COVENANTS NOT TO COMPETE AND INDEMNITY CLAUSES: AN OVERVIEW FOR ACCOUNTANTS

Ross Spence

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COVENANTS NOT TO COMPETE

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A. Common Law Background

At common law, agreements in restraint of trade are unenforceable. A covenant not to compete is considered an agreement in restraint of trade, so there is a general presumption that it is unenforceable. Only if the covenant not to compete is found to be (a) reasonable, and (b) ancillary to another contract would it be enforced. In order to be reasonable, the covenant must be reasonably limited as to (1) time, (2) scope, and (3) geographical extent. The contract to which it is ancillary must be "otherwise enforceable" and not merely the covenant not to compete itself or some other agreement in restraint of trade.

In 1987, the Texas Supreme Court changed prior common law with its decision in *Hill v. Mobile Auto Trim, Inc.* , 725 S.W.2d 168 (Tex. 1987). The Court held that a covenant not to compete must be supported by independent consideration, such as specialized training or the sharing of trade secrets. The Court went on to hold that covenants not to compete by employees engaged in a "common calling" are without consideration as a matter of law because there is no specialized training or trade secret involved in a common occupation. Subsequent cases held that sales, hairstyling, and even the medical profession are common callings.

B. Tug-of-War Between Legislature and Supreme Court

The practical effect of the *Hill* case was to invalidate the vast majority of covenants not to compete. This upset enough employers and legislators that a Covenants Not To Compete Act was passed in 1989. Codified at Sections 15.50 and 15.51 of the Tex. Bus. & Com. Code, the Act was intended simply to codify the common law standards that existed prior to the 1987 *Hill* decision. No independent consideration for the covenant not to compete was required if it was executed on the same day as the employment contract. The legislature did, however, add a new requirement that if the covenant not to compete was executed on a date different than the contract to which it was ancillary, then it had to be supported by independent consideration.

Not willing to let the legislature have the final say, the Texas Supreme Court did not try to reinstate its "common calling" rationale, but it did add an additional, non-statutory standard that must be met before a covenant not to compete can be enforced. Not only must the covenant be ancillary to an otherwise enforceable agreement and be reasonable as to time, scope, and territorial extent, but the employer's need for the protection afforded by the covenant not to compete must not be outweighed by either the hardship to the employee or any injury likely to the public. *DeSantis v. Wackenhut Corp.*, 793 S.W.2d 670, 681-82 (Tex. 1990). On the same day, the Supreme Court held that an "at-will" employment relationship is not an otherwise enforceable agreement, so a covenant not to compete is unenforceable if it is ancillary only to an at-will employment relationship. *Martin v. Credit Protection Ass'n, Inc.*, 793 S.W.2d 667, 670 (Tex. 1990).

The legislature attempted, once again, to rein in the Texas Supreme Court by amending the Covenant Not To Compete Act in 1993. The full text of the current Act is attached as **Appendix 1**. In a new Section 15.52, the legislature firmly stated:

> The *criteria* for enforceability of a covenant not to compete *provided by Section 15.50 of this Code* and the procedures and remedies in an action to enforce a covenant not to compete provided *by Section 15.51 of this Code are exclusive and preempt any other criteria* for enforceability of a covenant not to compete or procedures and remedies in an action to enforce a covenant not to compete *under common law or otherwise*.

The primary substantive change in the statute was to recognize expressly that covenants not to compete can be ancillary to at-will employment contracts. See Tex. Bus. & Com Code § 15.51(b).

In the first case decided under the amended statute, the Texas Supreme Court sought to reaffirm its supremacy. It stated:

> The enforceability of a covenant not to compete, including the question of whether a covenant not to compete is a reasonable restraint of trade, is a question of law for the court.

Light v. Centel Cellular Co. of Texas , 883 S.W.2d 642, 644 (Tex. 1994). The Court went on to hold that covenants not to compete cannot be ancillary to at-will employment contracts because at-will employment contracts lack consideration and are unenforceable. *Id.* at 644-45. The Court went on to hold, however, that even in at-will employment contracts there can be certain promises that are not illusory and that can serve as consideration for a covenant not to compete. In *Light*, the Court found that although the employment contract was at-will and unenforceable, the employer's promise to provide special training and the employee's promise to give 14 days' notice before leaving and to provide an inventory of employer's property at the end of the employment were enforceable agreements. *Id.* at 646.

The Court declared, however, that the covenant not to compete was not "ancillary" to these enforceable agreements because of a new standard for determining what is ancillary that the Court just adopted in the same case. In order for a covenant not to compete to be ancillary to an otherwise enforceable agreement:

> (1) 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
>
> (2) the covenant must be designed to enforce the employee's consideration or return promise in the otherwise enforceable agreement.

Id. at 647. The Court then held that the covenant in the *Light* case was not "ancillary." Although the first test might have been met by the employer's promise to train the employee, the covenant not to compete was not designed to enforce the employee's promises to give 14 days' notice and an inventory. *Id.* If the employee had promised not to disclose confidential or proprietary information in the ancillary agreement, then the covenant not to compete would have been enforceable because it would have assisted the employer in enforcing that promise. *Id.* at 647 n.15. It is not clear what other kinds of promises will satisfy the second prong of the "ancillary" test in *Light*.

II. Contracts Ancillary to Sale of Business

The courts have not been nearly as hostile to covenants not to compete incident to a sale of a business as they have to such covenants in employment contracts. Covenants not to compete ancillary to the sale of a business are "upheld as a necessity to secure the goodwill which the buyer purchases." *Williams v. Powell Elec. Mfg. Co.*, 508 S.W.2d 665, 667 (Tex. Civ. App.--Houston [14th Dist.] 1974, no writ). The seller's promise not to compete with the buyer increases the value of the business to the buyer. *Hill v. Mobile Auto Trim, Inc.*, 725 S.W.2d 168, 171 (Tex. 1987). "Without such a covenant the value of the business would be reduced, lessening the likelihood that businesses would be purchased." *Id.*

One reason courts are more likely to enforce covenants ancillary to the sale of a business is that the seller was paid for the covenant. The seller essentially cashes in on the goodwill he or she has built up and it would be inequitable to allow the seller to turn around and deprive the buyer of the goodwill it just paid for by using the seller's goodwill to start up a competing business. See *M.R.S. Datascope, Inc. v. Exchange Data Corp., Inc.*, 745 S.W.2d 542, 545-46 (Tex. App.--Houston [1st Dist.] 1988, no writ). Where such a covenant has reasonable limitations on time, scope, and geographical extent, courts should be willing to enforce it by enjoining the competition. *Id.* at 546. "When such an established business is sold with its goodwill, and there is a reasonable and valid covenant not to compete, the damages are presumed to be irreparable if the covenant is breached, and the remedy at law is considered inadequate." *Id.*

III. Particular Concerns In Accounting Firm Cases

One of the most important interests an accounting firm wants to protect is its relationship with its clients. It does not want to hire new or established accountants, train them and expose them to the firm's clients, and then learn one day that the accountants are leaving and taking the firm's clients with them. This may be difficult to achieve by means of a covenant not to compete ancillary to an employment contract. Though the "common calling" doctrine has been overturned by statute, an echo of it persists in the Supreme Court's holding that "customer information" is neither special training nor special knowledge. *Martin*, *supra*, 793 S.W.2d at 670. In *Martin*, the Supreme Court held that customer information is insufficient consideration for a covenant not to compete entered into after the date of employment. *Id.* Under the *Light* case, courts are required to collapse the transactions to determine whether the consideration given by the employer for the ancillary agreement is sufficient to give rise to the employee's covenant not to compete. Thus, even if an accounting firm were to enter into an ancillary agreement requiring the employee to keep all customer information learned on the job confidential after the job is terminated, the covenant not to compete may still not be enforceable. If customer information is insufficient consideration for a covenant not to compete, then it is not likely to be found to be sufficient consideration for an ancillary confidentiality agreement, which, in turn, must justify the covenant not to compete.

Another interest an accounting firm may want to protect is its special niche or accounting expertise. Unfortunately, the skills of accountancy are not likely to be held to be a trade secret. Accounting skills have specifically been held not to be specialized knowledge or training. *Bland v. Henry & Peters, P.C.*, 763 S.W.2d 5, 8 (Tex. App.--Tyler 1988, writ denied). In that case, the court held:

> Bland received no special training or knowledge specifically imparted to him by Henry & Peters or its officers. He came into Henry & Peters' employment with experience in accounting, and with sufficient skills and knowledge to practice his profession, although no one could reasonably argue that his years of work with Henry & Peters did not greatly enhance those skills and that knowledge.

Id. Thus, an accounting firm will have to go to great lengths to prove that, because of its special expertise, it is imparting specialized training or knowledge to its employees sufficient to be consideration for the employees' confidentiality agreements or covenants not to compete.

Recognizing the difficulty with enforcing a covenant not to compete, some accounting firms rely on a liquidated damages provision instead. One such provision was at issue in *Peat Marwick Main & Co. v. Haass*, 818 S.W.2d 381 (Tex. 1991). Peat Marwick ("PM") merged with a CPA firm in San Antonio. The partners in the acquired firm were given guaranteed salaries for 20 months, vesting rights in PM's retirement program, and other benefits. In return, PM required the merging accountants to agree that all of their existing clients became clients of PM on the date of the merger and any partner who voluntarily terminated his employment with PM thereafter and who, at any time during the 24 month period following the termination, solicited or furnished accounting services for PM clients would be liable to PM for: (a) payment in full of that client's account payable to PM as of the date PM learned that the client would be served by the former partner, and (b) reimbursement for all of PM's direct costs (out-of-pocket expense) paid or to be paid by PM in connection with the acquisition of such client, including retirement benefit obligations of any predecessor firm.

One of the new San Antonio partners subsequently left PM and took many clients with him. PM sought to enforce the damages clause, and the departing accountant argued that the damages provision was an unenforceable restraint of trade. The Texas Supreme Court agreed. The Court held that although neither party was asserting that the damages clause was a covenant not to compete, it had the effect of discouraging competition so it would be analyzed just as if it were a covenant not to compete. The Court proceeded to analyze the provision under its own common law requirements for a covenant not to compete and ignored the statute. The provision at issue was determined to be unenforceable for two specific reasons: (1) it applied to clients who first became clients after the accountant left PM, and (2) it applied to clients regardless of whether the accountant had contact with those clients while at PM. The Court implies that, if the provision had been more tightly drawn, it would have been enforceable. The Court cited and did not overrule a prior case in which a similar liquidated damages provision was enforced. See *Henshaw v. Kroenecke*, 656 S.W.2d 416 (Tex. 1983). In *Kroenecke*, the liquidated damages provision read:

> As liquidated damages, the parties agree that no injunction shall lie for breach of this section but that Kroenecke will pay to Henshaw an amount calculated as 12 times the average monthly partnership billing to each client or prior client with whom Kroenecke does business in violation of this covenant. Such average monthly partnership billing shall be computed by including only those months in which the partnership billed said client

> or past client in the twelve months preceding such termination. Henshaw agrees that there will be no geographical limitation under this covenant.

Id. at 417.

Another issue that comes up in accounting cases is whether an employee's breach of an unenforceable covenant not to compete entitles the accounting firm to withhold payment on a monetary obligation it has to the employee. One such case is*Peat, Marwick, Mitchell & Co. v. Sharp*, 585 S.W.2d 905 (Tex. Civ. App.--Amarillo 1979, writ ref'd n.r.e.). In that case, the firm partnership agreement had a non-compete provision and a provision that any former partner who violated the provision would lose his entitlement to benefits under the firm's retirement plan. *Id.* at 906-07. It was proven that the former partner was in violation of the covenant not to compete, but that covenant was held not to be enforceable because it failed to contain reasonable geographical limits. *Id.* at 907. The court went on to hold that because the covenant not to compete was invalid, the former partner was not precluded from recovering his $46,500 in accrued benefits under the retirement plan. *Id.* at 908. The opinion suggests that if PM had requested that the covenant be reformed to contain a geographical limit and had pleaded the partner's breach as an affirmative defense, they might have prevailed.

A similar issue occurred in *Greenstein v. Simpson*, 660 S.W.2d 155 (Tex.App.--Waco 1983, writ ref'd n.r.e.). In that case, a retired partner sued his former accounting firm to recover the balance due on promissory notes given in exchange for the retired partner's interest in the partnership. The firm defended on the grounds that the retired partner breached his covenant not to compete, which they successfully proved at trial. *Id.* at 159. The court held that the covenant not to compete was unenforceable because it contained no limit as to geographical area. *Id.* However, the court agreed that the retired partner's breach of the covenant was a defense to the firm's obligation on the notes because the notes were given in consideration for the partner's agreement to retire permanently from accounting. *Id.* at 160. The court held that to deny the firm this defense because the covenant is unenforceable would allow the retired partner to receive the full benefit of his agreement in the face of his breach of the essential covenant. *Id.* at 161. The firm could not have sued the partner for the breach due to the unenforceability of the covenant, but it was entitled to raise the breach as a defense. Arguably to the contrary is the case of *Frankiewicz v. National Comp. Associates*, 633 S.W.2d 505 (Tex. 1982). In that case, an insurance salesman sued for commissions due to him by his prior employer. It was undisputed that he had been selling insurance for his new employer in violation of the covenant not to compete he signed with his prior employer, but the court held that the covenant was unenforceable because it contained no geographical limits. The court further held that because the covenant was unenforceable, the employee's violation of the covenant could not be used as a defense by the employer to the employee's claim for commissions. The difference between the *Frankiewicz* case and *Greenstein* is that in *Greenstein* the accounting firm argued and successfully proved that the covenant not to compete was the direct consideration for the partnership's note to the departing partner.

In the converse situation it has been held that a former employer cannot enforce a covenant not to compete by injunction when the employer has breached that contract. *Professional Beauty Products, Inc. v. Jay*, 463 S.W.2d 288, 290 (Tex. Civ. App.--Amarillo 1970, no writ).

IV. Drafting Enforceable Provisions

Unfortunately, the law concerning covenants not to compete has been in a constant state of flux. The courts have shown no hesitancy to strike down covenants not to compete no matter how tightly they are drawn. Despite the efforts of the legislature to preempt the common law concerning covenants not to compete, it is still the courts, not the legislature, that decide each particular case.

In order to be enforceable, the covenant or damage provision will have to meet the following tests: (1) it must be ancillary to an otherwise enforceable agreement; (2) the consideration given by the employer to the employee in the ancillary agreement must give rise to the employer's need for a covenant not to compete; (3) the covenant not to compete must be designed to enforce the promises made by the employee in the ancillary agreement; and (4) the covenant must not contain limitations as to time, geographical area, and scope of activity that are unreasonable or impose a greater restraint than is necessary to protect the goodwill or other business interest of the employer. The following draft agreement attempts to address the foregoing elements in the difficult situation in which the covenant is ancillary to an employment agreement and the employee is an employee at will:

COVENANT NOT TO COMPETE

This agreement is entered into between ___________ (Employee) and ____________________ (Firm) on the date written below.

Employee and Firm understand and agree that:

1. Firm has a valid and protectable interest in and property right to its goodwill, client base, and client relationships.

2. Employee will, as a result of being hired by Firm, have the opportunity to meet and work with Firm clients and to work on accounting issues and matters that Employee has not previously worked on. Employee will receive specialized training and knowledge as a result of working for Firm. Each of these matters are sufficient consideration for this Covenant Not to Compete.

3. For a period of two years after Employee's voluntary termination from Firm, Employee shall not, in Harris County, Texas, solicit accounting work from nor perform any accounting work for any client of the Firm that was a client at any time prior to Employee's termination and for whom Employee performed any accounting services while employed by Firm.

4. This Covenant Not to Compete complies with and is enforceable under Chapters 15.50-15.52 of the Texas Business & Commerce Code. This Covenant Not To Compete is a reasonable restraint on commerce.

5. This Covenant Not To Compete is enforceable by temporary and permanent injunctive relief.

6. If Employee breaches this Covenant Not To Compete, Firm shall be entitled to recover from Employee

a sum equal to the total Firm billing in the 12 months preceding Employee's termination to each client or prior client for whom Employee performs accounting services in violation of this Covenant Not To Compete. This liquidated damage provision is reasonable in amount, and it would be difficult or impossible to calculate the damage to Firm's goodwill and client relations or to calculate Firm's investment in specialized knowledge and training for Employee in order to calculate damages in a manner other than as set forth in this provision.

7. Employee shall be liable to Firm for all attorneys' fees and expenses and all costs of court incurred by Firm in connection with efforts to enforce this Covenant Not To Compete.

8. If this Covenant Not To Compete should be found to be unenforceable in whole or in part, Employee shall indemnify Firm for all damages or losses resulting from the unenforceability of the Covenant Not To Compete or resulting from losses occasioned by Firm's negligence, gross negligence, or strict liability. Such loss shall include, but not be limited to, attorneys' fees and expenses.

AGREEMENT IN CONNECTION WITH AT WILL EMPLOYMENT

This agreement is entered into between ____________ (Employee) and ______________________ (Firm) on the date written below.

Employee and Firm understand and agree that:

1. Employee is an at will employee of Firm. Either Employee or Firm may terminate the employment relationship at any time and for any reason, or no reason at all.

2. While employed, Employee shall be given by Firm the opportunity to work for clients of the Firm. Employee shall receive specialized training and knowledge through on-the-job training, supervision, and other means. Employee shall have the opportunity to improve his professional reputation through his work, training and experience with the Firm and shall have the opportunity to develop customer relationships with Firm clients.

3. All work papers, files, work product, databases, and other matters developed by Employee or other members of Firm shall be the exclusive property of

Firm, and Employee will surrender all such materials, including any copies of same, to Firm at the conclusion of his employment. After Employee voluntarily ceases working for Firm, Employee shall not utilize any of the knowledge, accounting skills, customer relationships, or specialized training or knowledge he obtained as a result of employment by Firm to work on any matters for any clients or former clients of Firm.

INDEMNITY AGREEMENTS

I. In General

An indemnity agreement is defined as:

> A collateral contract or assurance, by which one person engages to secure another against an anticipated loss or to prevent him from being damnified by the legal consequences of an act or forbearance on the part of one of the parties or of some third person.

Dresser Industries, Inc. v. Page Petroleum, Inc., 853 S.W.2d 505, 508 (Tex. 1993). In English, an indemnity clause purports to shift responsibility for the payment of damages from one party to another. *Whitson v. Goodbodys, Inc.*, 773 S.W.2d 381, 382 (Tex.

App.--Dallas 1989, writ denied). For example, an insurance contract is an indemnity contract.

In the accounting context, indemnity clauses are frequently used in the sale of an accounting practice. Typically, partners in a CPA firm selling their practice agree to indemnify the purchaser for any claims made against the purchaser arising out of their accounting services rendered prior to the sale. The buyer does not want to assume unknown liabilities for accounting services he had nothing to do with just because he happens to be the successor-in-interest to the prior firm. An accountant would also like for his engagement letter to contain an indemnity from his client, but this might interfere with the accountant's role as an independent public accountant.

Texas courts construe indemnity agreements strictly against the person being indemnified. See *e.g., Ethyl Corp. v. Daniel Constr. Co.*, 725 S.W.2d 705 (Tex. 1987). This is because indemnity agreements are viewed with disfavor. There is an idea that a person who has an indemnity from someone else will be less careful about his actions. It is important to know the specific ways in which the Texas courts have rationalized the striking-down of indemnity agreements.

II. The Express Negligence Test

The "express negligence test" requires that if one party expects to be indemnified for his own negligence, then the indemnity provision must very clearly spell that out and the word "negligence" must actually be used. *Ethyl Corp. v. Daniel, supra*. This came as a great and rude surprise to all those persons who thought they were covered because their indemnity provisions were worded as broadly as possible, such as an indemnity for:

> All claims, demands, or damages of any and every kind, whether caused by Indemnitor, Indemnitee, some other person, or any combination of the foregoing.

If the claimant alleges the person covered by the foregoing indemnity clause was negligent, then there is no coverage.

The Texas Supreme Court recently invalidated many other indemnity provisions as well. Not only must negligence be expressly stated in order to be indemnified against, but so must other theories of recovery, such as strict liability. An indemnity will not protect against strict liability unless it specifically refers to strict liability. *Houston Lighting & Power Co. v. Atchison, Topeka & Santa Fe Railway*, 890 S.W.2d 445 (Tex. 1994). Based on the language and facts of the HL&P case, it would be prudent to spell out each of the other specific theories of recovery you want to be indemnified against, such as breach of warranty, breach of contract, breach of rules, regulations, or professional standards, breach of statute, breach of fiduciary duty, et cetera.

In the sale of an accounting practice, the seller usually does not indemnify the buyer for the buyer's own negligence. Rather, the seller gives an indemnity for prior negligence of the seller. Thus, the express negligence test, with its subsequent enlargements will not be an issue in most cases.

III. The Requirement Of Conspicuousness

In order for an indemnity agreement to be valid, "something must appear on the face of the contract to attract the attention of a reasonable person when he looks at it." *Dresser Industries, Inc. v. Page Petroleum, Inc.*, 853 S.W.2d 505, 508 (Tex. 1993). Whether a given indemnity clause is sufficiently conspicuous is a question to be decided by the court, not a jury. *Id.* at 510. Courts have held that indemnity provisions are not conspicuous when they are on the back side of a form or where they appear in small, light type and are surrounded by unrelated terms. *Id.* The Texas Supreme Court has adopted the following standard:

> A term or clause is conspicuous when it is so written that a reasonable person against whom it is to operate

> ought to have noticed it. A printed heading in capitals ... is conspicuous. Language in the body of a form is "conspicuous" if it is in larger or other contrasting type or color.

Id. at 511. Thus, it is best to put a large heading above the indemnity section and then print the indemnity language in all capitals in a different type font.

The result in the *Dresser* case was that the indemnity and release provisions at issue were held invalid by the Texas Supreme Court. They were contained in the body of the contract and were not in different type-font, size, or color. The effect is that two large industry players, bargaining at arm's length, are not free to contract amongst themselves to shift risk of loss as they see fit unless they happen to have tinkered with their word processors to change the print.

The only bright spot in the *Dresser* case is the following holding:

> The fair notice requirements are not applicable when the indemnitee establishes that the indemnitor possessed actual notice or knowledge of the indemnity agreement.

Id. at n.2. Parties who want to rely on an indemnity provision would be wise not only to do everything they can to make it conspicuous, but also to have the indemnifying party specifically review and initial that paragraph. That way, the other party cannot argue later that it was not conspicuous enough.

IV. How The Indemnity Provision Operates

Suppose the seller of an accounting firm indemnifies the buyer for any claims arising out of acts or omissions that occurred prior to the sale. After the sale, a claim is made against the buyer alleging some negligent act prior to the sale. The buyer notifies the seller and demands that the seller undertake the defense of the claim and any resulting liability.

What if the seller refuses to defend buyer? Assuming the indemnity provision is valid (*i.e.*, conspicuous), then the buyer can either settle the lawsuit or defend it all the way through trial and then sue the seller for all sums expended. If actual liability is proven at trial, then the buyer should have no problem recovering from the seller. What if liability is unclear and the buyer settles? The seller will assert that he does not have to indemnify the buyer unless the claim actually has merit, and he will obviously assert that the claim had no merit and should not have been settled. The rule is that, where the seller refused to undertake the defense, the buyer does not have to prove that the third-party's claim had merit. Instead, the buyer is entitled to full indemnity if he merely shows that there was a potential liability and that his settlement was reasonable, prudent and in good faith under the circumstances. *Cox, Colton, Stoner, Starr & Co., P.C. v. Deloitte, Haskins & Sells*, 672 S.W.2d 282, 286 (Tex. App.--El Paso 1984, no writ).

What if the seller does agree to defend the third-party claim against the buyer and wants to take it to trial, but the buyer (who wants to have ongoing business with the claimant) settles the claim anyway? The rule then is that the buyer will have to prove that the third-party's claim was valid and that there were no meritorious defenses that could have been asserted, or else the buyer cannot recover the amount he paid to settle the case. *Id.* This puts the buyer in the awkward position of having to sue the seller and having to prove that the buyer's own accounting firm committed malpractice in the past.

Typically, the buyer of an accounting firm obligates himself to pay the purchase price in installments over a period of months or years. When a client makes a claim against the firm and the seller disputes the buyer's demand for indemnity, what happens to the buyer's payment obligations to the seller? That was an issue in the *Cox v. Deloitte* case. Cox still owed Deloitte $240,000 for the purchase of Deloitte's El Paso office when the indemnity dispute arose. Cox asserted that Deloitte's failure to provide a defense and to furnish reimbursement for the settlement Cox paid to the firm's client excused Cox's obligation to pay the remainder of the purchase price. *Id.* at 286. The court disagreed on the basis that Cox had treated the contract as continuing. Cox kept insisting that Deloitte honor the indemnity provision and never asserted that the contract was no longer continuing. The rule is that:

> [W]hen one party breaches its contract, the other party is put to an election of continuing or ceasing performance, and action indicating an intention to continue will operate as a conclusive choice, not depriving the injured party of his cause of action for the breach which has already taken place, depriving him only of any excuse for ceasing performance on his own part.

Id. at 287. What Cox should have done, then, is declare that Deloitte had repudiated the contract and, therefore, that Cox had no further obligation under the contract.

CONCLUSION

Covenants Not To Compete and Indemnity Clauses are two areas in which Texas courts are guilty of judicial activism. The rule used to be that

> If there is one thing which more than another public policy requires it is that men of full age and competent understanding shall have the utmost liberty of contracting, and that their contracts when entered into freely and voluntarily shall be held sacred and shall be enforced by Courts of justice. Therefore, you have this paramount public policy to consider--that you are not lightly to interfere with this freedom of contract.

Wood Motor Co. v. Nebel, 238 S.W.2d 181, 185 (Tex. 1951). Instead of following this advice, recent Texas Supreme Courts have embarked on a paternalistic crusade to rewrite contracts they find offensive. Covenants Not To Compete are disfavored because they restrict a person's ability to work in a specific occupation or place. Indemnity Provisions are disfavored because they can enable a person to shift responsibility for his own conduct to another person. To give these type of contract clauses any teeth, drafters have to be careful and precise. To some extent, they must also be omniscient--predicting what the Supreme Court will do next.