, pet. denied). While directly competing with the employer is a breach of an employee's fiduciary duty, courts have found that *preparing* to compete is not. *Abetter*, 113 S.W.3d at 512 (concluding that forming the competitor entity and obtaining permits and insurance were mere preparations, particularly where employee disclosed his intention to form a competing company). The Texas Supreme Court has also approved of a decision that declined to find a fiduciary breach when the client was not asked to move its business while the employees were still employed, but where the client expressed interest in moving when "certain contingencies unrelated to the associates' formation of their own firm occurred." *Brewer & Pritchard*, 73 S.W.3d at 201 (citing *Bray v. Squires*, 702 S.W.2d 266, 271 (Tex. App.—Houston [1st Dist.] 1985, no writ).

Going beyond mere preparation to compete usually results in the usurpation of corporate opportunities. Courts usually treat usurpation of corporate opportunities as a breach of fiduciary duty claim or a claim for conversion. *In re Wilshire Homes Houston, Ltd.*, No. 10-32302-H2, 2013 WL 5162077 at *29 (S.D. Tex. Sept. 11, 2013). Simply put, a corporate fiduciary, such as an officer or director, has an obligation not to usurp corporate opportunities for her own personal gain. *Ritchie v. Rupe*, 443 S.W.3d 856, 883 (Tex. 2014); *see also, Ameripath, Inc. v. Hebert*, 447 S.W.3d 319, 340-41 (Tex. App.—Dallas 2015, pet. Denied) (holding that fact issues existed as to whether former employee breached his fiduciary duty to his former employer and usurped corporate opportunities when he negotiated new employment, took business from the former employer and facilitated the move of other employees of the former employer to the new employer).

Moreover, while mere preparations do not amount to a breach, an employee may breach his fiduciary duty if he fails to disclose those plans. *PAS, Inc. v. Engel*, 350 S.W.3d 602, 613-14 (Tex. App.—Houston [14th Dist.] 2011, no pet.) (stating that an employee "in dealing with his

principal on a matter involving his own self-interest that would limit his employer's contractual rights, [owes] a duty of full disclosure of all material facts"). An employee also may not mislead his employer about his intent to compete, particularly where the employer acts in reliance on the misleading acts or statements. *See Navigant*, 508 F.3d at 285. In *Navigant*, the court, applying Texas law, concluded that top employees breached their fiduciary duties by failing to disclose their preparations with a competitor to purchase the entire Dallas office's practice. *Id.* at 288. These mere preparations amounted to a breach particularly because the employees simultaneously committed the employer to a four-year Dallas office lease for space that would be unneeded following the purchase. *Id.*

Given Texas courts' interpretation of the scope of these duties, it seems likely that a court would not find an employee's work during employment for a *noncompetitor* to be a breach. However, there is one case affirming an injunction in part because the employee "failed to work normal hours and had low performance in the month preceding his move to FH1," and the "decreased performance was a result of the employee working for FH1." *FH1 Fin. Services, Inc. v. Debt Settlement Am*., Inc., 10-06-00167-CV, 2007 WL 2325652 (Tex. App.—Waco Aug. 15, 2007, no pet.). Though FH1 *was* a competitor, this same harm would arise even if the employee were working for a noncompetitor. An argument could be made that even an employee's work for a noncompeting company would "put his interests above that of [the employer] by a course of conduct designed to hurt [the employer]." *PAS*, 350 S.W.3d at 614.

Accordingly, based on the foregoing, the division manager/corporate director in this paper's third scenario likely does not breach a fiduciary duty by simply looking for office space for his new business. On the other hand, his solicitation of customers and vendors to move business over to his soon-to-be active startup likely constitutes a breach of fiduciary duty and a usurpation of corporate opportunities. Further, in the case of the moonlighting IT manager in this paper's second scenario, the IT manager could be subject to disciplinary measures if his productivity or job performance falters because of his consulting side business.

2. RECENT CASE LAW

- ***Heat Shrink Innov., LLC v. Medical Extrusion Tech.—Texas, Inc.*, No. 02-12-00512-CV, 2014 WL 5307191 (Tex. App.—Ft. Worth October 16, 2014, pet. denied) (mem. op.)**

While the majority of claims involving preparations to compete and breaches of fiduciary duties involve corporate officers or directors, this case illustrates that it is possible for an at-will employee to be liable for breach of fiduciary duty if that employee goes beyond merely just preparing to compete with his former employer. In *Heat Shrink Innovations*, the owner of a tubing manufacturing company, METT, hired Defendant Kevin Wolfe to work as the company's manager in 2006. *Id.* at *1. In early 2010, Wolfe began to seek out investors for a new company that would be a direct competitor with METT. *Id.* at *2. Wolfe also contacted at least one current METT customer and obtained a letter from that customer agreeing to transfer its business to Wolfe's new company. *Id.* Later that year, Wolfe hired two employees and took them to METT facility in Louisville without the knowledge of METTS' owners. *Id.* In February 2011, Wolfe incorporated his new business, Heat Shrink Innovations ("Heat Shrink"). *Id.* Two

months later, both he and his wife, METT's office manager, resigned from METT's employment to work at Heat Shrink. *Id.*

METT sued the Wolfes and Heat Shrink for, *inter alia*, misappropriation of trade secrets, breach of fiduciary duty, Texas Theft Liability Act violations, injunctive relief, unfair competition, unjust enrichment, tortious interference, civil conspiracy and conversion. *Id.* At trial, a jury found all three defendants liable and awarded METT $710,000 in damages. *Id.* The Wolfes and Heat Shrink appealed. *Id.* at *3.

On appeal, the Wolfes and Heat Shrink tried to persuade the Fort Worth Court of Appeals that because Wolfe was an at-will employee at METT he owned no fiduciary duty to METT and was able make preparations to form a competing business freely while still employed by METT. *Id.* at *10. The Court disagreed, stating that the issue was not whether an at-will employee may prepare to compete, but "what constitutes 'proper' planning and whether improper planning by an employee violates a fiduciary duty to his employer." *Id.* In no uncertain terms, the Court stated that if Wolfe used METT's confidential and proprietary information in preparing to compete, then he had taken steps beyond mere preparation and had breached his fiduciary duty to METT. *Id.* at *11. Ultimately, however, the trial court reversed the award of $600,000 in lost profits because of an evidentiary issue. *Id.* at *12.

C. CONSPIRACY, INTERFERENCE AND DISCLOSURE, OH MY.

1. CIVIL CONSPIRACY

In the third scenario above, the group of employees arguably acted in concert with the division manager/corporate officer to breach his fiduciary duty to their employer and likely committed conspiracy as well.

To determine whether moonlighting or departing employees conspired against their former employer depends on whether they participated in an underlying tort. *Homoki v. Conversion Servs., Inc.*, 717 F.3d 388, 402 (5th Cir. 2013). The derivative tort of civil conspiracy is a "combination by two or more persons to accomplish an unlawful purpose or to accomplish a lawful purpose by unlawful means." *Ameripath, Inc. v. Hebert*, 447 S.W.3d 319, 343 (Tex. App.—Dallas 2015, pet denied) *quoting, Firestone Steel Prods. Co. v. Barajas*, 927 S.W.2d 608, 614 (Tex. 1996). In Texas, a civil conspiracy claim can be based on a breach of fiduciary duty. *Homoki*, 717 F.3d at 403-04.

2. TORTIOUS INTERFERENCE WITH BUSINESS RELATIONS

The same conspiring employees above may have also conspired with their division manager to tortiously interfere with their employers' business relations—specifically its contracts with its current customers and vendors.

The elements of a claim for tortious interference with business relations are "(1) a reasonable probability that parties would have entered into a business relationship; (2) the defendant either acted with a conscious desire to prevent the relationship from occurring or knew

the interference was certain or substantially certain to occur as a result of the conduct; and (4) the plaintiff suffered actual harm or damages as a result of the defendant's interference." *Dumans v. Fort Bend Cty., Tex.*, No. 4:08-cv-01359, 2009 WL 7808946 at *6 (S.D. Tex. June 29, 2009). To establish liability, a plaintiff has to prove harm from defendant's conduct that was either independently tortious or unlawful. *Ameripath*, 447 S.W.3d at 341-42. Independently tortious means conduct that violates some other recognized tort duty according to the Texas Supreme Court. *Id.*; *Wal-Mart Stores, Inc. v. Sturges*, 52 S.W.3d 711, 713 (Tex. 2001). Finally, while an intent to injure is not required to prove liability, a plaintiff does have to show that the tortfeasor wants to cause the consequences of his action or that the tortfeasor believes that those consequences are certain to result from his action. *Lewallen v. Conmed Corp.*, 261 Fed. Appx. 704, 707 (5th Cir. 2008).

Tortious interference claims in the employment context are not limited to claims in which employees moonlighting for another business or their own startup interfere with their primary employer's customer or vendor contracts for their own gain. In fact, situations do exist in which the competing business can tortiously interfere with the primary employer's contractual relationships with its own at-will employees. The Southern District of Texas denied a motion to dismiss a tortious interference claim last year on the basis that an oilfield services provider had validly stated that a competitor had tortiously interfered with the confidentiality, non-solicitation and non-compete agreements that the oilfield services provider had with certain at-will employees. *Schlumberger Tech. Corp. v. Coil Tubing Sols., LLC*, 103 F.Supp.3d 846, 851 (S.D. Tex. 2015). The district court stated that, in general, at-will employees may be "lured away without consequence," but not when wrongful conduct is involved. *Id.* at 850. In this case, the wrongful conduct alleged was the breach of confidentiality, non-compete and non-solicitation agreements that occurred when the competitor recruited dozens of employees in Texas, North Dakota and Louisiana to leave their jobs to go to work for the competing business. *Id.* at 849-851. According to the court, "[w]ith respect to tortious interference with employee contracts, including the employees' ongoing breaches of non-competition, non-solicitation, and/or confidentiality agreements under the laws of the various states, the Court finds that the pleadings are sufficient to raise a right to relief above the speculative level…." *Id.* at 854; *see also, Totino v. Alexanders & Assocs., Inc.*, No. 01-97-01204-CV, 1998 WL 552818 at *9-10 (Tex. App.—Houston [1st Dist.] Aug. 20, 1998, no pet.) (not designated for publication) (holding that trial court did not abuse its discretion in granting a temporary injunction against competitor to stop the breaching of employment contracts between the employer and its current employees).

3. Is Disclosure of Confidential Information Inevitable or Probable?

Finally, the conspiring group of employees and their division manager, and even the game designers in the first scenario and the IT manager in the second scenario of this paper, may commit the tort of inevitable or probable disclosure even if they had no intention of doing so.

Some states have recognized a common law claim based on the theory that, in certain situations, an employee in possession of his employer's confidential information who undertakes an endeavor so similar to his employer's business will inevitably disclose the former employer's confidential information to his new employer. *See, e.g., McGowan & Co., Inc.* 93 F. Supp.3d

624, 646 (S.D. Tex. 2015) (noting that Ohio courts safeguard an employer's trade secrets from a former employee's potential misuse under its "inevitable use" or "inevitable disclosure" doctrine).

Texas state and federal courts, on the other hand, have not yet met the doctrine with open arms. Rather, courts have acknowledged the doctrine's existence, but, despite some occasional application, widespread acceptance has not occurred. Simply put, over the past 20 years, Texas has refused to adopt a bright- or hard-line stance on whether or not the inevitable disclosure doctrine is alive and well in the state. *See, e.g., Conley v. DSC Comm. Corp.*, No. 05-98-010510CV, 1999 WL 89955 at *4-8 (Tex. App.—Dallas Feb. 24, 1999, no pet.) (not designated for publication) (reaffirming prior ruling that an employee may be enjoined from using confidential information when disclosure is "probable" and stating that evidence of an employee's misconduct, the apparent need for the confidential information, similarity between the employee's former and new positions, the new employer's lack of effort to protect the former employer's information and the existence of a noncompetition agreement may be used to support such injunctive relief); *Cardinal Health Staff Network, Inc. v. Bowen*, 106 S.W.3d. 230, 243-44 (Tex. App.—Houston [1st Dist.] 2003, no pet.) (noting that no Texas case had expressly adopted the inevitable disclosure doctrine and declining to adopt *Conley's* probable disclosure doctrine because no evidence of any employee taking or using their former employer's confidential information existed); *M-I LLC v. Stelly*, No. H-09-cv-01552, 2009 WL 2355498 at *7 (S.D. Tex. July 30, 2009) (stating that Texas courts have not "expressly adopted" the inevitable disclosure doctrine and, similar to *Conley*, refusing to apply the doctrine or any modified version due to the lack of evidence that the former employee had taken or would use any confidential information); *see also, M-I LLC v. Stelly*, 733 F.Supp.2d 759, 770 n3 (S.D. Tex. 2010) (declining to consider if pleading the inevitable disclosure doctrine meets the requirements of the Federal Rule of Civil Procedure 12(b)(6)); *St. Jude Med. S.C., Inc. v. Janssen-Counotte*, No. A-14-CA-877-SS, 2014 WL 7237411 at *16 (W.D. Tex. Dec. 17, 2014) (stating that the record contained no evidence of "a substantial likelihood of probable or inevitable disclosure" but that to show this likelihood requires more than the fact that the employee is now president of a competitor and possesses trade secrets of the former employer). *But see Rugen v. Interactive Bus. Sys.*, 864 S.W.2d 548 (Tex. App.—Dallas 1993, no writ) (where an employee possessing his former employer's confidential information left to compete against the employer, temporary injunction prohibiting solicitation of former employer's customers proper on the grounds that the employee was "in possession of [the] confidential information and is in a position to use it."); *Mabrey v. Sandstream, Inc.*, 124 S.W.3d 302, 319 n. 44 (Tex. App.—Fort Worth 2003, no pet.).

The recent adoption by Texas of the Texas Uniform Trade Secret Act (TUTSA) further complicates this analysis. Though TUTSA does not directly address the inevitable-disclosure doctrine, the inclusion of "threatened" misappropriation as a basis for injunction adds fuel to the inevitable-disclosure fire. Other jurisdictions have treated the language as interchangeable with the inevitable-disclosure doctrine.[1]

[1] Richard F. Dole, Jr., Permanent Injunctive Relief for Trade Secret Misappropriation Without an Express Limit Upon its Duration: The Uniform Trade Secrets Act Reconsidered, 17 Boston Univ. J. SCI. & TECH. L. 173 (Summer 2011) (citing *PepsiCo., Inc. v. Redmond*, 54 F.3d 1262 (7th Cir. 1995)).

Defendants faced with claims of "threatened" misappropriation under TUTSA may find it difficult to avoid an injunction if they have possession of trade secrets and are working in a field where the trade secret would be useful. Is such a situation "threatening"? Probably—but in the first case to address this question since TUTSA's adoption, Judge Sparks rejected this argument in one of the first cases applying TUTSA, noting that a former Vice President for a medical-device company should not automatically be considered a "threat" simply because she now works for a competitor. *St. Jude Medical S.C., Inc.*, 2014 WL 7237411 at *14. In declining to enjoin her from working in her new position as president of the competing medical-device company, the court reasoned that under these grounds for an injunction:

> If accepted, ***non-disclosure obligations would morph into non-compete agreements.*** Janssen is already prohibited by law from disclosing any of the trade secrets she learned while at [the former medical-device company]. To show a substantial likelihood of threatened disclosure, [Plaintiff] must establish more than the facts Janssen is the president of a competitor and possesses trade secret information.
>
> *Id.* (emphasis added).

The law thus remains unsettled on whether an injunction may be granted against competing former employees when they have not actually misappropriated trade secrets. Former employers in trade-secret cases should continue to rely on *Rugen* and *Mabrey*. Those cases remain persuasive even after TUTSA's enactment in light of the statute's explicit inclusion of "threatened" misappropriation as a grounds for injunction. *See* Tex. Civ. Prac. & Rem. Code § 134A.003(a). Defendants, though, should focus on public-policy interests against restraints of trade. *See* Alex Harrell, *Is Anything Inevitable*, 76 Tex. B.J. 757, 760 (Sep. 2013). The Defendants' arguments should harvest the reasoning from *St. Jude*, and other cases like it, that have concluded that an injunction without a noncompetition agreement is inappropriate where the former employee has done no wrong.

In October 2015, the Fifth Circuit Court of Appeals weighed in on the viability of the inevitable disclosure doctrine under Texas law. The case involved a dispute brought by former executives of an Oklahoma-based bank against a Texas-based acquiring bank. *Cardoni v. Prosperity Bank*, 805 F.3d 573 (5th Cir. 2015). As a condition its acquisition of F&M Bank and Trust Company, Prosperity Bank required that 35 senior-level F&M employees sign employment contracts which contained, among other things, nondisclosure, noncompetition and nonsolicitation provisions as a condition of its acquisition of an Oklahoma bank. *Id.* at 577-78. Within months of the merger, the bankers claimed that their pay, benefits and working conditions were worse than before the merger. *Id.* at 578. Litigation ensued with actions filed in Texas and Oklahoma state courts, which were then removed to federal court and consolidated in the Southern District of Texas. *Id.* In September 2014, the bankers terminated their employment and went to work seven miles away at a rival bank. *Id.* Prosperity applied to the district court twice for injunctive relief to compel compliance with the restrictive covenants in the employment agreements but was unsuccessful both times. *Id.* at 578-79. In particular, the district court concluded that the nondisclosure provision was likely enforceable but that Prosperity had failed to show a likelihood of success or irreparable injury because it made only a

speculative showing that its confidential information had been disclosed or used. *Id.* at 579, 589-90. Interlocutory appeals to the Fifth Circuit followed. *Id.* at 579.

In light of the district court's factual findings on lack of disclosure, Prosperity argued on appeal that Texas law recognizes inevitable disclosure—that an employee will be hard-pressed to prevent disclosure of his former employer's trade secrets at his new employment regardless of his intentions or any desire not to do so. *Id.* at 580. The Fifth Circuit distinguished the three cases cited by Prosperity from the 1970s, 80s and 90s and looked to more recent case law, including *Cardinal Health Staffing Network, M-I, L.L.C.* and *Conley*, to affirm the lower court's determination that "individualized assessment of whether disclosure had occurred or was likely to occur" was not clear error. *Id.* at 590. In short, the Fifth Circuit held that no "blanket" inevitable or probable disclosure doctrine exists in Texas to protect the likely use of confidential and proprietary information, but it did leave the door open to its application as wholly dependent on the factual underpinnings of a case. *Id.* at 589-90.

IV. A MATTER OF CONTRACT

In addition to common law and statutory remedies, an employer also has a number of contractual provisions in its arsenal to prevent an employee's unauthorized use of the employer's confidential and proprietary information and to protect ideas developed during the employment relationship. Two primary methods that come into play with the moonlighting employee are covenants not to compete and an assignment of inventions agreement.

A. PERFECTING THE NON-COMPETITION CLAUSE

One of the most common contractual restrictions, if not the most common, but hardest to enforce, is the covenant not to compete, which in Texas is governed by statute. *See* Texas Bus. & Com. Code §15.50 *et seq*. Section 15.50(a) provides that a covenant not to compete is enforceable "if it is ancillary to or part of an otherwise enforceable agreement at the time the agreement is made" to the extent that it contained reasonable time, geographic and scope of activity limitations "that do not impose a greater restraint than is necessary to protect the goodwill or other business interest…." In the employment context, the enforceability of a covenant not to compete has been addressed by the Texas Supreme Court several times in the past 22 years.

1. BACKGROUND ON THE EVOLUTION OF THE NON-COMPETE

In 1994, in *Light v. Centel Cellular of Texas*, 883 S. W.2d 642 (Tex. 1994), the Texas Supreme Court determined that in order for a noncompetition agreement to be ancillary to an otherwise enforceable agreement, it could not be conditioned on at-will employment or a promise that was dependent on a continued period of the at-will employment relationship. 883 S.W.2d at 644-45. The Court reasoned that a covenant not to compete that did so was unenforceable because the person making the promise could avoid performance by terminating the employment at any time and for any reason. *Id.* The court noted that the promise to provide confidential information by the employer in exchange for the employee's promise not to disclose that information could be such an enforceable promise. *Id.* at 647 n14. The *Light* opinion

resulted in much litigation as to what "ancillary to an otherwise enforceable agreement" actually means.

In 2006, the Texas Supreme Court revisited its *Light* opinion to determine "whether an at-will employee who signs a non-compete covenant is bound by that agreement if, at the time, the agreement is made, the employer has no corresponding enforceable obligation." *Alex Sheshunoff Management Services, L.P. v. Kenneth Johnson and Strunk & Associates*, 209 S.W.3d 644, 646 (Tex. 2006). The *Sheshunoff* court determined that, in contrast to *Light*, a noncompetition covenant only needed to be ancillary to or part of the agreement at the time the agreement was made. *Id.* at 651. The Texas Supreme Court further reasoned that an enforceable, unilateral contract forms when the employer simply performs the promise that was originally illusory when the employer made it. *Id.*

The Texas Supreme Court tweaked its analysis three years later in *Mann Frankfort Stein & Lipp Advisors, Inc. v. Fielding*, 289 S.W.3d 844 (Tex. 2009). In *Mann*, the Court held that an employer is not required to make an express promise to provide confidential information in all cases. *Id.* at 845. The Court stated:

> If the nature of the employment for which the employee is hired will reasonably require the employer to provide confidential information to the employee for the employee to accomplish the contemplated job duties, then the employer impliedly promises to provide confidential information and the covenant is enforceable so long as the other requirements of the Covenant Not to Compete Act are satisfied.

Id. at 845.

2011 brought the fourth major opinion by the Texas Supreme Court on a covenant not to compete in the employment context. In *Marsh USA, Inc. v. Cook*, the court expanded the "ancillary" requirement to allow for employer consideration other than consideration in the otherwise enforceable agreement giving rise to the employer's interest in restraining the employee from competing. 354 S.W.3d 764, 775-76 (Tex. 2011). The court held that the relationship between the employer's legitimate interest being protected and the otherwise enforceable agreement need only be "reasonable." *Id.* In *Marsh*, the court found that a noncompetition agreement linked to an employee stock option agreement was reasonably related to the company's interest in protecting its own goodwill. *Id.*

Thus, while 20 years ago it would have been difficult to enforce the covenants not to compete for the conspiring employees in this paper's introductory scenarios, the continuing legal evolution of noncompete jurisprudence highlights the relative ease employers now have when they seek to enforce a covenant not to compete today.

2. RECENT CASE LAW

a. *Premier Polymers, LLC v. Wendt*, No. H-15-1812, 2015 WL 4434551 (S.D. Tex. July 17, 2015)

In this case, an account manager signed a Confidentiality and Non-Solicitation Agreement with his employer in which he agreed that he would not disclose confidential information or to solicit customers. *Id.* at *1. After the account manager left Premier Polymers to work for a competitor, Premier Polymers discovered that the employee had been forwarding pricing information to his personal email account and recruiting customers as well as moonlighting for a third company while employed by Premier Polymer. *Id.* Premier Polymer filed suit and the state court issued a temporary restraining order. The court held that the 18-month restriction was reasonable and that the non-solicitation provision was part of an otherwise enforceable agreement. *Id.* at *3-5. Premier Polymers argued that the court should toll the injunction period so that it started from the date of injunction but the court determined that it began on the date that he started working for the competitor. *Id.* at *5.

b. *Hunn v. Dan Wilson Homes, Inc.*, 789 F.3d 573 (5th Cir. 2015)

In *Hunn v. Dan Wilson Homes, Inc.*, the Fifth Circuit affirmed the district court's refusal to enforce a non-compete covenant (also a customer non-solicit provision similar to the one in *Premier Polymers*, supra) on the basis that the agreement was not ancillary to any otherwise enforceable agreement. 789 F.3d at 586. The appellate court held that because the former employee never expressly promised not to disclose confidential information, then "there was no corresponding implied promise to provide confidential information—and therefore, there was no agreement regarding confidential information" to which the non-compete covenant could be ancillary. *Id.*

3. WHAT TO INCLUDE AND WHAT TO AVOID WHEN DRAFTING A NON-COMPETE

Should an employer determine that it is in the company's best interest to ask its employees to sign post-employment covenants not to compete, it is critical to review recent case law because the landscape of restrictive covenants is ever-shifting (as the above cases from the past 22 years demonstrate). When drafting an agreement containing these restrictive covenants, an employer should consider including sections on attorney's fees, forum selection and choice of law. Additionally, a strong noncompetition covenant will integrate and incorporate by reference any other agreement that relates to the covenant not to compete, such as a nondisclosure agreement or an inventions assignment agreement, as discussed, in the next section of this paper.

Conversely, it is imperative to avoid imposing limitations that are unreasonable in terms of the restrictions placed on scope of activity, geography and time limitation. For example, a court will likely rule against an employer in most situations if that employer attempts to enforce a covenant not to compete that seeks to prevent a former employee from working for a competitor for more than two years. Further, although a court may blue pencil or reform the restriction to be reasonable, rather than strike it completely, the result is that an employer will lose the ability to collect damages beyond injunctive relief for breach of the covenant from the employee. TEX. BUS. & COM. CODE §15.51(c).

B. DEFINING THE SCOPE, BREADTH AND REACH OF AN EFFECTIVE INVENTIONS CLAUSE.

What about the self-taught game designers who created their own games in their spare time in the first scenario of this paper? These individuals signed a basic inventions assignment agreement, but never informed their employer of their inventions. Questions arise as to who owns the resulting games; who should get the profits; and whether it is in the best interest of the employer to even claim ownership in the long run.

It is commonplace in technology industries that employers require their employees to agree to an assignment of inventions provision. In general terms, an inventions assignment provides that an employee agrees to assign his rights, interest in, and ownership of all inventions relating to the employer's business or resulting from the employee's work for the employer during the period of employment. If an employee is moonlighting, it is not always clear who owns the rights to any resulting inventions or intellectual property. Was the invention developed on-site and/or during work hours, or was it done with the employee's own equipment on his own time? Did the employee utilize special skills and confidential information that he would not have had but for his employment with his primary employer? Who has the subsequent ability to assign the rights to the invention, the employee or the employer? Depending on the language of the inventions assignment agreement, most, if not all, of these questions can be answered and subsequent disputes over those inventions may be avoided.

1. PRE-INVENTION ASSIGNMENTS TO THE EMPLOYER

Texas courts have endorsed contractual agreements regarding the assignment of inventions by an employee to his employer. Typically, such a provision will contain language that is reasonable rather than unconscionable.

The importance of an effective invention assignment clause cannot be overstated and is by no means child's play. For example, in April 2005, a small privately held toy company, MGA Entertainment, sued toy giant Mattel over a line of children's dolls. MGA maintained that Mattel had infringed upon MGA's Bratz doll line. Mattel countered that Mattel owned the rights because the doll designer, Carter Bryant, worked for Mattel at the time he came up with the idea for Bratz and was working under an employment agreement with an inventions assignment clause. After much legal wrangling, including an appeal and remand for a new trial, a jury concluded that the idea of the Bratz doll was not owned by Mattel because of the language in the employment contract. Specifically, the contract defined the term "invention" to include discoveries, improvements, processes, developments, designs, knowhow and data computer programs, *but not ideas.* The jury ultimately awarded MGA $88.5 million dollars for their claims against Mattel.

2. RECENT CASE LAW

a. *DDB Technologies, L.L.C. v. MLB Advanced Media, L.P.,* 676 F.Supp. 2d 519 (W.D. Tex. 2009)

This case illustrates that an employer's actions regarding a written inventions assignment are just as important as the inventions assignment itself. In this case, Schlumberger Technology Corporation's Schlumberger-Doll Research Center Division employed a computer scientist who signed a Patent and Confidential Information Agreement ("Agreement") in connection with his employment. In the Agreement, the employee agreed, *inter alia*, to grant and assign his "entire right, title and interest" to all "ideas, inventions and improvements" which related "in any way to the business or activities of [the] Company." *Id.* at 521. During his employment, the computer scientist and his brother submitted applications for four patents—one issued during his Schlumberger employment and the other three after he left the company. *Id.* at 521-22. The computer scientist and his brother then executed patent assignments to DDB, which, coincidentally, was jointly owned by the brothers to commercialize and develop their inventions. *Id.* DDB sued a third entity, MLB, for patent infringement and nearly two years into the lawsuit, Schlumberger, a nonparty to the action, assigned its rights in the four patents to MLB, "including a retroactive license to practice the patents from the dates of their issuance." *Id.*

MLB argued that the patents fells within the ambit of the Agreement and thus the computer scientist's right, title and interest were automatically assigned to Schlumberger. *Id.* DDB, on the other hand, claimed that the patent did not fall within the Agreement's scope and thus, Schlumberger never had title or right to the patents. *Id.*

Relying in part on evidence that the computer scientist had admitted in a letter to his brother that there was a relationship between the patent and his work at Schlumberger, the court held that under a broad reading of the Agreement, the patents were accordingly "suggested by or related to" the computer's scientists work at Schlumberger. *Id.* at 531. However, in light of Schlumberger's actions following the computer scientist's disclosure during his employment of the project that led to the patents, the Court held that the breadth of the Agreement's language was ambiguous and at odds with Schlumberger's construction. Specifically, the court determined that Schlumberger never intended to construe the Agreement as broadly as it was written. *Id.* at 532. Using the testimony of Schlumberger's in-house counsel, the computer scientist's supervisor and his group leader, the district court held that, despite the broad Agreement, Schlumberger took a narrower view and believed that an employee's invention related to the company's business if the invention had a "practical benefit" to Schlumberger. *Id.* at 532. The Court stated that, "[i]f the employee invention appeared to have only benefit to the employee, Schlumberger construed the Agreement to exclude the invention." *Id.* As such, the Court ruled that the computer scientist's invention and the patents were not covered by the Agreement and that DDB had legal title to those patents. *Id.*

b. *Adaptix, Inc. v. Alcatel-Lucent USA, Inc.*, No. 6:12cv22, No. 6:12cv369, --- F.Supp.3d ---, 2015 WL 5913195 (E.D. Tex. Sept. 22, 2015)

Adaptix is a good example of the inventions-ownership issues faced by companies who allow their employees to hold other employment while still working for the primary employer. In *Adaptix*, a professor was employed by the University of Washington ("UW") in 1998. *Id.* at *4. At the onset of his employment, he signed an employment agreement that stated that the university has a "valid interest" in his discovery or invention of patentable items and also

required him to disclose all discoveries and inventions to the school as well as assign those inventions to UW. *Id.*

Specifically, the employment agreement provided:

> As a condition of my employment with the University of Washington, I hereby agree to disclose to the University all discoveries and inventions made while I am employed by the University and assign to the University all discoveries and invention in which the University has an interest.

Id. at *6.

In 2000, the professor requested and was granted a partial leave of absence and in October 2000 he created two inventions for which patents were issued. *Id.* In June 2001, the professor took a partial leave of absence from UW to assist Adaptix' predecessor, Broadstorm, develop 4G broadband wireless networks. *Id.* In June 2002, the professor requested and was granted another part-time leave to transition from Broadstorm back to UW full time. *Id.* at 5. In approving the request, the electrical engineering department chair recommended conditioning that approval on the basis that "all new intellectual property developed by [the professor] during the Fall 2002 quarter be considered to be UW intellectual property." *Id.* Finally, in 2007 the professor requested a sabbatical for 2008-2009 school year so that he could conduct research at the Chinese Academy of Science and at Intel Communication Technology Lab to broaden his research activities. *Id.*

Adaptix filed an infringement action lawsuit regarding the patents that covered a network comprising subscriber units and base station. *Id.* at *1. Adaptix ultimately filed a motion for partial summary judgment and argued that, based on the course of conduct between the professor and UW that the school "had expressed no interest in the Adaptix patents" and, thus, there was no automatic assignment to the university. *Id.* Defendants argued, among other things, that the patents were invalid under 35 U.S.C. § 103(c) based on prior art. In support of their arguments, the defendants claimed that the professor was a UW employee while he also consulted for Broadstorm and that his employment agreement and the inventions provision remained in effect during his partial leaves of absence. *Id.* at *6.

The district court approved the magistrate judge's report and recommendation that Adaptix' motion for summary judgment be denied on the basis there was a fact issue as to whether the professor's claimed inventions were automatically assigned to UW and not Broadstorm. *Id.* The district court noted that allowed the professor to work at Broadstorm but never claimed an interest in that work, and also considered the employment agreement's language that the school had a "valid interest" in the professor's discovery or invention of patentable items. *Id.* at 2. The magistrate judge relied upon the fact that the professor was expected to continue his UW research duties during the same time period that claimed the inventions were conceived. *Id.* As such, it was impossible for the court to preclude summary judgment for Adaptix.

3. DEFEND TRADE SECRETS ACT

Congress recently passed the Defend Trade Secrets Act "(DTSA") which includes a requirement for all employers to also provide a notice-of-immunity to employees and contractors "in any contract or agreement with an employee that governs the use of a trade secret or other confidential information."

The DTSA will for the first time federalize a civil right of action for employers, contractors, and companies who pursue trade secret misappropriation claims. The legislation expressly reflects that Congress believes trade secret theft harms both the companies that own the trade secrets and its employees. The remedies for a violation of DTSA include injunctive relief and several forms of monetary damages measured by the actual loss caused by the misappropriation and any unjust enrichment not addressed in computing damages for actual loss, or in exceptional cases by a reasonably royalty. One interesting aspect of the DTSA is ex parte civil seizure. The law provides a mechanism for law enforcement officials to seize property necessary to preserve evidence or prevent the propagation or dissemination of the trade secret at issue in extraordinary circumstances. DTSA claims must be brought within three years after the date the misappropriation is discovered or should have been discovered.

The DTSA also provides limited whistleblower immunity to employees who disclose trade secrets in confidence to government officials or to an attorney and solely for the purpose of reporting or investigating a suspected violation of law. Under the provision, employers are required to provide notice of the immunity "in any contract or agreement with an employee that governs the use of a trade secret or other confidential information" or refer to a policy document rather than restating the entire immunity provision in each agreement. An employer who fails to provide this notice will not be able to collect exemplary double-damages or attorney fees in a lawsuit against an employee suspected of violating the DTSA.

4. MODEL LANGUAGE

Based on the *DDB* and *Adaptix* cases above, it is imperative that any invention assignment agreement be clear and concise and not so overreaching that it creates a gray area that ultimately may tie up employers and employees in costly litigation. This need for precision and specificity is even more necessary when an employer allows its employees to moonlight or pursue other outside projects. Further, an employee must be diligent in enforcing an inventions clause and taking steps to ensure that it continues to protect its protectable interests.

The following is sample model language of an inventions assignment provision that can be used and adapted to an employer' business and particular coverage needs.

> *1.0 IP that you created, owned, or had an interest in before you were hired by the Company remains yours ("Prior Intellectual Property" or "Prior IP"). Subject to the limitations in this agreement, you have a continuing right to develop and exploit Prior IP using non-Company Resources and non-Confidential Information.*

To avoid any future confusion or dispute, you should provide a list of Prior IP to the Company's IP Committee (or Human Resources department) within ten (10) business days of signing this agreement. IP should be described in such a way that it can be easily identified or distinguished. If there is any dispute about IP ownership, the Company will be deemed the rightful owner unless you can provide conclusive written evidence of Prior IP. Such notice as is described in this Section or other verifiable records such as government registration, a distribution to a third party, or repository commit dates may serve as evidence of ownership.

Subject to the limitations in this agreement, new IP that you create while you are employed by the Company using only non-Company Resources is also yours, and you have a right to develop and exploit it using non-Company Resources.

a. Notice. You will promptly notify the Company's IP Committee whenever you start any new project that involves the creation or development of IP. The proposed project, licensing, and resulting IP must be described in enough detail to allow the Company to understand the scope, purpose, timeline, and any known conflicts. You must also promptly notify the IP Committee if the nature or scope of an existing project changes significantly.

b. No Subject Matter Conflicts. You will not knowingly participate in the development of IP related to a current or planned Company product, service, technology, or offering without prior authorization from the Company's IP Committee. Knowledge of a product, service, technology, or offering includes knowledge of perceived gaps or opportunities for add-ons, extensions, improvements, complementary technologies, or value-added services. If you have any question as to whether something is in the scope of the Company's business activities, then this clause applies. The Company's IP Committee must specifically approve in the development of any possibly conflicting development.

c. Authorization. The Company understands that you may not know the full scope of the Company's business activities, and so a project may pose an inadvertent subject matter conflict. To address the possibility of inadvertent subject matter conflicts, the IP Committee will have sixty (60) days (the "Notice Period")

to provide an initial response to your request. If the Committee replies with clear words of authorization, you may participate in the project within the scope and purpose of your notice. If the Committee provides a clear but qualified authorization, you may only participate in the project within the limits and guidelines provided in the response. If no response is provided within the Notice Period, your participation is deemed to be authorized within the scope and purpose of your notice. If the Committee responds to your notice with anything other than clear words of authorization, you may not participate in the project.

1.1 Ownership of Company IP. Any IP created by you using Company Resources belongs to the Company ("Company Intellectual Property" or "Company IP"), whether or not the IP is related to your specific job duties. By signing this agreement, you hereby assign and promise to assign all right, interest, and title to all Company IP to the Company. In addition, you promise to cooperate with the Company in securing and protecting our rights in Company IP that is created by you, whether or not you continue to be employed by the Company, and you hereby appoint the Company as your limited agent for that purpose.

1.2 Release of Company IP. The Company's IP Committee is the only entity authorized to establish new licensing terms for any piece of Company IP, including the open sourcing or other release of IP. If you believe that your work would be beneficial to release as open source or otherwise license, send an email describing the suggestion to the IP Committee.

1.3 Works for Hire. To the extent permitted by applicable law, work covered by this Section is a work made for hire. If you are employed within the state of California, the Company's ownership rights under this section do not apply to those inventions that fall under California Labor Code section 2870, and you agree to inform the Company in writing about any inventions that you believe meet this code section.

If the work is not a "work made for hire," then you hereby and irrevocably assign and promise to assign all right, title and interest in the work, to the fullest extent allowed by the intellectual property laws of the United States and the laws of any other country in which the work is made, used, performed, imported,

> *exported, or sold. You agree to cooperate with the Company in signing documents, providing information, and doing other things needed to evidence the Company's ownership of the work, to transfer rights to, and/or to patent any invention or discovery, both before and after the end of your employment with the Company, with additional reasonable compensation if substantial assistance is required from you after your employment with the Company ends. You hereby appoint the Company as your agent and attorney-in-fact to act only on your behalf to sign documents and do other things required by this Agreement.*

A proper inventions assignment agreement should include any relevant state laws, which can be attached as an exhibit and incorporated by reference. Further, the agreement should include a statement that if any provision is found to be inconsistent with applicable law, the parties agree that it is their intention that the agreement be deemed modified to be consistent with applicable law and enforced as modified.

C. POLICIES ON MOONLIGHTING

Finally, it is important for employers to evaluate both the need and the desire to regulate potential moonlighting from its workforce. Should a company determine that moonlighting should be addressed with its employees, then it will likely want to draft a written moonlighting policy to include in its employee handbook as well as in any employment agreement signed by new employees—a policy that strikes the correct balance between the employer's legitimate, protectable business interests and an employee's right engage in the lawful off-duty conduct. An overreaching policy could lead to a violation of the law in some states. For example, California law makes it difficult to enact a company-wide, outright ban of moonlighting activities. *See* CAL. LAB. CODE §96(k) (stating that the Labor Commission may pursue claims for wage loss resulting from "demotion, suspension, or discharge from employment for lawful conduct occurring during nonworking hours away from the employer's premises"). Conversely, an under reaching policy may allow for an employee to moonlight in a manner that could affect adversely the company's bottom line.

Accordingly, an effective moonlighting policy will prohibit an employee from engaging in other work that creates a conflict of interest with the primary employer, such as working for a competitor or a client. An effective policy will also state that all employees will be held to the same performance and attendance standards to deter an employee from focusing on her supplemental work while at her primary job. This policy should also contain a provision that an employee notify the employer of his intent to work another job as well as provide specific information about the work for the employer to determine if a conflict exists.

Case in point: *Kaup v. Texas Workforce Comm.*, 456 S.W.3d 289 (Tex. App—Houston [1st Dist.] 2014, no pet.). Global Security Consulting hired David Kaup as a security compliance officer in July 2010. *Id.* at 292. On his application Kaup indicated that he had been unemployed since May 2010. *Id.* In March 2012, Kaup also signed an employee handbook acknowledgement form indicating his receipt and responsibility to read and comply with its

contents. *Id.* The handbook contained a moonlighting policy that if an employee decided to seek additional employment, then the employee should inform their manager to ensure that no conflict with Global Security's business interests exists. *Id.* at 292-93. Later than year, Global Securities anonymously placed a job listing for a security manager online and, subsequently, received an application from Kaup's personal email account in addition to a copy of his resume which was sent during work hours. *Id.* On his resume, Kaup stated that he had been a consultant to two other security companies since May 2009 and March 2012 respectively. *Id.* As a result, one week later, Global Security terminated Kaup's employment for job-hunting when he should have been working and for having obtained additional employment without company approval. *Id.*

Kaup applied for unemployment with the Texas Workforce Commission ("TWC") and was denied based on misconduct connected with work for violating the moonlighting policy. *Id.* Kaup appealed the decision to the TWC Appeal Tribunal and lost. *Id.* Kaup then filed a petition for review with the district court which entered a final judgment against him because substantial evidence existed to support the TWC decision. *Id.* Kaup appealed that decision to the Houston Court of Appeals, First District. On appeal, he argued, among other things, that the moonlighting policy was unreasonable and an "unconscionable attempt to control his off-duty time." *Id.* The appellate court ruled that Kaup had not met his burden to establish that the policy was unreasonable. Specifically, the court stated that in Texas it is permissible for employers to limit their outside employment to avoid conflicts of interest. The court also noted, "the Global Security policy does not wholly prohibit outside employment but merely requires employees to disclose and obtain approval of the outside employment in light of the company policy aimed at avoiding conflicts of interest in security-sensitive positions." *Id.*

The following is a sample conflicts of interest policy that may be used by an employer who desires to enact a moonlighting policy with regard to its employees. This example is not state specific, so it is imperative to check to see if any state laws exist that relate to moonlighting and the regulation of off-duty conduct.

POLICY ON CONFLICTS WITH COMPANY INTERESTS

It is the company's policy that all employees, as well as officers and directors, will avoid any actual or apparent conflict between their own personal interests and the company's interests. It is also the company's expectation that all employees, officers and directors will devote their time and attention solely to the company's business during their working hours and not outside activity. All employees, officers and directors are expected to refrain from engaging in any outside employment that competes with the business interests of the company or from diverting business opportunities from the company for their own personal gain or the gain of others by virtue of their employment with the company. Employees, officers and directors are also prohibited from using corporate assets as well as the company's confidential and proprietary information (as that term is defined in the

> *Nondisclosure of Confidential and Proprietary Information Agreement to which all employees, officers and directors are bound) for their own personal gain, the gain of others or in connection with any outside employment. Although the company does not prohibit outside employment, employees, officers and directors are required to inform and receive approval from their immediate manager and human resources prior to engaging in any outside employment so that any conflict with the company's business interests can be avoided.*

V. CONCLUSION

The days when moonlighting simply meant an office assistant taking a few shifts as a waiter during the evenings so that he can make a few extra dollars are long gone. Today, it is the IT manager consulting with his own client base before and after work. It is the game designers who teach themselves game design and coding so that they can create their own profitable games. It is the group of employees working off the clock to undertake the lawful, and sometimes unlawful, clandestine steps with their division manager to form a competing company.

Perhaps in step with the times, more and more high-tech companies are beginning to relax strict rules against employee moonlighting and conflicts of interest. In an example of creating a "win-win" policy for both employees and employers, around the beginning of 2011, Microsoft changed its policy and began allowing its employees to moonlight and keep the resulting intellectual property and a large portion of revenue, provided that the employee was moonlighting as an app writer for Windows Phone 7-based cell phones.

More recently, in March 2016, Nintendo acknowledged that it also allows employee moonlighting. Ironically, Nintendo's acknowledgement was made in connection with the discharge of a marketing employee for "violation of an internal company policy involving holding a second job in conflict with Nintendo's corporate culture." Chelsea Stark, *Nintendo: Female employee fired for moonlighting, not online pressure*, MASHABLE (March 30, 2016), http://mashable.com/2016/03/30/nintendo-alison-rapp-fired-moonlighting/#rjQr8Wm3TiqQ.

Regardless, it is clear that the attitudes, law and policies governing moonlighting high-tech employees and the ramifications of their secondary employment are changing as quickly as the technologies they are developing.