TO PREEMPT OR NOT TO PREEMPT: THE TEXAS SPLIT ON TUTSA'S PREEMPTION OF BREACH OF FIDUCIARY DUTY

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In September 2013, the Texas Legislature passed the Texas Uniform Trade Secret Act (TUTSA).[1] With minor exceptions, TUTSA mirrors the Uniform Trade Secret Act (UTSA).[2] Texas lawmakers enacted this legislation to help trim the fat on trade secret litigation by eliminating inconsistent theories of common law relief for the same types of harm.[3] Previously, too many common law claims on the misuse of trade secrets existed that essentially claimed the same thing.[4] So, TUTSA did what its title claimed—it unified trade secret law in the state of Texas by creating a singular path for litigating the abuse of one's trade secrets.[5]

However, since TUTSA's enactment, the path for trade secret litigation has been unpredictable. Lawyers struggle to navigate exactly what claims, once readily at their disposal prior to TUTSA, are still in their toolbox. Currently, a split of opinions exists across the federal district courts on what claims are replaced or "preempted" by TUTSA.[6]

This article intends to clarify that split, specifically the division of opinions on whether a breach of fiduciary duty claim based on the misuse of confidential information is replaced with or "preempted" by TUTSA. This article explores TUTSA and its preemption provision before digging into the majority approach on this matter as represented in *Embarcadero v. Redgate*,[7] and the minority approach represented in *DHI v. Kent*.[8]

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1. TEX. CIV. PRAC. & REM. CODE ANN. § 134A.001. In doing so, Texas joined what would become 47 states that have adopted some form of the Uniform Trade Secret Act. *Trade Secret*, CORNELL LAW INST. https://www.law.cornell.edu/wex/trade_secret#:~:text=Overview,Columbia%20have%20adopted%20the%20UTSA (last visited Mar. 21, 2023).

2. Among the differences to UTSA, TUTSA contains a slightly broader definition of trade secrets that would encompass customer lists. It also eliminated the requirement that information be in "continuous use" to be a trade secret. Michelle Evans, *The Uniform Trade Secrets Act Makes Its Way to Texas*, 23 TEXAS INTELL. PROP. L. J. 25, 28 (2013).

3. ScaleFactor, Inc. v. Process Pro Consulting, LLC, 394 F. Supp. 3d 680, 684 (W.D. Tex. 2019) (quoting Super Starr Int'l, LLC v. Fresh Tex Produce, LLC, 531 S.W. 3d 829, 843 (Tex. App.—Corpus Christi–Edinburg 2017) ("[T]he purpose of TUTSA preemption is to 'prevent inconsistent theories of relief for the same underlying harm by eliminating alternative theories of common law recovery which are premised on the misappropriation of a trade secret.")).

4. For example, in *Embarcadero Techs., Inc. v. Redgate Software, Inc.*, No. 1:17-CV-444-RP, 2018 WL 315753 (W.D. Tex. Jan. 5, 2018), the plaintiff combined a breach of fiduciary duty claim, based solely on the misappropriation of trade secrets, with a misappropriation of trade secrets claim under TUTSA.

5. Cleveland & Coffman, *Protecting Trade Secrets Made Simple*, 76 Tex. B.J. 751 (2013) ("TUTSA codifies and modernizes Texas law on misappropriation of trade secrets by providing a simple legislative framework for litigating trade secret cases.")

6. *See Embarcadero*, 2018 WL 315753 at *2.

7. *Embarcadero*, 2018 WL 315753.

8. DHI Grp., Inc. v. Kent, 397 F. Supp. 3d 904 (S.D. Tex. 2019).

I. TUTSA AND ITS PREEMPTION PROVISION

TUTSA helps unify trade secret causes of action by first providing a definition, albeit broad, of the type of information that can be considered a trade secret. Section 134A.002(6) of the Act defines trade secret information to include:

> [A]ll forms and types of information, including business, scientific, technical, economic, or engineering information, and any formula, design, prototype, pattern, plan, compilation, program device, program, code, device, method, technique, process, procedure, financial data, or list of actual or potential customers or suppliers, whether tangible or intangible and whether or how stored, compiled, or memorialized physically, electronically, graphically, photographically, or in writing.[9]

Still, the Act preserves the standard legal test for determining what information qualifies as a trade secret, namely that (1) the owner employs "reasonable measures" to keep the information secret,[10] and (2) the information must derive some independent economic value from not being readily available or easily ascertainable by another person.[11]

Not only does TUTSA unify trade secret law by providing a comprehensive definition, but TUTSA also unifies trade secret law by preempting other competing or similar civil claims. The Act contains a preemption provision which states the Act "displaces conflicting tort, restitutionary, and other law of this state providing civil remedies for misappropriation of a trade secret."[12] However, from reading the statute, one can assume the legislature did not want to displace claims unrelated to trade secrets. According to the plain text of the statute, the preemption does not affect "other civil remedies that *are not based upon misappropriation of a trade secret*."[13]

Some non-TUTSA civil claims are factually and legally based on misappropriation of trade secrets and are quickly preempted and dismissed by Texas courts. For example, complaints alleging violations of Texas's Harmful Access by Computer Act (HACA) and the Texas Theft Liability Act (TTLA) are doomed to preemption.[14] As an illustrative example, under TTLA, "a person who commits theft is liable [civilly] for the damages resulting from the theft."[15] In other words, the TTLA

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9. TEX. CIV. PRAC. & REM. CODE ANN. § 134A.002(6) (West 2013).
10. *Id.* at § 134A.002(6)(A).
11. *Id.* at § 134A.002(6)(B).
12. *Id.* at § 134A.007.
13. *Id.* (emphasis added).
14. ScaleFactor, Inc. v. Process Pro Consulting, LLC, 394 F. Supp. 3d 680, 685 (W.D. Tex. 2019) ("Like its conversion claim . . . ScaleFactor's HACA claim is preempted by TUTSA."); Stone-Coat of Texas, LLC v. ProCal Stone Design, LLC, 426 F. Supp. 3d 311, 332 (E.D. Tex. 2019) ("The enrolled bill, known as the TUTSA, became effective on September 1, 2013, and displaces both common-law misappropriation-of-trade-secret and TTLA theft-of-trade-secret claims.").
15. *In re* Minardi, 536 B.R. 171, 185 (Bankr. E.D. Tex. 2015).

allowed someone to sue another for misappropriating their trade secrets. TUTSA preempts this claim. A plaintiff could not make both the TTLA claim and a TUTSA claim.[16]

Likewise, other civil remedy claims are preempted when they are clearly based on the same facts as the misappropriation of a trade secret claim. For example, conversion or unfair competition claims are preempted if the alleged theft is of alleged trade secrets[17] and the alleged unfair competition is due to the alleged misuse of another's trade secrets.[18] For example, in *StoneCoat v. Procal*, the plaintiff allegedly met with the defendant so that the defendant could decide whether to invest in their company.[19] During that meeting, StoneCoat shared confidential information.[20] The defendant declined to invest and instead allegedly took the information from the meeting and created a competing company to the plaintiff's detriment.[21] The plaintiff filed claims, including conversion and TUTSA misappropriation.[22] The Eastern District of Texas dismissed the conversion claim at summary judgment because the conversion and misappropriation claims came from the same facts. The conversion claim arose out of the defendant misappropriating, or "stealing," trade secrets; thus, TUTSA preempted.[23]

However, there is a conflict as to the application of the TUTSA preemption provision when a complaint alleges the taking of confidential information that may or may not fall under the definition of a TUTSA trade secret.[24] How could a claim be preempted if, contrary to the exception, the remedy is not based on misappropriating a trade secret, but rather on the taking of confidential information? While other non-TUTSA civil claims face similarly conflicting applications of the preemption provision, the way courts handle a claim for "post-employment" breach of fiduciary duty most clearly illustrates the divide on this matter.

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16. *StoneCoat*, 426 F. Supp. 3d at 332.

17. *Id.* at 337-38 ("ScaleFactor's conversion claim is fundamentally concerned with the unauthorized acquisition [and later destruction] of company information, 'some but not all of which is trade-secret'") (quoting *ScaleFactor*, 394 F. Supp. 3d at 685) ("... Because ScaleFactor's TUTSA and conversion claims each 'stem from the same underlying harm—the taking of [ScaleFactor's] confidential information'—its conversion claim is preempted by TUTSA.").

18. *Id.* ("The harm stemming from this claim and Plaintiffs' TUTSA claim are the same – the taking of Plaintiffs' confidential information. Like the conversion claim, the Court finds Plaintiffs' unfair competition claim is preempted by TUTSA.").

19. *Id.* at 318.

20. *Id.*

21. *Id.*

22. *Id.*

23. *Id.* at 337-38.

24. *Id.* at 337 ("Here, Plaintiffs' unfair competition claim is 'fundamentally concerned' with the unauthorized acquisition of StoneCoat information, 'some but not all of which is trade-secret.'").

II. "POST-EMPLOYMENT" BREACH OF FIDUCIARY DUTY

A fiduciary duty does not solely exist between lawyers and clients, doctors and patients, or trustees and beneficiaries. Instead, a fiduciary duty may be found in any "confidential relationship[,] [which] may be found whenever one party is justified in reposing confidence in another."[25] For instance, an employer can be uniquely vulnerable to an employee, especially a high-ranking one, where valuable information is learned that could be used against the employer. Therefore, courts will review the nature of the employer/employee relationship to determine whether a fiduciary duty exists and act from there.[26]

When a fiduciary duty exists between an employee and employer, "the employee has a duty to act primarily for the benefit of the employer in matters connected with his agency."[27] This duty requires the employee not to compete with the employer directly in their business or disclose matters that may affect the business.[28] The employee may breach their fiduciary duty if, for example, he appropriates trade secrets during employment, solicits the employer's customers while still working for the employer, or recruits other employees to work for him later in a competing business.[29]

Further, the employer-employee fiduciary duty persists even after employment in one specific instance. The employee retains the duty to not use confidential information given to him during employment.[30] For the purposes of this article, this type of breach of fiduciary duty will be referred to as a "post-employment" breach of fiduciary duty.

Long before TUTSA, litigators filed a "post-employment" breach of fiduciary duty type claim along with a misappropriation of trade secrets claim.[31] The rationale was to increase potential damages by tacking on the types of damages a breach of fiduciary duty claim would allow, namely disgorgement fees and a cause of action against anyone who may have acted in "knowing participation" of the breach.[32] The latter would allow for an attack on deeper pockets.[33]

Attaching a breach of fiduciary duty claim in a post-TUTSA Texas lawsuit may, however, fall flat depending on which court the claim is made in. As introduced earlier, there is a judicial divide as to whether

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25. Tolson Firm, LLC v. Sistrunk, 789 S.E.2d 265, 268 (2016).

26. *See id.*

27. Abetter Trucking Co. v. Arizpe, 113 S.W.3d 503, 510 (Tex. App.—Houston [1st Dist.] 2003, no pet.).

28. *Id.*

29. *Id.* at 512.

30. *Id.*

31. Zach Wolfe & Paul T. Freeman, *Trade Secrets 101: What Texas Businesses and Their Lawyers Need to Know*, 48 TEX. J. BUS. L. 1, 15 (2019).

32. *Id.*

33. *Id.*

TUTSA preempts a "post-employment" breach of fiduciary duty claim.[34] The Southern District of Texas represents the "minority approach" of this divide.[35] Meanwhile, the rest of Texas follows the "majority approach."[36]

III. THE MAJORITY APPROACH TO TUTSA PREEMPTION

In *Embarcadero v. Redgate*, the Western District of Texas provided the first holding on the preemption of breach of fiduciary duty claims by TUTSA.[37] There, the plaintiffs alleged the defendant left the company with confidential information in tow and formed a competing company to the plaintiffs' detriment.[38] Plaintiffs brought a variety of claims, including both misappropriation of trade secrets and breach of fiduciary duty.[39] The breach of duty was based solely on the use of confidential information against the employer after the employee ceased working for the employer.[40] In other words, the plaintiff alleged a "post-employment" breach of fiduciary duty claim.

The defendants argued that TUTSA preempted the breach of fiduciary duty claim.[41] The plaintiff, however, claimed the breach of fiduciary duty claim only alleged improper taking of confidential information; therefore, it should not be preempted by TUTSA.[42] Acknowledging a lack of case law in Texas on TUTSA's preemption on this particular type of claim, the court reviewed the reasoning of a similar matter in a Texas state appeals court and courts in other states that employed the Uniform Trade Secret Act (UTSA) in their jurisdictions.[43] The court also analyzed the text of the preemption provision itself.[44]

The court then applied what legal scholars label the "majority approach" to the issue.[45] Prior to the case, a majority of UTSA-adopting jurisdictions determined that UTSA's intent was to displace any claim based on the misuse of information.[46] The Texas court found this reasoning persuasive and held that "TUTSA's preemption provision

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34. *See* Embarcadero Techs., Inc. v. Redgate Software, Inc., No. 1:17-CV-444-RP, 2018 WL 315753, at *2 (W.D. Tex. Jan. 5, 2018).

35. DHI Grp., Inc. v. Kent, 397 F. Supp. 3d 904, 923 (S.D. Tex. 2019).

36. *Embarcadero*, 2018 WL 315753, at *3.

37. *Embarcadero*, 2018 WL 315753.

38. *Id.* at *2.

39. *Id*.

40. *Id.*

41. *Id.*

42. *Id.*

43. *Id.* at *2-3 (analyzing Super Starr Int'l, LLC v. Fresh Tex Produce, LLC, 531 S.W.3d 829, 843 (Tex. App.—Corpus Christi-Edinburg 2017, pet. granted)).

44. *Id.* at *2.

45. *Id.* at *3.

46. *Id.*

encompasses all claims based on the alleged improper taking of confidential business information" and not just information that qualifies as a trade secret.[47] The court was not concerned with the fact that some of the mishandled information could have been simply confidential and not rise to the status of trade secret, finding "[t]he fact that some of the confidential information taken may not fit the statutory definition of trade secret does not change the outcome."[48] The court granted the motion for summary judgment for the defendant and the "post-employment" breach of fiduciary duty was preempted.[49]

Over a number of cases, the Northern, Eastern, and Western Districts of Texas have applied the same "majority approach" utilized in *Embarcadero*.[50] In some of these cases, it appears that preemption at summary judgment could be avoided with some careful pleading. In fact, in *Embarcadero*, the court reasoned the breach of fiduciary duty claim was preempted, partly due to the plaintiffs' allegation that a breach of fiduciary duty occurred because of the defendants' use of confidential information *and* trade secrets.[51] However, a recent Northern District of Texas case suggests that there is no way to plead around the breach of fiduciary duty preemption in courts that apply the majority approach. In *DeWolff v. Pethick*, the plaintiff's "post-employment" breach of fiduciary duty claim pleaded only the misuse of confidential and proprietary information.[52] There, the court was not persuaded that the claim side-stepped preemption, finding such a claim to be preempted "regardless of the labels used by [p]laintiff in its pleading to describe the information at issue."[53]

Accordingly, regardless of how a litigator approaches their complaint, the TUTSA preemption provision looms in any court in Texas that applies the "majority approach." Instead, a breach of fiduciary duty

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47. *Id.*

48. *Id.* at *4.

49. *Id.*

50. *See generally* Comput. Sci. Corp. v. Tata Consultancy Servs. Ltd, No. 3:19-CV-970-X(BH), 2020 WL 2487057 (N.D. Tex. Feb. 7, 2020); StoneCoat of Texas, LLC v. ProCal Stone Design, LLC, 426 F. Supp. 3d 311 (E.D. Tex. 2019); ScaleFactor, Inc. v. Process Pro Consulting, LLC, 394 F. Supp. 3d 680 (W.D. Tex. 2019); Title Source, Inc. v. HouseCanary, Inc., 612 S.W.3d 517 (Tex. App.—San Antonio 2020, no pet.); UATP Mgmt., LLC v. Leap of Faith Adventures, LLC, 02-19-00122-CV, 2020 WL 6066197, at *7 (Tex. App.—Fort Worth 2020, no pet.); BKL Holdings, Inc. v. Globe Life Inc., No. 4:22-CV-00170, 2023 WL 2432012 (E.D. Tex. Mar. 9, 2023); DeWolff, Boberg & Assocs., Inc. v. Pethick, No. 3:20-CV-3649-L, 2022 WL 4589161 (N.D. Tex. Sept. 29, 2022); Philips N. Am. LLC v. Image Tech. Consulting, LLC, No. 3:22-CV-0147-B, 2022 WL 17168372 (N.D. Tex. Nov. 21, 2022).

51. *Embarcadero*, 2018 WL 315753, at *4 ("Here, Plaintiffs' sole basis for their breach of fiduciary duty claim is the misappropriation of confidential business information. Plaintiffs state in their amended complaint that their breach of fiduciary duty claim is expressly based upon the misappropriation of trade secrets."); *see also ScaleFactor*, 394 F. Supp. 3d. at 685 ("Indeed, ScaleFactor alleges that its conversion damages include the "loss of confidential, proprietary, and trade secret information.").

52. *DeWolff*, 2022 WL 4589161, at *4.

53. *Id.*

claim would perhaps find life in a different forum, one that applies the "minority approach," specifically within the Southern District of Texas.

IV. THE MINORITY APPROACH

In *DHI v. Kent*, the Southern District of Texas took a completely different approach to the preemption by TUTSA question. In that case, the defendant, Kent, sold his business to DHI, then proceeded to download information that belonged to DHI.[54] The defendant created a new business and used the information to generate a commercial advantage to the plaintiff's detriment.[55] While the civil case was pending, Kent was criminally convicted for his action and was sentenced to one year in prison.[56]

DHI's civil complaint contained both a misappropriation of trade secrets and a breach of fiduciary duty claim.[57] Consequently, Kent moved for summary judgment on the breach of fiduciary duty claim based on the preemption provision in TUTSA.[58] Surprisingly, the Southern District took "the minority approach" or as one scholar calls it, the "No Uniform Act Trade Secret, No Preemption View."[59] As the name suggests, this view precludes preemption of a civil claim if the civil claim fails to allege a trade secret violation.[60]

The *DHI* court defended its different approach by examining the one taken in *Embarcadero,* and it was not satisfied by that court's reasoning.[61] The Southern District found that "the plain language of the TUTSA's preemption provision states that it does not affect 'other civil remedies that are not based upon misappropriation of a trade secret.'"[62] The *DHI* court held that the *Embarcadero* holding conflicted with "TUTSA's plain language," and could not come to terms with how the language of the preemption provision would preempt civil remedies based on the misappropriation of information that is not a trade secret.[63] Neither party established that any of the allegedly stolen information qualified as a trade secret, and thus, summary judgment was denied and both claims were allowed to persist to trial.[64]

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54. DHI Grp., Inc. v. Kent, 397 F. Supp. 3d 904, 912–14 (S.D. Tex. 2019).

55. *Id.*

56. DHI Grp., Inc. v. Kent, No. 21-20274, 2022 WL 3755782, at *1 (5th Cir. Aug. 30, 2022).

57. *DHI Grp.*, 397 F. Supp. 3d at 922.

58. *Id.*

59. *Id.* at 923; *see also* Richard F. Dole, Jr., *Preemption of Other State Law by the Uniform Trade Secrets Act*, 17 SMU SCI. & TECH. L. REV. 95 (2014).

60. *See DHI Grp.*, 397 F. Supp. 3d at 922; *see also* Dole, *supra* note 59.

61. *DHI Grp.*, 397 F. Supp. 3d at 923.

62. *Id.*

63. *Id.*

64. *Id.*

The Southern District has used the "minority approach" towards preemption in a number of cases since *DHI.*[65] Unlike the "majority approach," a complaint's pleadings can play a role in surviving preemption in the early stages.[66] If the claim states the allegedly abused information qualifies as either a trade secret or simply confidential information, the claim will escape preemption.[67]

However, the results of *DHI* may hint at what might happen to these claims that escape preemption. After the trial, the jury found Kent liable for violating TUTSA with damages of $3 million *and* misappropriation of confidential information with damages of $2.5 million.[68] The jury also found Kent liable for breach of fiduciary duty, but did not award damages on that claim.[69] In any other district in Texas, a court would preempt both the misappropriation of confidential information and breach of fiduciary duty claims.

V. CONCLUSION

When litigators contemplate filing claims arising out of the misappropriation of trade secrets, they must take into consideration what approach to TUTSA the court of jurisdiction applies. A majority of the courts will severely limit the types of claims presented that contain misappropriation of information, due to preemption, regardless of the wording in the pleading. However, a Southern District court is more likely to let the claims through to see the next phase of litigation and, at least temporarily, escape preemption by TUTSA. While TUTSA attempts to provide uniformity in trade secret litigation, the courts that interpret its provisions remain divided. Until clarification comes from higher courts, litigators will have to do their homework before pressing forward.

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65. *See generally* AMID, Inc. v. Medic Alert Found. U.S., Inc., 241 F. Supp. 3d 788 (S. D. Tex. 2017); 360 Mortg. Grp., LLC v. Homebridge Fin. Servs., Inc., No. A-14-CA-00847-SS, 2016 WL 900577 (W.D. Tex. Mar. 2, 2016); F. Energy Techs., Inc. v. Jason Oil & Gas Equip., LLC, No. CV H-20-3768, 2022 WL 1103078 (S.D. Tex. Apr. 13, 2022).

66. *F. Energy Techs*, 2022 WL 1103078, at *7 (S.D. Tex. Apr. 13, 2022) (finding complaints seeking relief on a theory that the defendant misused trade secrets, and in the alternative, under the theory that the defendant misused information that was not a trade secret, but instead confidential information, was likely to escape TUTSA preemption).

67. *Id.*

68. DHI Grp., Inc. v. Kent, No. 21-20274, 2022 WL 3755782, at *1 (5th Cir. Aug. 30, 2022).

69. *Id.*