

Lawyer Insights

Texas Noncompete Law's Atty Fee Preemption Status In Limbo

By Clarissa Medrano and Alan Marcuis
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Although the [Federal Trade Commission](#) may soon invalidate Texas' version of the federal antitrust statute,¹ the Texas Covenants Not to Compete Act seeks to impose what the [Texas Supreme Court](#) called "reasonable restrictions on the freedom to contract" in its 2010 *Marsh USA Inc. v. Cook* opinion, and governs economic competition in trade and commerce.²

Arguably, the most common litigation under the act involves an action seeking injunctive relief against an ex-employee by their former employer as well as a claim for breach of the employment contract under the Texas Civil Practice and Remedies Code, Section 38.001.

As will be discussed in more detail below, several Texas appellate courts have held that the act preempts an award of attorney fees by a suing employer. However, the Texas Supreme Court has not expressed the same certainty.

Although appellate courts' holdings in favor of preemption are generally in line with the language of the statute, experience reveals courts' hesitancy to rule decisively on the preemption issue.

Notwithstanding, because attorney fees are an appealing remedy that may or may not be available under the statute and because preemption should be pled as an affirmative defense out of an abundance of caution,³ preservation of these issues are key on both sides of any noncompete litigation.

Section 38.001 of the Texas Civil Practice and Remedies Code allows for the recovery of attorney fees by a prevailing party when the breach of contract claim involves any of the eight enumerated grounds in the statute, including the eighth ground itself — an oral or written contract.⁴

Of note, another ground for recovering fees arises when the claim involves rendered services.⁵ In contrast, the act seemingly precludes an award of attorney fees to the suing employer.⁶

The act also purports to preempt other "remedies in an action to enforce a covenant not to compete under common law or otherwise."⁷ But does the act preempt the recovery of attorney fees under Section 38.0001, or any other Texas statute for that matter?

When presented with this exact preemption issue in 2002, the Texas Supreme Court did not clearly indicate that the act preempts a claim for attorney fees under Section 38.001 or other any other Texas statute. In that case, *Texas Disposal Systems Inc. v. Albert Perez*,⁸ an employer brought suit against its former employees, alleging that they violated the covenants not to compete in their employment contracts.

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The employer sought attorney fees under the Covenant Not to Compete Act and Texas Civil Practice and Remedies Code, Section 38.001(8).⁹ The trial court enjoined the employees, reformed the agreement and awarded attorney fees to the employer after finding that each defendant had breached their employment agreements.¹⁰ No actual damages were awarded.

On appeal, the intermediary court held that the trial court erred in awarding attorney fees under the act because although the covenants were reformed in favor of the employer, no damages were awarded and thus the employer was not a prevailing party.¹¹

On review, the Texas Supreme Court remanded, holding only that the court of appeals had not considered the employer's alternate basis for attorney fees under Section 38.001 for services rendered, even though the court cited to Section 38.001(8) regarding an oral or written contract.¹²

Based on the reasons provided for remand, it appears that the Texas Supreme Court expressed no concern with a claim for attorney fees by a former employer under both the act and the Texas Civil Practice and Remedies Code.

Moreover, although the act only discusses awarding the employee fees,¹³ the Texas Supreme Court directed the appellate court to consider the employer's alternative claim for attorney fees under Texas statutory law — i.e., Section 38.001.

In stark contrast, the court of appeals held on remand that "the Act preempts an award of attorney's fees under any other statute," and therefore the employer was "not entitled to recovery of its fees under section 38.001."¹⁴

Since this holding, many other courts have similarly held that the enforcement of a noncompete contract under Section 15.52 preempts a party's ability to seek attorney fees under Section 38.001(8) of the Texas Civil Practice and Remedies Code.¹⁵ This is so even after the Texas Supreme Court, when presented with the issue in *Perez*, did not address or indicate preemption.

Despite the Texas Supreme Court's relative silence on the issue, Texas appellate courts have used strong language indicating preemption and cited to the act itself as authority.

For instance, in a 2020 opinion from the U.S. District Court for the Southern District of Texas that was affirmed by the [U.S. Court of Appeals for the Fifth Circuit](#) in *Ureteknologia de Mexico SA de C.V. v. Uretek USA Inc.*, the court noted that "[s]everal courts have found that enforcement of a non-compete contract under Section 15.52 preempts a party's ability to seek attorney fees under Section 38.001(8) of the Texas Civil Practice and Remedies Code."¹⁶

The court specifically cited to Texas appellate court decisions *Glattly v. Air Starter Components Inc.* in 2010 and *Rieves v. Buc-ee's Ltd.* in 2017 regarding Section 15.52 of the act, which the courts held did not permit employers to recover attorney fees under Section 38.001 of the Texas Civil Practice and Remedies Code.¹⁷

Rieves, however, also debated preemption of another Texas statute — namely the Declaratory Judgments Act.¹⁸ In *Rieves*, the appellate court found that Section 15.52 of the act preempted a fee award under both Section 38.001 of the Texas Civil Practice and Remedies Code and the Declaratory

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Judgments Act.¹⁹ The court in Rieves ultimately reversed a fee award to the employer.

In 2015, the Texas Court of Appeals in *Ginn v. NCI Building Systems Inc.* held that the Covenants Not to Compete Act preempts a claim for attorney fees under Section 27.01 of the Texas Business and Commerce Code for false representations in transactions involving stock in corporations.²⁰

In that case, the court held that "the Act does not allow employers to recover attorney's fees in suits to enforce covenants not to compete."²¹ This seems to correspond with the language in the statute regarding the recovery of fees by the employer if "otherwise" equates to statutory law. As noted, the act specifically references Texas common law.²²

Although appellate courts — and specifically Houston appellate courts — sound certain that the act preempts an award under any other Texas statute when the act is invoked, the Texas Supreme Court has not expressed the same opinion and has not clearly addressed the issue.

Accordingly, ambiguity surrounds the issue of preemption by the act of attorney fee claims under contract or statute. Ambiguity similarly surrounds whether an employer can recover attorney fees at all in conjunction with the act.

Attorneys and their clients are thus faced with inconsistent holdings in which courts may find preemption, decline to address preemption or deny that the act is dispositive of a claim for attorney fees by an employer. Even if the FTC's proposed rule goes into effect, this issue will remain unresolved until decisive authority from the Texas Supreme Court issues.

The best practice is to always affirmatively plead preemption with respect to a claim for attorney fees by the suing employer under the act, in the event that the trial court chooses to adopt Texas appellate precedent concerning an award of fees under common law or otherwise. To decisively address the issue, special exceptions or a partial motion for summary judgment on the issue can be utilized to get clarity from the court.

This is especially true if the pleadings are unclear whether the act has been invoked or the dispute is contractual in nature. In turn, suing employers that choose to plead for attorney fees may want to brief the applicability of the preemption language in the statute or simply note that the high court has not ruled on the preemption issue, in addition to stating the basis for the fee claim.

Overall, being aware of the fact that Texas law is unsettled in a noncompete action makes for better advocacy, especially when attorney fees are at issue. Until then, noncompete litigators anxiously await any further guidance from the Texas Supreme Court or more drastic measures from the FTC.

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Notes

1. Proposed FTC Ban on Non-Competes: Considerations for M&A Transactions, Jan. 18, 2023, <https://www.huntonak.com/en/insights/proposed-ftc-ban-on-non-competes-considerations-for-manda-transactions.html>.
2. Tex. Bus. & Com. Code Ann. § 15.04. [Marsh USA Inc. v. Cook](#), 354 S.W.3d 764, 768 (Tex. 2011) (citing [Fairfield Ins. Co. v. Stephens Martin Paving, LP](#), 246 S.W.3d 653, 663–64 (Tex.2008)).
3. "In pleading to a preceding pleading, a party shall set forth affirmatively ... any other matter constituting an avoidance or affirmative defense." Tex. R. Civ. P.94.
4. See Tex. Civ. Prac. & Rem. Code Ann. § 38.001(1).
5. See Tex. Civ. Prac. & Rem. Code Ann. § 38.001(1).
6. Tex. Bus. & Com. Code Ann. § 15.53 ("the court may award the promisor the costs, including reasonable attorney's fees, actually and reasonably incurred by the promisor in defending the action to enforce the covenant").
7. Tex. Bus. & Com. Code Ann. § 15.52 ("remedies in an action to enforce a covenant not to compete provided by Section 15.51 of this code are exclusive and preempt any other criteria for enforceability of a covenant not to compete or procedures and remedies in an action to enforce a covenant not to compete under common law or otherwise").
8. [Tex. Disposal Sys., Inc. v. Perez](#), 80 S.W.3d 593 (Tex. 2002).
9. Perez, 80 S.W.3d 594.
10. Id.
11. [Perez v. Tex. Disposal Sys., Inc.](#), 53 S.W.3d 480, 481 (Tex. App.—San Antonio 2001), review granted, judgment rev'd, 80 S.W.3d 593 (Tex. 2002).
12. Perez, 80 S.W.3d 594.
13. Tex. Bus. & Com. Code Ann. § 15.53.
14. Perez v. Tex. Disposal Sys., Inc., 103 S.W.3d 591, 592 (Tex. App.—San Antonio 2003, pet. denied).
15. [Ureteklogia de Mexico S.A. de C.V. v. Uretek \(USA\), Inc.](#), No. CV H-16-2762, 2020 WL 3127925, at *2 (S.D. Tex. June 12, 2020), aff'd, No. 20-20073, 2022 WL 29638 (5th Cir. Jan. 3, 2022) (citing [Glattly v. Air Starter Components, Inc.](#), 332 S.W.3d 620, 644 (Tex. App.—Houston [1st Dist.] 2010, pet. denied); [Rieves v. Buc-ee's Ltd.](#), 532 S.W.3d 845, 854 (Tex. App.—Houston [14th Dist.] 2017, no pet.)); See also [Franlink, Inc. v. GJMS Unlimited, Inc.](#), 401 S.W.3d 705, 712 (Tex. App.—Houston [14th Dist.] 2013, pet. denied).

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16. Ureteklogia de Mexico S.A. de C.V., 2020 WL 3127925, at *2 (citing Glattly, 332 S.W.3d at 644; Rieves, 532 S.W.3d at 854).

17. Ureteklogia de Mexico S.A. de C.V., 2020 WL 3127925, at *2-3.

18. Ureteklogia de Mexico S.A. de C.V., 2020 WL 3127925, at *3 (citing Rieves, 532 S.W.3d at 854).

19. Id. (citingid.) . See also [Sadler Clinic Ass'n, P.A. v. Hart](#), 403 S.W.3d 891, 900 (Tex. App.—Beaumont 2013, pet. denied) (holding that "the exclusivity and preemption provision of the Covenants Not To Compete Act preclude[d] an award of attorney fees under the Declaratory Judgments Act") (citing See Tex. Bus. & Com. Code Ann. § 15.52; [MBM Fin. Corp. v. Woodlands Operating Co., L.P.](#), 292 S.W.3d 660, 669 (Tex. 2009) ("[T]he rule is that a party cannot use the [Declaratory Judgments] Act as a vehicle to obtain otherwise impermissible attorney's fees.")).

20. [Ginn v. NCI Bldg. Sys., Inc.](#), 472 S.W.3d 802, 827 (Tex. App.—Houston [1st Dist.] 2015, no pet.).

21. Id. (citing Tex. Bus. & Com. Code Ann. §§ 15.51(c), 15.52).

22. Tex. Bus. & Com. Code Ann. § 15.52.

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