STATE OF MICHIGAN

IN THE SUPREME COURT

INNOVATION VENTURES, LLC f/d/b/a LIVING ESSENTIALS, ~~a Michigan Limited Liability Company~~,

Plaintiff-Appellant,

v

LIQUID MANUFACTURING, LLC, ~~a Michigan Limited Liability Company,~~ K & L DEVELOPMENT OF MICHIGAN, LLC, ~~a Michigan Limited Liability Company,~~ LXR BIOTECH, LLC, ~~a Michigan Limited Liability Company~~, ETERNAL ENERGY, LLC, ~~a Michigan Limited Liability Company,~~ ANDREW KRAUSE, ~~an individual~~, and PETER PAISLEY, ~~an individual,~~

150591 Defendants-Appellees.

Supreme Court No. ________

Court of Appeals No. 315519 13-2344

Oakland County Circuit Court Case No. 12-124554-CZ

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APPELLANT INNOVATION VENTURES, LLC'S APPLICATION FOR LEAVE TO APPEAL

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STATEMENT OF APPELLATE JURISDICTION

This Court has jurisdiction under MCR 7.301(A)(2) to grant leave to appeal from the Court of Appeals' opinion entered on October 23, 2014.

JUDGMENT APPEALED FROM AND RELIEF SOUGHT

Plaintiff Innovation Ventures, LLC seeks leave to appeal from the Court of Appeals' opinion affirming the Oakland County Circuit Court's summary disposition grant on all counts of Innovation Ventures' complaint, even though Defendants only sought summary disposition on Innovation Ventures' contract-based claims. The Court of Appeals concluded that (1) Innovation Ventures' contracts with Defendant Andrew Krause and his company, K&L Development of Michigan, LLC, were unenforceable because the agreements did not last long enough to constitute adequate consideration; (2) non-compete agreements between sophisticated businesses should be governed by the law applicable to employment relationships rather than commercial relationships; and (3) Defendants were entitled to summary disposition on Innovation Ventures' claims for trade-secret misappropriation before any meaningful discovery had taken place.

These rulings essentially say that sophisticated companies cannot rely on the enforceability of written contracts at the time of execution. The rulings also undermine Michigan's intellectual-property protection. If the Court of Appeals opinion is left in place, it will have a sever chilling effect on any company that has intellectual property and is considering moving to or expanding in Michigan, and the holdings will frustrate reasonable expectations regarding contracting in a wide variety of employment and commercial contexts. Innovation Ventures respectfully requests that this Court grant leave to appeal or peremptorily reverse and remand the case to the circuit court.

STATEMENT OF QUESTIONS PRESENTED

1. Whether a written contract, which memorializes an oral contract that existed for years, must be continued "for a substantial time" to make a non-compete provision enforceable in Michigan.

The trial court did not answer this question.

The Court of Appeals, *sua sponte*, answered: Yes.

Plaintiff-Appellant answers: No.

Defendants-Appellees have never previously raised this issue but now will presumably answer: Yes.

2. Whether the test for analyzing the validity of a non-compete provision in an employment contract should also be used to evaluate a non-compete provision in a commercial contract, rather than the rule of reason this Court has applied since 1873.

The trial court answered: Yes.

The Court of Appeals answered: Yes.

Plaintiff-Appellant answers: No.

Defendants-Appellees answer: Yes.

3. Whether summary disposition is appropriate on a claim for trade-secret misappropriation before any meaningful discovery has taken place.

The trial court answered: Yes.

The Court of Appeals answered: Yes.

Plaintiff-Appellant answers: No.

Defendants-Appellees answer: Yes.

INTRODUCTION AND REASONS FOR GRANTING LEAVE TO APPEAL

Plaintiff Innovation Ventures, LLC, is a Michigan company based in Farmington Hills that invented and sells "5-hour Energy," an energy shot that is distributed to retailers around the country. From 2007 until 2010, Innovation Ventures contracted with Defendant Liquid Manufacturing, LLC, through its owner and President, Defendant Peter Paisley, to produce and package 5-hour Energy in Brighton. To design, manufacture, and install the packaging equipment at Defendant Liquid's plant, Innovation Ventures contracted with Defendant Andrew Krause and his company, Defendant K&L Development of Michigan, LLC. Based solely on the contractual relationship among the parties, Paisley, Krause, and their companies had access to every important aspect of Innovation Ventures' operations, including production, sales, and distribution information.

In 2010, Innovation Ventures was ready to in-source production. Innovation Ventures could have simply kept the Brighton production and packaging equipment for itself. But at Defendants Liquid and Paisley's request, Innovation Ventures instead allowed those Defendants to use royalty free (and later purchase) the equipment to produce certain pre-approved energy drinks (such as Red Bull) or energy shots for other companies. This use was expressly conditioned on strict non-compete agreements that allowed Innovation Ventures to control how its propriety equipment was used, by pre-approving products that could be manufactured with that equipment.

Without Innovation Ventures' knowledge, Defendants almost immediately started violating the express contract conditions. For example, Paisley and Liquid obtained pre-approval from Innovation Ventures to produce an energy shot called Eternal Energy for five tattoo parlors. Paisley and Liquid did not disclose that Krause owned the Eternal Energy company, did not disclose that Paisley and Krause changed the Eternal Energy recipe after approval, and did not disclose that plan was to produce Eternal Energy not only for the five tattoo parlors but for Walmart, one of Innovation Ventures' largest and most important customers. Indeed, this is precisely the type of equipment misuse that Innovation tried to prevent.

When these details came to light, Innovation Ventures obtained a TRO that ordered Defendants to stop producing Eternal Energy and gave Innovation Ventures the right to inspect Liquid's facility. A first inspection revealed that Defendants were producing energy shots with the names One Shot, E6, and Quick Energy, none of which Innovation had pre-approved, as expressly required under the parties' contract. A second inspection one week later revealed that Defendants were also producing Quencher and 9 Hour Empower, again all without Innovation pre-approval. And Innovative Ventures later learned of another unapproved energy shot, Krause's Perfectly Petite.

Despite all this, the lower courts refused to enforce the parties' non-compete agreements. Regarding the contract between Innovation Ventures and Krause/ K&L Development, the Court of Appeals voided the agreement, ignoring the oral agreement between the parties as well the written contract memorializing the long standing oral agreement, based on an issue that no party or the trial court had ever even raised: the requirement in some **foreign** jurisdictions (but never previously applied in Michigan) that for a continued business relationship to provide adequate consideration, it must be of a "substantial duration." (Innovation Ventures terminated the parties' contract pursuant to its terms shortly after execution for business reasons that will be explained in full when Innovation is allowed to proceed with discovery in this dispute.) That holding conflicts with this Court's long-standing decisions that parties' freedom to contract will not be circumscribed by courts' evaluation of the reasonableness of consideration.

The Court of Appeals also voided Innovation Ventures' contract with Paisley/Liquid because by applying the wrong standard and holding that the written non-compete covenant was purportedly unreasonable under the rubric for analyzing a non-compete provision in an **employment** context. But Paisley was never an Innovation Ventures employee; the contract was between sophisticated businesses. The Court of Appeals' holding conflicts with published decisions that the rule of reason applies when evaluating the validity of a non-compete agreement between commercial parties.

Finally, the Court of Appeals upheld the grant of summary disposition for Defendants on Innovation Ventures' claim for trade-secret misappropriation. The Court of Appeals so held, even though summary disposition was granted before discovery closed and before Innovation Ventures had received any meaningful written discovery or conducted any depositions.

This Court should grant leave to appeal for multiple reasons. *First*, the contract issues are of jurisprudential significance to all commercial parties who do business in Michigan. No Michigan court has ever before imported the requirement that contractual consideration should be evaluated based on a contract's **post** execution duration. Under the Court of Appeals' analysis, sophisticated companies cannot rely on an oral contract that existed for years or on a contract they just executed, memorializing the oral contract, if one of them later decides to terminate the agreement in accordance with its terms.

Similarly of jurisprudential significance is the Court of Appeals' conflation of the standards for evaluating a non-compete provision in an employment agreement versus a commercial contract. This issue involves appropriate interpretation of the Michigan Antitrust Reform Act, an Act that this Court has not addressed for several decades, since the law was well settled. The Court of Appeals opinion unsettles what was previously clear Michigan law regarding non-competition agreements and will give significant pause to any company considering whether to enter a contract that actually **promotes** competition (as did the contracts here) for fear of losing any ability to protect confidential and proprietary competitive information.

Second, the Court of Appeals opinion has a broad application. The opinion's conclusion that courts must evaluate contractual consideration post-hoc, depending on how long the contract lasts, will affect restrictive covenants found in employment agreements, professional-services contracts, contract-manufacturing agreements, supply agreements, and many other types of agreements among sophisticated business parties across all industries. None of these parties are likely to take a philosophical wait-and-see approach to determine whether the Court of Appeals' detailed analysis here will be adopted in a subsequent published opinion.

Third, the decision will have a deleterious effect on business throughout the state because of the reduced reliability of restrictive covenants and the increased difficulty in ensuring the protection of valuable confidential information and intellectual property. Businesses considering whether to remain in the state or to relocate to Michigan will view this decision as a significant deterrent because of its failure to protect intellectual property.

Fourth, even though this opinion is unpublished, it is likely to have significant effect because it is lengthy and unusually detailed. Trial court judges are unlikely to disregard the analysis in this case simply because it is unpublished. Further, it addresses two issues that have not been addressed by this Court in decades, and represents a major shift in the law. And in any event, unpublished Court of Appeals decisions are for all practical purposes binding in the federal courts in Michigan.

Finally, the Court of Appeals' decision is plainly erroneous. The decision's absurd result is that Krause, Paisley, and their companies were relieved of all their contractual promises to protect Innovation Ventures' trade secrets and propriety information and were allowed to freely and directly compete with Innovation **using Innovation Ventures' own manufacturing**

equipment and confidential business information. Conversely, Innovation Ventures has no ability to re-negotiate the consideration it received in exchange for allowing what was supposed to be limited competition. In other words, the Court of Appeals did not just void and rescind the parties' contracts, it rewrote them entirely, giving Defendants the unfettered ability to produce and sell products in direct competition with Innovation Ventures based on the **knowledge** Defendants acquired from Innovation, all at no cost to Defendants.

The Court should grant leave to appeal, reverse, and remand the case for additional proceedings in the trial court. Alternatively, the Court should peremptorily reverse and remand.

BACKGROUND

The parties and an overview of their business relationships

Innovation Ventures manufactures and markets liquid dietary supplements, including a two-ounce energy shot known as 5-hour Energy. (2d Am Verified Compl ¶ 10.) That product is what solely supports hundreds of jobs between Michigan and Indiana. 5-hour Energy is a singularly successful product, with sales of more than $700 million between 2004 and the beginning of 2012. (*Id.* ¶ 19.) Innovation Ventures has spent more than $450 million on advertising, marketing, and promoting 5-hour Energy to establish its brand identity and product integrity. (*Id.*) As a result of that investment, 5-hour Energy can be found in more than 100,000 retail stores and health clubs throughout the United States and Canada. (*Id.* ¶ 20.)

From 2007 until 2010, Innovation Ventures contracted with Defendant Liquid Manufacturing, LLC to produce and package 5-hour Energy. (*Id.* ¶ 11.) Defendant Peter Paisley is Liquid's owner, president, and chief executive officer. (COA Op 2.)

About a year after Krause and K&L Development's long-term business relationship with Innovation Ventures ended, Krause started a new venture to produce competing energy-shots. (Krause Aff ¶ 6; 2d Am Verified Compl ¶¶ 13-14.) He created several companies to market and distribute his competing products, including Defendants Eternal Energy, LLC, and LXR Biotech, LLC. (*Id.*) Krause and his businesses contracted with Liquid to manufacture and package his competing products on Innovation Ventures' equipment.[1] (Krause Aff ¶ 11.)

[1] A dispute between Krause and one of his business partners subsequently revealed that Paisley is also an owner of LXR and Eternal Energy (see Innovation Ventures' COA Br, Ex 28 *Welker v LXR Labs LLC* Verified Compl ¶ 8), a fact Defendants did not disclose to Innovation Ventures.

Innovation Ventures works with Liquid and Krause

In March 2007, Innovation Ventures first contracted with Liquid to manufacture 5-hour Energy. (See 2d Am Verified Compl, Ex 2 Am Mfg Agreement 1 (attached as Exhibit A).) Among the first things that the parties did was work out a Confidentiality Agreement. (See 2d Am Verified Compl, Ex 1 Confidentiality Agreement.) Liquid agreed to bind its employees, including Paisley (who executed the agreement for Liquid), to the Confidentiality Agreement. (*Id.* ¶ 2.)

A few months later, Liquid and Innovation Ventures executed an Amended Manufacturing Agreement. (Ex A, Am Mfg Agreement.) The Manufacturing Agreement also protected Innovation Ventures' confidential information and intellectual property. Liquid agreed that it would not "produce or formulate any other Energy Drink in packaging of 4 fluid ounces or less" as well as energy drinks of any size containing certain specified ingredients. (*Id.* § 17.) Liquid's exclusivity obligations extended to three years after the agreement terminated. (*Id.*)

The Manufacturing Agreement included considerable discussion of the production equipment. (*Id.* §§ 8, 20.b.) Because Innovation Ventures pioneered the energy-shot market, Innovation Ventures and Liquid could not simply purchase a complete energy-shot bottling and packaging line. (Henderson Aff ¶ 15.) Instead, Innovation Ventures pieced together various components and made extensive modifications to meet its quality, sales, and production needs. (*Id.*) Accordingly, the Manufacturing Agreement provided that Innovation Ventures could provide production equipment for Liquid's use, and it could also require Liquid to obtain specific production equipment. (Ex A, Am Mfg Agreement § 8.a.) The parties agreed that when either party ended the Manufacturing Agreement, Innovation Ventures had the right to purchase any production equipment Liquid had acquired. (*Id.* § 10.)

Because Innovation Ventures faced a number of quality-control and manufacturing challenges related to bottling its energy shot, Innovation Ventures retained Defendant Andrew Krause and his company, Defendant K&L Development to specifically "help design, manufacture, and install certain manufacturing and packaging equipment" solely to meet the production needs of 5-hour Energy (See Henderson Aff ¶ 4; Apr 29, 2009 email from Krause to K. Smith.) Innovation Ventures entered into an oral agreement with Krause and his company, K&L Development of Michigan, LLC, to help design, manufacture, and install proprietary manufacturing and packaging equipment. (Henderson Aff ¶ 4.) Krause worked from inside Innovation Ventures' Farmington Hills headquarters, and the equipment was installed at Liquid's Brighton facility. (See *id.*; 2d Amd Compl ¶¶ 10-12.) Innovation Ventures worked with Krause and K&L Development until May 2009. (Krause Aff ¶ 5.) Specifically, Krause and K&L Development made certain production equipment "that is specific to the manufacturing and packaging needs of [Innovation Ventures]." (*Id.*)

Krause helped Innovation Ventures resolve several challenges in manufacturing and packaging of 5-hour Energy. (See Henderson Aff ¶ 15.) Most significantly, Krause helped Innovation Ventures develop a patented cap that prevents leaks and allows customers to easily remove the shrink wrap from the cap. (*Id.* ¶¶ 10-12.)

Krause also assisted Innovation Ventures with modifying the production equipment to tailor it to the manufacture and packaging of 5-hour Energy, including:

- Modifying the fill nozzles on bottling equipment to reduce drips on the outside of the bottle (Henderson Aff ¶ 15.a.);
- Changes to the labeling process to ensure uniform label application without wrinkles (*id.* ¶ 15.b.);
- Identifying the specific amount of torque necessary to tighten the cap to minimize leakage while not over tightening and breaking the bottle (*id.* ¶ 15.c.); and

- Creating equipment to allow multipack packaging (*id.* ¶ 15.e.; Apr 29, 2009 email from Krause to K. Smith).

This proprietary equipment that was designed from within Innovation Ventures' headquarters was installed at Liquid's facility. (Henderson Aff ¶ 4.)

Before working with Innovation Ventures, Krause and K&L Development had no knowledge or experience regarding liquid energy-shot products. (*Id.*¶ 8.) Yet, within a few years, Krause acknowledged that he was functioning as Innovation Ventures' "Production Manager and Supply Chain Director." (Apr 29, 2009 email from Krause to K. Smith.) In that role, Krause learned the sophisticated and proprietary nuances of Innovation Ventures' manufacturing and packaging processes, much of which was highly confidential. (Henderson Aff ¶ 9.) He also directly negotiated contracts with Innovation Ventures' suppliers on behalf of Innovation Ventures, giving him access to highly sensitive and confidential pricing and supplier information. (See *id.* ¶ 9.h.; Apr 29, 2009 email from Krause to K. Smith.)

Innovation Ventures' contracts with Krause and K&L Development

For years, Krause and K&L Development's long-term relationship with Innovation Ventures operated pursuant to oral agreements. (2d Am Verified Compl ¶ 34; Henderson Aff ¶¶ 4-5.) One of the executives at Innovation Ventures met Krause at church and there had been a significant amount of trust placed in Krause. In 2009, the parties agreed to memorialize their oral agreements and put them in writing. Accordingly, Innovation Ventures executed two written contracts with K&L Development regarding the previously oral terms, an Equipment Manufacturing and Installation Agreement ("EMI"), and a Nondisclosure and Confidentiality Agreement. (2d Am Verified Compl, Ex 3 EMI (attached as Exhibit B), Ex 4 Nondisclosure Agreement (attached as Exhibit C).) Krause executed both contracts on April 27, 2009, as the managing member of K&L Development. (*Id.*) He also signed the EMI in his personal capacity. (See Ex B, EMI § 16.)

The EMI contains three provisions memorializing the terms protecting Innovation Ventures' confidential information and intellectual property. As previously agreed to orally, Krause and K&L Development reaffirmed in writing that any intellectual property related to the production equipment that it manufactured for Innovation Ventures belongs to Innovation Ventures. (Ex B, EMI § 8.1.) The contract also included an express confidentiality provision. (*Id.* § 9.) Additionally, Krause and K&L Development reaffirmed in writing that in the energy-drink market, they would provide services exclusively to Innovation Ventures. (*Id.* § 10.)

Just as with the oral agreement between the parties, K&L Development's written non-disclosure agreement also protected Innovation Ventures' intellectual property. The written agreement broadly defined confidential information to include information K&L Development had already obtained from Innovation Ventures during the parties' contractual relationship under the oral agreement, and barred disclosure of that information. (Ex C, Nondisclosure Agreement § 1.) The agreement further required K&L Development to obtain written confidentiality agreements from each of its employees who worked on projects for Innovation Ventures (which K&L Development did). (*Id.* §§ 2.7, 2.8.) Innovation Ventures specifically reserved the right to enforce the employee-signed confidentiality agreements as a third-party beneficiary. (See *id.* § 2.11.)

Around the same time that Innovation Ventures executed these agreements to document its long-standing relationship with K&L Development and Krause, Innovation Ventures hired Karl Smith and assigned responsibility to him for overseeing Krause's contract work. (See Apr 29, 2009 email from Krause to K. Smith.) Krause immediately sent Smith an email to make sure that his "new boss" was aware of the "substantial technical and substantial financial benefits" that Krause brought to the table. (*Id.*) The additional equipment Krause and K&L Development manufactured was installed in Innovation's Indiana facility. (2d Am Verified Compl ¶ 45.) Nonetheless, Innovation Ventures' relationship with Krause ended in May 2009.[2] (Krause Aff § 5.)

Innovation Ventures allows Liquid to use its proprietary production equipment

Innovation Ventures informed Liquid that it was opening a production facility in Indiana in 2009, but Liquid continued to manufacture and package 5-hour Energy for Innovation Ventures under the Manufacturing Agreement into 2010. (See 2d Am Verified Compl ¶ 45.) By 2010, Innovation Ventures was ready to in-source the production to its Indiana facility. (*Id.* ¶ 45.) Accordingly, Liquid and Innovation Ventures ended their Manufacturing Agreement effective April 22, 2010. (*Id.*, Ex 5 Agreement to Terminate & Exercise Purchase Option 1 (attached as Exhibit D).)

Still, Innovation Ventures wanted to ensure that Liquid and Peter Paisley continued to thrive, so, at their request, Innovation Ventures allowed Liquid to continue to use its customized production equipment to produce energy shots on a limited basis for others. (Dolmage Aff ¶ 7.) However, Innovation Ventures did not want its competitors to obtain an unfair competitive advantage from Liquid's use of the equipment in which, through time and money spent in research and development and trial and error, confidential information, proprietary information,

[2] The Court of Appeals stated that the parties' relationship ended around May 10, 2009. (COA Op 3.) The trial court likewise stated that the parties' relationship ended "just two weeks" after the agreements were executed. (3/14/2013 Op & Order 27.) But the only record evidence on this point is a single line in Krause's Affidavit: "My work for [Innovation Ventures] was terminated in May, 2009 by Living Essentials." (Krause Aff ¶ 5.)

and trade secrets were incorporated. (*Id.* ¶ 11.) Accordingly, the parties executed the Agreement to Terminate and Exercise Purchase Option.

In the Termination Agreement, Innovation Ventures purchased the additional specialized production equipment that Liquid had acquired under the Manufacturing Agreement. (See Ex D, Termination Agreement.) The Termination Agreement effectively resulted in Innovation Ventures obtaining title to all of the production equipment embodying its intellectual property and licensing Liquid to use the equipment for a limited number of competitors, but subject to the conditions noted below. (See *id.* § 1.) Innovation Ventures agreed to allow Liquid to use its manufacturing equipment "for a period of one year . . . and Liquid may use the Manufacturing Equipment, **royalty-free** [sic] . . . ." (*Id.* § 6(a) (emphasis added).)

In return, Liquid agreed that it would not produce any competitor's energy drink for three years without Innovation Ventures' pre-approval. (Ex D, Termination Agreement § 1(b).) Innovation Ventures immediately approved the production of 36 energy drinks, including Red Bull, the biggest energy-drink manufacturer. (*Id.* §§ 1(a), 24(i), Ex C; Esterl and Lublin, *Corporate News*, Wall Street Journal (Aug 16, 2014), p B3.) The Termination Agreement contemplated that the list of permitted products would be amended from time to time, but did not limit Innovation Ventures' discretion to decide what products would be approved. (Ex D, Termination Agreement § 24(i).) Liquid agreed that it would not start producing any of the pre-approved products until after its customer executed an agreement not to disclose that its products were being produced by the same manufacturer that made 5-hour Energy. (*Id.* § 4(b), Ex D.) Finally, the parties agreed that Innovation Ventures could revoke permission to manufacture the permitted products "at any time . . . for Liquid's violation of this Agreement" provided that

Liquid was given 30 days to cure the violation if the violation could be reasonably cured within that period. (*Id.* § 1(a).)

Liquid again agreed to protect Innovation Ventures' confidential information and intellectual property. Not only did the Termination Agreement contain confidentiality and non-disclosure provisions (*id.* §§ 2, 4), but Liquid also agreed to "take all reasonable steps to prevent any representatives from any company affiliated with the Permitted Products from inspecting, photographing, videotaping (or other image capturing), [or] having access to" anything in Liquid's possession or control relating to Innovation Ventures' products (*id.* § 1(a)). Liquid also agreed that its employees to whom Innovation Ventures' confidential information was disclosed would be made aware of and bound by the Termination Agreement. (*Id.* § 2.c.)

The record contains no evidence that Liquid ever produced all 36 approved products. Instead, those products were simply pre-approved by Innovation Ventures. (See *id.* Ex C.) Nor is there any evidence in the record that Innovation Ventures ever rejected a request to approve a competing product.

Liquid manufactures Eternal Energy in violation of the Termination Agreement

Around the same time that Innovation Ventures and Liquid were negotiating the Termination Agreement, Krause began to develop a competing energy shot, Eternal Energy. (Krause Aff ¶ 6.) According to Krause, in a period of less than a month, he obtained and finalized the formula for Eternal Energy and approached Paisley about contracting with Liquid to manufacture the drink. (*Id.* ¶¶ 6-12.) Krause had worked extensively with Liquid for Innovation Ventures when Krause was working to improve the manufacturing and packaging process for 5-hour Energy. (2d Am Verified Compl ¶¶ 34-36; Henderson Aff ¶ 4; Dolmage Aff ¶ 12.)

On September 20, 2010, Liquid emailed Innovation Ventures to request approval to manufacture Eternal Energy, an energy shot Liquid represented would be produced by a tattoo-parlor company. (9/20/2010 Email from Criso to Kulpa.) Liquid sent Innovation Ventures a specific ingredient list for Eternal Energy along with label artwork. (*Id.*) Despite the fact that Krause, and Krause's relationship with Innovation Ventures, was well known to Liquid and Paisley, Liquid did not disclose that it was Krause who approached Liquid about bottling Eternal Energy.

Not knowing Krause was behind Eternal Energy, Innovation Ventures approved Liquid's request, but referenced the parties' pre-existing understanding that "any change in the included formula shall require Innovation Venture's additional consent to be re-added as a Permitted Product." (9/21/2010 Email from Kulpa to Criso.) A product with a different formula but the same name would require separate approval. (See *id.*)

Liquid and Innovation Ventures had no further discussion about Eternal Energy until the next year. In the meantime, after more than eight months of royalty-free use of Innovation Ventures' production equipment, Liquid purchased the production equipment from Innovation Ventures for $275,000. (2d Am Verified Compl, Ex 7 Equipment Purchase Agreement.) Liquid could not make a lump-sum payment, so payment was made in monthly installments. (See *id.*) The purchase agreement did not modify Liquid's duties under the Termination Agreement to keep Innovation Ventures' information confidential, protect its intellectual property, and limit its manufacture of energy drinks to the permitted products for three years. (See generally, *id.*)

In April 2011, Innovation Ventures heard that Eternal Energy might have boasted to Wal-Mart that their product was manufactured at a facility previously used by 5-hour Energy. (4/20/2011 Email from Kulpa to Criso.) Innovation Ventures contacted Liquid to ensure that

Liquid provided a non-disclosure agreement executed by Eternal Energy before beginning production. (*Id.*) Innovation Ventures reminded Liquid that it needed to provide the agreement before beginning production. (*Id.*) Liquid responded that it had already run two small batches of Eternal Energy. (4/21/2011 Email from Kulpa to Criso.) Liquid told Innovation Ventures that it would "send you a copy of the [non-disclosure] with Eternal and reiterate that they cannot use the prior Liquid/[Innovation Ventures] relationship in their product promotion." (*Id.*) Liquid failed to send anything until after Innovation Ventures sued to enforce the Termination Agreement. (COA Op 3-4.) In the meantime, Liquid ramped up production of Eternal Energy because Krause and Eternal Energy had obtained a contract with Wal-Mart worth approximately **$40 million**. (See Krause Aff ¶ 13; Dolmage 2d Aff ¶ 4 (in one month, Liquid produced at least 290,000 bottles of Eternal Energy).)

Innovation Ventures sues—and learns of additional contract violations

In the following months, Innovation Ventures became increasingly concerned that Liquid, K&L Development, Paisley, and Krause were using Innovation Ventures' confidential information and intellectual property to produce and market Eternal Energy in violation of their contractual obligations. (Dolmage Aff ¶¶ 18-21.) Innovation Ventures learned, for example, that Eternal Energy was being sold to Wal-Mart, using an unapproved formula. (*Id.* ¶¶ 16, 18.) And Innovation Ventures uncovered that Krause was behind Eternal Energy. (*Id.* ¶ 20.) Given these developments, Innovation Ventures sued to enforce its contracts and protect its trade secrets.

When Innovation Ventures sued, it also obtained an order allowing Innovation Ventures to enter Liquid's facility to inspect whether Defendants were manufacturing Eternal Energy and other liquid energy shots that were not authorized by Innovation Ventures. (TRO 3.)

Innovation Ventures sent Liquid notice under the Termination Agreement that it was revoking consent to produce the permitted products because Liquid violated the Agreement. (1/27/2012 letter from Dolmage to Paisley.) Innovation Ventures inspected Liquid's facilities twice.[3] During the first time Innovation Ventures was allowed to inspect Liquid's facilities, Innovation Ventures observed 290,000 bottles of Eternal Energy that Liquid had produced earlier in the month. (Dolmage 2d Aff ¶ 4.) Innovation Ventures also uncovered evidence that Liquid was producing other unapproved energy shots with the names One Shot, E6, and Quick Energy, none of which was a permitted product (nor was prior approval even sought for them). (*Id.* ¶¶ 5-9.)

A week later, Innovation Ventures inspected the facility again. It discovered that Liquid was continuing to manufacture energy shots including—**in violation of the TRO**—including E6. (*Id.* ¶¶ 11-13.) Innovation Ventures observed that in addition to One Shot, E6, and Quick Energy, Liquid was also producing other violative energy shots, Quencher and 9 Hour Empower, none of which were permitted products under the Termination Agreement. (See *id.* ¶¶ 16-19.) And Innovation Ventures later learned that Liquid was also producing a second unapproved energy shot, Perfectly Petite, for Krause. (See 2d Verified Am Compl ¶¶ 72-74.) In sum, Innovation Ventures' court-ordered inspections uncovered evidence that Liquid was producing no fewer than **six** unapproved energy-shot drinks **in addition to** Eternal Energy. And each inspection identified more violations.

[3] The Court of Appeals' decision may leave the impression that Defendants "allowed" Innovation Ventures to tour Liquid's facility. (COA Op 4.) Nothing could be further from the case—the inspections were done under court order. Indeed, the first time Innovation Ventures arrived at Liquid's facility with the court order to inspect the facility in hand, Liquid's attorney met the Innovation Ventures' attorney and CFO at the door and prevented inspection in direction violation of the court's order.

Liquid responded to Innovation Ventures' notice revoking consent to the manufacture of the permitted products by, for the first time, producing a non-disclosure agreement executed by Eternal Energy. (2/17/2012 Letter from Paisley to Dolmage.) Liquid claimed that by producing the non-disclosure agreement, it had cured any breach of the Termination Agreement. (*Id.*) But Liquid made no reference to the six unapproved energy-shot drinks that it was producing, nor did Liquid cure its breach with respect to those unapproved drinks.

Following the inspections, Innovation Ventures filed its Verified Second Amended Complaint alleging that the Defendants breached various contractual obligations, violated the Michigan Uniform Trade Secrets Act by using Innovation Ventures' trade secrets, and committed various business torts. (2d Verified Am Compl.) The verified complaint averred that Krause and his companies' ability to rapidly achieve such a high level of production and product placement in a short period was the direct result of using Innovation Ventures' confidential information and trade secrets, in violation of Innovation's agreements with all the Defendants. (*Id.* ¶ 86.)

Trial court grants summary disposition before discovery is complete

The procedural history of the case in the trial court is unusual. After allowing emergency discovery in the TRO, resulting in, not merely confirmation of the violations alleged in the original complaint but also discovery of numerous other violations, the court refused to allow Plaintiff any further discovery and stayed all discovery pending Defendants' early motions for summary disposition **by Defendants.**

The court initially denied Defendants' motions except as to tortious-interference claims against Krause and Paisley. (6/15/2012 Op & Order.) In its opinion, the court explained that as to all of the other claims, Innovation Ventures' complaint was adequate, a factual dispute existed, and additional discovery was necessary. (*Id.* at 14-16.) The court specifically noted that "virtually every material fact is vigorously contested by the parties" and that additional discovery was necessary. (*Id.* at 15; see *id.* at 5-13.) With regard to the breach of contract claims against Krause and Paisley, the court held that there were questions of fact regarding whether Krause was bound by the Nondisclosure and Confidentiality Agreement as a "utilized party," and Paisley by the Termination Agreement because it applied to Liquid's employees. (*Id.* at 15-16.)

Discovery proceeded fitfully for five months. (Appellant's Br Ex 8.) The parties haggled over the adequacy of productions as well as the language for the protective order without any resolution. (See *id.*, Ex 9.) While discovery was pending, Innovation Ventures produced thousands of documents to Defendants, but Defendants collectively produced only a handful of documents, with Krause and his companies producing fewer than 10 documents. Because of the incomplete document discovery, neither party took depositions of the parties' principles. (Appellant's Br 12.) As the Court of Appeals explained, when Innovation Ventures sought discovery from third parties including Defendants' customers and business associates, the trial court again stayed discovery while Defendants filed new summary-disposition motions, even though no meaningful discovery was conducted since the order denying the previously filed motions for summary disposition only a few months earlier. (COA Op 4.) In short, Innovation Ventures has not yet had the opportunity to conduct even the most basic discovery necessary to discern how extensively Defendants have breached their agreements with Innovation.

In their second round of summary-disposition motions, Defendants asserted generically that all claims should be dismissed, but they only presented legal arguments for dismissing Innovation's breach-of-contract claims. (See 12/21/2012 Mots for Summ Disp.) Notably, Defendants never contended that there was any failure of consideration for Krause and K&L Developments' contracts with Innovation Ventures.

Even though discovery had not been completed and no depositions had occurred since its earlier ruling denying summary disposition, the court reversed course and granted summary disposition. (3/15/2013 Op & Order.) The court then entered judgment in favor of Defendants as to **all** claims, not just the contract claims the parties had addressed in their summary-disposition pleadings. (*Id.* at 36.)

The trial court concluded that Innovation's ability to pre-approve the products that Liquid could manufacture on Innovation's customized manufacturing and packaging equipment was not reasonable and therefore not enforceable. (*Id.* at 21-24.) The court was particularly troubled by the fact that after the Termination Agreement went into effect, Liquid purchased the customized equipment from Innovation Ventures but continued to be bound by its agreement to limit its use of the equipment. (*Id.* at 23-24.) Essentially, the court declared any post-sale restrictions on use of personal property agreed to by two corporations voice. The trial court did not address or even acknowledge the fact that, bur for the pre-approval limitation, Innovation never would have licensed or sold the proprietary equipment to Liquid at all.

The trial court's assessment of whether the parties had struck good deals continued. For example, the court concluded that K&L Development's agreement to the Nondisclosure Agreement was not supported by adequate consideration, ignoring the fact that it memorialized an oral agreement between the parties that was in place for years. (*Id.* at 25-28.) Specifically, the court reasoned that K&L Development entered into the Nondisclosure Agreement because it desired to provide additional services to Innovation Ventures. (*Id.* at 26.) The court conceded that continuation of the business relationship was adequate consideration at the time the agreement was executed. (*Id.*) But the court assumed—without the benefit of discovery or any record evidence—that "K&L was not given any additional work under the contract because the

Plaintiff terminated that contract two weeks after it was signed. Because the parties' relationship did not continue, it cannot provide consideration for the agreement extracted from K&L." (*Id.* at 26.) The court also concluded that the agreement was unreasonable because the parties agreed to a non-competition agreement "at a time when K&L would derive no further benefit from its relationship with the Plaintiff" (*id.* at 27), The court ignored the fact that it memorialized the long-standing oral agreement between the parties and therefore K&L had received years of benefit.

Finally, the trial court determined that none of the information related to the production of 5-hour Energy could possibly be a trade secret. Specifically, the court reasoned that when Innovation Ventures licensed the use of its customized production equipment to Liquid for the production of competing products, all of the confidential information was disclosed to those competitors. (*Id.* at 29-30.) The court did not address the fact that Liquid's use of Innovation Ventures' customized equipment would not reveal the specifications of the equipment, Innovation Ventures' suppliers, its customers, its pricing, the pricing it obtained from suppliers, its profit margins, or any of the other myriad details that Liquid, Krause, and K&L Development learned exclusively from their work with Innovation Ventures to Innovation Ventures' competitors. Indeed, it was this confidential and proprietary information that motivated Innovation Ventures to bargain for explicit non-compete provisions with Krause and Paisley's companies before allowing Liquid to use Innovation Ventures' own equipment to produce potentially competitive products.

The Court of Appeals affirms the circuit court's decision

The Court of Appeals affirmed the circuit court's decision, but for different reasons. The court agreed with the circuit court's analysis that the limitations on Liquid's use of Innovation Ventures' customized production equipment are an unreasonable non-competition agreement.

(COA Op 7.) Like the trial court, the Court of Appeals based its analysis on cases addressing the enforceability of non-compete agreements in the employment context, rather than in commercial transactions. (See *id.* at 7-8.) The court concluded that because the agreement allowed limited use of its customized production equipment to produce some competitors' products, the agreement was unreasonable. (*Id.*) The court agreed that preventing anti-competitive use of Innovation Ventures' confidential information is a legitimate business interest that would support a restrictive covenant. But the court concluded that because Innovation Ventures allowed Liquid's production of 37 competing products (and thus the use of its confidential information and intellectual property), it could not bar Liquid's unlimited use of that information and intellectual property. In short, the court concluded an agreement between two corporations to prevent all competitive use is reasonable, but an agreement between two corporations for limited competitive use was not reasonable; accordingly, only a complete contractual ban on competition is allowed in Michigan. In conducting this analysis, the Court of Appeals incorrectly asserted that Innovation Ventures was only asserting that the production of Eternal Energy and Perfectly Petite violated the Termination Agreement. (COA Op 6.) As the verified complaint and the appeal brief make crystal clear, Innovation Ventures has always maintained that production of Eternal Energy—and all six other energy shots—violated the contract.

The Court of Appeals also reasoned that Paisley was not bound by the confidentiality provisions in the Termination Agreement because he executed the contract only in his official capacity, as an employee of the company. (*Id.*) The Court noted that the Termination Agreement expressly bound Liquid's employees to abide by the terms of the agreement, but concluded that the provision was unenforceable because Paisley had not signed a writing in his individual capacity, purportedly creating a statute of frauds problem. (*Id.*)

The Court of Appeals then turned to the enforceability of the Nondisclosure Agreement and the EMI. It rejected the trial court's conclusion that the agreements were not supported by adequate consideration, noting that because the agreements recited the continuation of the business relationship, "the agreements, on their face, contained valid consideration . . . ." (COA Op 10.) But the court then adopted a new theory for why the contracts could not be enforced that the parties and the trial court had never even suggested—the contracts were **rescinded** based on failure of consideration. (*Id.* at 10-12.) The court reasoned that because Innovation Ventures "terminated the business relationship within two weeks after the agreements were signed, plaintiff's forbearance in terminating the relationship [at will] amounted to a nullity." (*Id.* at 11.) The court then cited cases from foreign jurisdictions imposing a requirement that for continuation of employment to constitute consideration, it must be for "a substantial time." (*Id.*)

The Court of Appeals affirmed the circuit court's rejection of Innovation Ventures' other claims. It relied on Krause's claims that he did not receive any confidential information from Innovation Ventures and Innovation Ventures' purported failure "to make any effort to keep the bottling process a trade secret" (*id.* at 13), despite disputed questions of material fact on these very points created by Innovation Ventures' own, countervailing affidavits. (Dolmage Aff ¶¶ 4-6, 11; Henderson Aff ¶¶ 9-12, 19.) The court criticized Innovation Ventures for failing to identify the specific trade secrets that Defendants misappropriated. (COA Op 13.) And the court rejected Innovation Ventures' argument that it could not do so because discovery was not completed and it had not had the opportunity to depose Krause, Paisley, or any other witnesses. (*Id.* at 17.) Notwithstanding Defendants' readily apparent damaging evidence of Defendants Liquid's and Krause's violations from Innovation Ventures, the court required that Innovation

Ventures produce "independent evidence that a factual dispute exists" and rejected Innovation Ventures' assertions as to what additional discovery could demonstrate. (*Id.*)

STANDARD OF REVIEW

This Court reviews summary-disposition decisions de novo "to determine if the moving party is entitled to judgment as a matter of law." *Maiden v Rozwood*, 461 Mich 109, 118; 597 NW2d 317 (1999). Under MCR 2.116(c)(10), courts must consider the evidence submitted by the parties "in the light most favorable to the party opposing the motion." *Id.* at 120.

ARGUMENT

I. The Court of Appeals' failure-of-consideration analysis is an impermissible backdoor evaluation of the adequacy of consideration that limits parties' freedom to contract.

K&L Development and Krause agreed originally orally, and later in writing, to the EMI and the Nondisclosure Agreement based on their business judgment that the obligations set forth in the contracts were worth the benefit of a long-standing business relationship with Innovation Ventures as well as the potential for further business. The EMI expressly contemplated that the parties' business relationship could be terminated by either party by giving 14-days' notice. Ignoring the oral agreement between the parties, which governed their working relationship for years and was memorialized in the EMI, the Court of Appeals determined that the few-weeks duration of the parties' business relationship after execution of the written agreement resulted in a total failure of consideration is incorrect because it did fulfill the parties' contractual obligations. But even more fundamentally, the Court of Appeals erred by assessing the adequacy of consideration at all.

A bedrock tenet of Michigan's jurisprudence is that "[c]ourts enforce contracts according to their unambiguous terms because doing so respects the freedom of individuals freely to arrange their affairs via contract." *Rory v Cont'l Ins Co*, 473 Mich 457; 703 NW2d 23, 30 (2005). For this reason, "[c]ourts do not generally inquire into the sufficiency of consideration." *Gen Motors Corp v Dep't of Treas*, 466 Mich 231, 239; 644 NW2d 734 (2002) (citing *Harris v Bond & Mfg Corp*, 329 Mich 136, 145; 45 NW2d 5 (1950)). Indeed, the Court has concluded that even the bare opportunity to discuss and possibly resolve a post-warranty complaint with a car manufacturer is legally sufficient consideration. *Id.* at 239-241. In other words, it does not take very much for a court to find adequate consideration; the proverbial peppercorn will do.

"[T]he freedom to contract also permits parties to enter into new contracts or modify their existing agreements." *Quality Prods & Concepts v Nagel Precision, Inc*, 469 Mich 362, 370-371; 666 NW2d 251 (2003). The mere fact that parties consider it to their advantage to modify their agreement is sufficient consideration for the modification. *Buck v N Dairy Co*, 364 Mich 45, 49; 110 NW2d 756 (1961). Indeed, the Legislature has specifically provided that an agreement to modify a contract or other obligation is enforceable—without additional consideration—if it is signed by the party against whom the modification is being enforced. MCL 566.1.

The complete failure of consideration warrants rescission of a contract. *Adell Broadcasting v Apex Media Sales*, 269 Mich App 6, 12; 708 NW2d 778 (2006). Failure of consideration occurs when the consideration that existed at the time the contract was formed becomes worthless or ceases to exist. *Id.* at 12-13 (quoting *Black's Law Dictionary* (5th ed)). Impossibility of performance is the usual grounds for finding the failure of consideration. E.g., *Vowels v Arthur Murray Studios of Mich, Inc*, 12 Mich App 359, 363; 163 NW2d 35 (1968).

Failure of consideration is different from and greater than a breach of the contract. *Adell*, 269 Mich App at 13 (citing *Abbate v Shelden Land Co*, 303 Mich 657, 666; 7 NW2d 97 (1942)).

Here, the parties modified their existing business relationship and set forth the modified agreement in two separate writings that were signed by both parties. (Ex B, EMI; Ex C Nondisclosure Agreement.) No additional consideration was necessary as the parties were modifying their existing oral contractual relationship. See MCL 566.1. But even if additional consideration was necessary, it was provided. As the Court of Appeals identified, the EMI and the Nondisclosure Agreement recite that on-going business relationship *is* part of the consideration for the agreements. (COA Op 10; Ex B EMI 1; Ex C Nondisclosure Agreement 1.) As a matter of Michigan law, that consideration is enough.

The Nondisclosure Agreement does not contain a term provision. The EMI does, providing that the contract expires upon K&L Development and Krause's completion of their services under the Agreement, upon material breach by Krause or K&L Development, or upon 14 days advance written notice from any party. (Ex B, EMI § 12.1.) The parties were thus on reasonable notice that their ongoing business relationship, in the absence of material breach, could be as short as 14 days. Again, such an on-going relationship is more than the proverbial penny or peppercorn, and it is legally sufficient consideration. See *Gen Motors*, 466 Mich at 239.

The Court of Appeals recognized that the trial court erred in assessing the adequacy of the consideration provided by the parties' agreements, but sought to rectify that error by re-characterizing the issue as one of failure of consideration.[4] (COA Op 10-12.) Defendants did

[4] Absence of consideration and failure of consideration is an affirmative defense, and the burden of proving failure of consideration rests on the party asserting it. MCR 2.119(F)(3)(a); *Adell*, 269 Mich App at 12 (citing *Turner v Peoples State Bank*, 299 Mich 438, 450; 300 NW 353

not argue failure of consideration to the Court of Appeals—it was raised *sua sponte* by the Court of Appeals' opinion. (See Appellee's Br 29-32.) The Court of Appeals contended that "Krause and K&L Development never received that which they were promised under the agreements," and "[w]here plaintiff terminated the business relationship within two weeks after the agreements were signed, plaintiff's forbearance in terminating the relationship amounted to a nullity." (COA Op 11.) The court supported its assessment by citing cases from foreign jurisdictions holding that "continued employment promised in exchange for signing a non-compete agreement must be 'for a substantial time'." (*Id.* (quoting *Lucht's Concrete Pumping v Horner*, 255 P3d 1058, 1063 (Colo, 2011); citing additional cases from applying the law of Illinois, Vermont, New York, Tennessee, and Maryland).)

The Court of Appeals' analysis errs for two reasons. *First*, the court characterized purported non-performance of the contract by Innovation Ventures as failure of consideration. There is no evidence that Innovation Ventures failed to perform or otherwise breached the parties' contracts. The parties agreed that the business relationship could be terminated by either party on 14-days' notice or upon material breach. (Ex B, EMI § 12.) The record does not disclose precisely how long after the contracts with K&L Development and Krause were executed before the parties' relationship ended other than that it ended in May 2009. (See Krause Aff ¶ 5.) And because discovery was not even close to being completed, there is no record evidence as to why or how the relationship ended. Nonetheless, on this record vacuum, the Court of Appeals concluded that the relationship ended two weeks after the agreements were executed. (COA Op 11; accord 3/15/13 Op & Order 24, 26.) Thus, even when facts favorable to

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(1941) (Boyle, J, concurring)). Defendants Krause and K&L Development never pled lack of consideration as an affirmative defense. (Krause and K&L Development's Answer to 2d Am Compl 18-19.) Both courts identified their own grounds for refusing to enforce the parties' agreements.

Krause and K&L Development are assumed, Innovation Ventures performed the consideration anticipated in the EMI.

Performance of the contract was not rendered impossible. The Court of Appeals may have implicitly concluded that the continuation of the business relationship for two weeks was worthless (COA Op 10-12), but to do so it had to draw factual inferences in favor of Defendants contrary to the standard of review applicable to motions for summary disposition. Accordingly, the Court of Appeals' characterization of the termination of the parties' business relationship as a failure of consideration is wrong.

Second, the Court of Appeals adopted a standard from other states that requires "substantial" continued employment as consideration for nondisclosure and non-competition covenants. (*Id.* at 10-11.) This standard is inconsistent with this Court's jurisprudence that courts do not assess the legal sufficiency of consideration. *Gen Motors*, 466 Mich at 239 & n 13 (noting that this principle is almost as old as the doctrine of consideration itself (quoting 3 Williston, Contract (4th ed), § 7:21, pp 383-386)). See *Curtis 1000, Inc v Seuss*, 24 F3d 941, 946 (CA 2, 1994) (noting that requirement of a "substantial period" is a departure "from the traditional refusal to inquire into the adequacy of consideration.") The Court of Appeals offered no justification for why this rule does not apply to contracts like the EMI and Non-Disclosure Agreements that contain confidentiality, non-disclosure, and non-competition provisions. Nor did the Court of Appeals cite any basis in Michigan law for this proposition.

That is because, under Michigan law, there is no basis for the Court of Appeals' incorporation of a minimum-duration requirement where a continued business relationship is the consideration for a contract. To the contrary, the Court of Appeals' ruling artificially limits parties' ability to freely contract by imposing a judicial assessment of what is reasonable or beneficial. As a result, the Court of Appeals' approach enmeshes the Michigan courts in attempting to discern precisely **what** constitutes a substantial continuation of the relationship. According to the Court of Appeals, two weeks is apparently not enough. Is a month? Six months? A year? Such uncertainty undermines existing non-competition agreements throughout the state, and creates uncertainty in future employment, independent-contractor, supplier, and service relationships. Further, imposing a specific durational term hinders a party's ability to terminate a relationship for cause without risking the loss of its protection from unfair competition.

This case is an excellent vehicle to address the "substantial time" issue. Because discovery on this issue never occurred, the Court of Appeals' ruling results in a bright-line rule: employment or a business relationship must continue for a considerable time—definitely more than two weeks—to provide consideration for a non-competition agreement, regardless of the reason for the benefitted party's termination of the relationship. Indeed, given the standard for granting summary disposition, any inference to be drawn regarding why Krause and K&L Development's relationship with Innovation Ventures ended must favor Innovation Ventures.

Accordingly, this Court should grant leave to appeal and reject the Court of Appeals' failure-of-consideration analysis, or peremptorily reverse the Court of Appeals' decision.

II. The Court of Appeals erred by concluding that Liquid's agreement to manufacture energy-shot products only for pre-approved competitors was unenforceable.

Innovation Ventures allowed Liquid to use its customized energy-shot production equipment royalty free to manufacture competing energy drinks, subject to Innovation Venture's prior approval. Innovation Ventures could have prevented Liquid from producing *any* competing products by simply removing its equipment after it transitioned production in-house or enforcing Liquid's three-year exclusivity obligation. But because Innovation Ventures acceded to Paisley's request and allowed limited competition, the lower courts determined its agreement with Liquid was an unreasonable and unenforceable non-competition agreement. The Court of Appeals' analysis misapplies the rule of reason because it focuses on the heightened scrutiny imposed by the Legislature on employment non-compete agreements and fails to consider the pro-competition effect of the Termination Agreement.

The Michigan Antitrust Reform Act ("MARA") applies to determine the enforceability of non-compete agreements. See *Bristol Window & Door, Inc v Hoogenstyn*, 250 Mich App 478; 650 NW2d 670 (2002). Section 2 of MARA sets forth a general standard: "A contract, combination, or conspiracy between 2 or more persons in restraint of, or to monopolize, trade or commerce in a relevant market is unlawful." MCL 445.772. In Section 4a, the Legislature adopted a separate provision addressing covenants not to compete in the employment setting. MCL 445.774a. That provision states, in relevant part, as follows:

> An employer may obtain from an employee an agreement or covenant which protects an employer's reasonable competitive business interests and expressly prohibits an employee from engaging in employment or a line of business after termination of employment if the agreement or covenant is reasonable as to its duration, geographical area, and the type of employment or line of business. [MCL 445.774a(1).]

Covenants not to compete contained in non-employment contexts are not subject to Section 4a, and are analyzed under Section 2. *Bristol Window*, 250 Mich App 494-498.

Courts have interpreted MCL 445.772 to incorporate the common-law rule of reason first adopted by this Court in 1873. *Id.* at 486, 494-495. Cf. *State Oil Co v Khan*, 522 US 3, 10 (1997) (noting that the federal courts have adopted the same analysis with regard to similar language in the Sherman Act). The rule of reason provides that contracts in restraint of trade are valid "if, considered with reference to the situation, business and objects of the parties, and in the light of all the surrounding circumstances with reference to which the contract was made, the restraint contracted for appears to have been for a just and honest purpose, for the protection of the legitimate interests of the party in whose favor it is imposed, reasonable as between them and not specifically injuries to the public . . . ." *Hubbard v Miller*, 27 Mich 15, 19 (1873).

Under the analogous provisions of the Sherman Act, the United States Supreme Court has explained that among the circumstances that must be considered is whether the agreement has anticompetitive effects. See *Continental T V, Inc v GTE Sylvania Inc*, 433 US 36, 59 (1977). There must be an actual adverse effect on competition as a whole in the relevant market. *Major League Baseball Props, Inc v Salvino, Inc*, 542 F3d 290 (CA 2, 2008). In other words, for an agreement to be an unlawful restraint on trade, it must have an actually anticompetitive effect in the market.

In 2006, the Court of Appeals asserted that Section 4a(1) of MARA codified the rule of reason that had already been applied under Section 2. *St Clair Med, PC v Borgiel*, 270 Mich App 260, 265-266; 715 NW2d 914 (2006) (citing *Bristol Window*, 250 Mich App at 495). The *St Clair Medical* decision effectively reinterpreted the rule of reason to require the heightened analysis of employment non-competes adopted by the Legislature in Section 4a(1). *Id.* Specifically, the rule adopted in *St Clair Medical* melds Section 4a with the rule of reason:

> [A] restrictive covenant must protect an employer's reasonable competitive business interests, but its protection in terms of duration, geographical scope, and the type of employment or line of business must be reasonable. Additionally, a restrictive covenant must be reasonable as between the parties, and it must not be specially injurious to the public. [*St Clair Med*, 270 Mich App at 266.]

This analysis is entirely appropriate in the context of an employment non-competes. But it cannot be applied in reverse to define the rule of reason as applied to non-compete agreements among sophisticated commercial parties.

As the Court of Appeals explained in *Bristol Window*, the Legislature's repeal of an earlier statute barring non-compete agreements and adoption of MARA revived the rule of reason as to all restrictive covenants including non-compete agreements. 250 Mich App at 492-496. The adoption of Section 4a resulted in additional analysis of reasonableness for covenants not to compete in the employment setting. *Id.* at 494-496; MCL 445.774a. Consequently, non-competition provisions in commercial contracts must meet the four standards established in *Hubbard*:

> First, the covenant must be for an honest and just purpose. Second, it must be established for the protection of the legitimate interest of the party in whose favor it is imposed. Third, it must be reasonable as between the parties to the contract. Finally, it must not be specially injurious to the public. [*Cardiology Assoc of SW Mich, PC v. Zencka*, 155 Mich App 632, 636; 400 NW2d 606 (1985).]

As *Hubbard* demonstrates, this analysis must be done with a view to the entire context surrounding the agreement and not just the text of the agreement itself. *Hubbard*, 27 Mich at 19.

Here, even though the Termination Agreement does not involve employment, and even though the issue was expressly addressed at oral argument, the Court of Appeals inexplicably applied the *St Clair Medical* synthesis of the rule of reason and MCL 445.774a. (COA Op 6, 7-8 (citing *St Clair Med*, 270 Mich App 266).) In so doing, the Court of Appeals erred. That error led the Court of Appeals to ignore the context of the parties' Termination Agreement and focus on the contract itself.

None of the contracts at issue in this case involve employment. Nor do any of them arise in a context where an individual or a company is prevented from earning a livelihood. Kraus and K&L Development assisted other companies with manufacturing solutions. Liquid existed as a contract bottler before working with Innovation Ventures. This situation arose because Innovation Ventures chose to **allow** limited competition.

In an analogous situation, the Court affirmed an agreement under the rule of reason because the agreement did nothing to decrease competition. *Staebler-Kempf Oil Co v Mac's Auto Mart, Inc*, 329 Mich 351, 357; 45 NW2d 316 (1951). In *Staebler-Kampf*, the Court enforced an argument requiring the purchasers of a gas station to buy gasoline from the property seller and setting the price the station purchaser could charge for the fuel. The Court reasoned that because "there can be no question" that the property seller could have imposed the same requirements if it had retained ownership, the property seller could impose those same requirements on the buyer. *Id.* The Court then noted the absence of any significant anticompetitive effort. *Id.* at 358. Here, the same analysis applies.

Under the parties' Manufacturing Agreement, Innovation Ventures was entitled to remove all of its production equipment, and Innovation Ventures had the right to purchase any production equipment that Liquid had acquired to produce 5-hour Energy. (Ex A, Am Mfg Agreement §§ 8.d., 20.b.) Given the absence of off-the-shelf production lines for producing energy-shot drinks, removal of the production equipment would have effectively prevented Liquid from bottling any energy drinks. Period. (See Dolmage Aff ¶ 7.) Further, Liquid agreed not to produce competing energy drinks for the duration of the Manufacturing Agreement and three years after termination. (Ex A, Am Mfg Agreement § 17.) There is little question that the exclusivity provision in the Manufacturing Agreement was valid to protect Innovation Ventures' goodwill and confidential information. *Rooyakker & Sitz, PLLC v Plante & Moran, PLLC*, 276 Mich App 146, 158; 742 NW2d 409 (2007) (protecting confidential information is a legitimate business reason for a non-competition agreement); *St Clair Med*, 270 Mich App at 268 (protecting goodwill is a valid business reason). Consequently, under the Manufacturing

Agreement, Liquid was practically and legally prohibited from bottling energy-shot drinks until April 22, 2012, i.e. three years.

The parties' Termination Agreement superseded the Manufacturing Agreement. (Ex D, Termination Agreement § 22.) The Termination Agreement promoted competition in the energy-shot market in two ways. First, Innovation Ventures released Liquid from the Manufacturing Agreement's broad non-compete, allowing Liquid to bottle some competitors' products. (*Id.* §§ 1, 24(i), Ex C.) Liquid agreed to obtain Innovation Ventures' approval before producing any competing product for the same three-year period as the Manufacturing Agreement. (*Id.* § 1.b.) The competitors whose products Liquid was authorized to produce were not just small players with a limited distribution; they included Red Bull, the largest player in the energy-drink market. (*Id.* at Ex C.)

Second, despite purchasing the production equipment, Innovation Ventures left the customized production equipment at Liquid's facility and gave Liquid the license to use Innovation Ventures' equipment royalty free. (*Id.* §§ 6, 14.) When the parties executed the Termination Agreement, it *promoted* competition by allowing Liquid to use Innovation Ventures' customized production equipment to manufacture and package competitors' products.

Further, the record demonstrates that in addition to promoting competition, albeit limited competition, the permitted-products limitation in the Termination Agreement served several other purposes: (1) preventing representations by competitors in which they traded on Innovation Ventures' goodwill by reporting that their product was being made by the same company that made 5-hour Energy (Dolmage Aff ¶ 11); (2) avoiding the misappropriation of Innovation Ventures' confidential information and intellectual property including ingredients, formulas, packaging techniques, and distribution network (*id.*); (3) protecting Innovation Ventures' legitimate interest in its otherwise proprietary information; and (4)avoiding the promotion of competitors' products that infringed on 5-hour Energy's trademark (see 9/20/2010 email from Criso to Kulpa).

By focusing on the wrong legal standard for evaluating a commercial non-compete, the Court of Appeals did not address the context in which the Termination Agreement arose. Instead, the court identified the various limitations imposed on Liquid's ability to bottle competitors' products and concluded that the parties' agreement was unreasonable. The effect of the Court of Appeals' decision is pernicious—Innovation Ventures was apparently required to prevent *any* competitive use of its production equipment or allow *all* competitive use. The rule of reason is not so limited.

Accordingly, the Court should grant leave to appeal and restore the appropriate application of the rule of reason to non-compete agreements that arise in a non-employment context.

III. The Court of Appeals' requirement that a party identify specifically which trade secrets and confidential information was misappropriated without discovery is unworkable.

The judgment in this case was entered before discovery closed, before the Defendants produced any meaningful written discovery, and before any depositions were taken. Nonetheless, the Court of Appeals criticized Innovation Ventures for being unable to identify the specific trade secrets and confidential information that Defendants had misappropriated. (COA Op 13.) However, in misappropriation of trade secrets cases involving the inevitable-disclosure doctrine, it is frequently impossible for a plaintiff to be able to identify the specific confidential information and trade secrets that were actually misappropriated until *after* discovery is completed.

"Generally, a circuit court should not grant summary disposition unless no fair likelihood exists that additional discovery would reveal more support for the nonmoving party's position." *Wurtz v Beecher Metro Dist*, 495 Mich 242, 258; 848 NW2d 121 (2014). Michigan "has a strong historical commitment to a far-reaching, open, and effective discovery practice." *Dorris v Detroit Osteopathic Hosp Corp*, 460 Mich 26, 36; 594 NW2d 455 (1999). The fact that discovery remains open does not automatically mean that the decision to grant summary disposition is premature. *Marilyn Froling Revocable Living Trust v Bloomfield Hills Country Club*, 283 Mich App 264, 292; 769 NW2d 234 (2009). Instead, a plaintiff arguing that additional time for discovery is necessary must "articulate the support she had for her allegations regarding a factual dispute." *VanVorous v Burmeister*, 262 Mich App 467, 478; 687 NW2d 132 (2004).

For a case before this Court on a ruling entered under MCR 2.116(C)(10), this case is in a strange procedural posture. Summary disposition was granted before discovery was completed and without Defendants having even raised in their second summary disposition motion a legal argument supporting dismissal of Innovations Ventures' trade-secret misappropriation claim. Indeed, discovery had been truncated by several lengthy stays imposed by the circuit court. As the Court of Appeals noted, the circuit court even stayed discovery in order to prevent Innovation Ventures from conducting discovery against third parties and to allow Defendants to move for summary disposition. (COA Op. 4.) Despite the complexity of the issues in this case, the parties' lengthy relationship, and the undoubted communications between Paisley and Liquid and Krause and Eternal Energy, no discovery regarding those subjects ever occurred despite several pending sets of discovery requests to the Defendants. And no depositions were taken by any party.

Nonetheless, the circuit court granted summary disposition to Defendants not only on the contract claims for which they had argued summary disposition, but on all of Innovation Ventures' non-contract claims. (3/15/2013 Op & Order 28-37.) The circuit court *sua sponte* reached the remaining claims and concluded no genuine issues of material fact existed. (*Id.*). This result is especially anomalous given that a few months before, the circuit court had concluded that summary disposition on those very counts was *not* appropriate due to questions of material fact.[5] (6/15/2012 Op & Order 5)

In its briefing to the Court of Appeals, Innovation Ventures identified no less than 20 issues on which discovery was needed. (Appellant's Br 13-15.) The court nonetheless concluded that additional discovery was not necessary because Innovation Ventures "did not provide independent factual evidence that a factual dispute exists." (COA Op 17.) The Court erred because Innovation Ventures *did* present evidence from which it was reasonable to conclude a factual dispute exists, and because the very nature of a case involving claims that a party misappropriated trade secrets makes imposing such a burden before meaningful discovery unworkable.

Throughout this case, Innovation Ventures has repeatedly identified the jarring fact that Krause and Eternal Energy were able to near instantly move from marketing their energy-shot drink at five tattoo parlors to a $40 million contract with Wal-Mart. That kind of market move simply does not happen absent use of the type of confidential and trade secret information that Innovation Ventures made available to Defendants pursuant to the parties' contracts. (See 2d Am Verified Compl ¶¶ 7, 85-87.) There is a genuine dispute between the parties regarding

[5] Innovation Ventures thus did not even have the opportunity before summary disposition was granted to argue that additional discovery was necessary as to the non-contract claims and submit affidavits demonstrating the additional facts and/or factual disputes that would have be elucidated by additional discovery.

whether Krause obtained any confidential or trade secret information while working with Innovation Ventures. (Krause Aff ¶ 4; Dolmage Aff ¶¶ 12, 20-21; Henderson Aff ¶¶ 8-12, 15-16.) There is no dispute that Krause, K & L Development, Liquid, and Paisley had access to significant confidential information regarding Innovation Ventures' suppliers, marketing, ingredients, costs, production techniques, manufacturing process, formulas, and packaging. (Dolmage Aff ¶ 11-12; Henderson Affidavit ¶ 9-12.) There is also no dispute that Defendants were unfamiliar with the energy-shot drink market before working with Innovation Ventures. (Henderson Aff ¶ 8; see Krause Aff ¶ 6.) Consequently, the very fact that after their relationship with Innovation Ventures ended, Defendants started a competing business and had immediate success is sufficient to demonstrate that there was a fair likelihood that additional discovery would reveal more support for Innovation Ventures' position.

Moreover, the very nature of this dispute—whether a party misappropriated another party's trade secrets—almost always involves calculated efforts to conceal the relevant conduct from the plaintiff. Very few cases involving the use of confidential information and the misappropriation of trade secrets arise where the defendants openly identify what they have done. Instead, the reality is that this sort of conduct occurs in secret, usually with deliberate efforts by the defendant to prevent the plaintiff from learning what has occurred. See *Kubik, Inc v Hull*, 56 Mich App 335, 340; 224 NW2d 80 (1974) (noting that documents and testimony showed efforts by defendants to conceal their efforts to misappropriate plaintiffs' trade secrets); *Dana Ltd v Am Axle & Mfg Holdings, Inc*, 2012 WL 2524008, at *8 (WD Mich, June 29, 2012) (weighing defendants "surreptitious" activity, and participation in projects done for new employer that "paralleled" projects done for plaintiff"). Discovery is needed to identify what has occurred, especially the production of emails and depositions of the appropriate parties. The

Court of Appeals' expectation of additional independent evidence of Defendants' misappropriation of Innovation Ventures' confidential information and trade secrets is unworkable.

For this additional reason, the Court should grant leave to appeal and reverse, or peremptorily reverse the Court of Appeals' decision and remand this case for additional proceedings in the circuit court.

CONCLUSION AND REQUESTED RELIEF

For all the foregoing reasons, the Court should grant leave to appeal and reverse, or peremptorily reverse and remand the case to trial court for further proceedings.

Respectfully submitted,

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