Proving (or Attacking) Lost Profits Damages in Trade Secrets and Other Cases

Texas Bar CLE – Live Webcast

Kelly Leonard
Strasburger & Price

Robert Ford
Fogler Brar Ford O'Neil Gray

Moderator: Zach Wolfe
Fleckman & McGlynn

DAMAGES AVAILABLE IN TRADE SECRETS CASES GENERALLY

Statutory Misappropriation of Trade Secrets under the Texas Uniform Trade Secrets Act (TUTSA) [*codified at* Tex. Civ. Prac. & Rem. Code 134A.001 *et seq.*].

- Governs trade-secrets claims accruing on or after Sep. 1, 2013. *Sw. Energy Production Co.*, 2016 WL 3212999 at *6, n.7.
- "Displaces conflicting tort, restitutionary, and other laws of this state providing civil remedies for misappropriation of a trade secret." TEX. CIV. PRAC. & REM. CODE § 134A.007(a).

DAMAGES AVAILABLE IN TRADE SECRETS CASES GENERALLY

- Actual Damages can be in addition to or in lieu of injunctive relief and include:

  (i) (a) Actual loss caused by misappropriation; plus (b) the unjust enrichment caused by misappropriation that is not taken into account in computing actual loss;

  --OR--

  (ii) "in lieu of damages measured by any other methods," damages caused by misappropriation may be measured by "a reasonable royalty for a misappropriator's unauthorized disclosure or use of a trade secret." *Id.* § 134A.004(a).

DAMAGES AVAILABLE IN TRADE SECRETS CASES GENERALLY

- Court may award prevailing party its reasonable attorney's fees if, *inter alia*, willful and malicious misappropriation. *Id.* § 134A.005(3).
- Exemplary damages, in an amount not to exceed 2x the damages above, if willful and malicious misappropriation proven by clear and convincing evidence. *Id.* § 134A.004(b).
- *Note: There is a question whether all of the pre-TUTSA lost-profits precedent applies to post-TUTSA trade secrets cases – more on this later.*

Lost profits damages, generally.

- Lost profits in trade secret cases can arise from past loft profits or anticipated future profits. These profits are provided for by statute.

- Lost profits must be proven with reasonable certainty, and whether lost-profits evidence is reasonably certain is a fact-intensive inquiry. *Phillips v. Carlton Energy Grp., LLC*, 475 S.W.3d 265, 279 (May 8, 2015); *Holt Atherton Indus., Inc. v. Heine*, 835 S.W.2d 80, 84 (Tex. 1992).

Lost profits damages, generally.

- The amount of loss need not be subject to exact calculation but need only be shown by competent evidence based on objective facts, figures, or data from which the amount may be ascertained with reasonable certainty.
- At a minimum, "opinions or estimates of lost profits must be based on objective facts, figures, or data from which the amount of lost profits can be ascertained." *Heine*, 835 S.W.2d at 84.

EXPERT TESTIMONY ON LOST PROFITS DAMAGES

What isn't required:

- "Recovery of lost profits does not require that the loss be susceptible of exact calculation. " *ERI Consulting Eng'rs, Inc. v. Swinnea*, 318 S.W.3d 867, 876 (Tex. 2010).
- Proponent of lost-profit expert testimony need not "produce in court the documents supporting the lost-profits opinions or estimates." *AZZ Inc. v. Morgan*, 462 S.W.3d 284, 289 (Tex. App.—Fort Worth 2015, no pet.). *But see Swinnea*, 318 S.W.3d at 876 ("[a]lthough supporting documentation may affect the weight of the evidence").
- Need not prove up lost-profits through retained expert; owner of the trade secret can testify. *Id.*

EXPERT TESTIMONY ON LOST PROFITS DAMAGES

What *is* required:

- Must show the amount of the loss by competent evidence with reasonable certainty. *Swinnea*, 318 S.W.3d at 876.
- What constitutes reasonably certain evidence of lost profits=fact-intensive determination. *Id.*; *accord Holt Atherton Indus., Inc. v. Heine*, 835 S.W.2d 80, 84 (Tex. 1992).
- "At a minimum, opinions or estimates of lost profits must be based on objective facts, figures, or data from which the amount of lost profits may be ascertained." *Id.*; *accord Szczepanik v. First S. Trust Co.*, 883 S.W.2d 648, 649 (Tex. 1994).
- Facts and assumptions upon which expert relies must be valid, and that validity must be "rigorously examined" by the Court. *Sw. Energy Production Co.*, 2016 WL 3212999 at *11 (quoting *Hous. Unlimited, Inc. Metal Processing v. Mel Acres Ranch*, 443 S.W.3d 820, 832–33 (Tex. 2014)).

Southwestern Energy v. Berry-Helfand: The treasure map takes off

- Tory Berry-Helfand is an engineer who sued SEPCO for misappropriation and theft of trade secrets arising from its use of a "treasure map" and drilling techniques.
- Helfand developed her methodology and geological profile from publicly available information and presented the compiled work to SEPCO in 2005 pursuant to a confidentiality and non-compete agreement. SEPCO and Helfand engaged in further discussions following the presentation, but SEPCO did not make an offer.
- Helfand and her co-worker then approached Petrohawk. It agreed to use the information on the following terms: (i) a $1.8 million payment, (ii) a sliding-scale overriding royalty interest (which averaged 3% on these leases), and (iii) a 6.25% after-payout working interest.

SEPCO hits pay dirt and Berry-Helfand sues

- While these negotiations ensued, SEPCO embarked on an unprecedented and aggressive drilling campaign in the relevant area, ultimately acquiring 888 leases and drilling more than 140 wells in areas clustered around the sweet spots identified by Helfand on her “treasure map.”
- The wells had a 100% success rate and generated $381.5 million in revenue for SEPCO. Berry-Helfand discovered SEPCO’s success and later sued it for misappropriation.

JURY AND TRIAL JUDGE EACH DROP THE HAMMER ON SEPCO:

- Jury values the trade secrets at $11.445 million, or exactly 3% of the $381.5 million in profits that SEPCO made on its play *(Evidence showed that Helfand averaged a 3% royalty on a deal that she had previously cut with Petrohawk involving the same trade secrets and the same play.). Id.* at *6.
- Jury finds SEPCO's "benefits, profits, or advantages" from the trade secrets to be $11.445 million, or exactly 3% of the $381.5 million in profits that SEPCO made on its play. *Id.*
- Post-verdict, Trial Judge tacks on an additional $23.89 million in equitable disgorgement of profits, and enters a total judgment for more than $40 million ($11.445M (value of trade secrets) + $23.89M (disgorgement) + $4.6M (Atty's fees). *Id.*

Texas Supreme Court's Opinion

- Court reversed and remanded, explaining:

"In trade-secret cases, a measure of uncertainty is tolerated, and to an extent, unavoidable. However, **when there is objective evidence from which more certainty can be gleaned, it is incumbent on the plaintiff to produce that evidence**. An estimate or an average based on a small sample may be sufficient in some cases, but not in this case. Because the actual overriding royalty interest on the disputed wells could have been determined under the methodology of the exemplary transaction, applying 3% across the board paints an incomplete and misleading picture about the royalty terms a willing buyer and seller would negotiate."

Texas Supreme Court's Opinion Cont'd

"To illustrate, if Helfand [the engineer] owned a trade secret vital to the making of widgets and XYZ widget company misappropriated the information to make 3,000 widgets, a prior licensing agreement with a third party involving a licensing fee of $2 per widget would be strongly probative of a $2 reasonable royalty. But if Helfand previously negotiated a licensing fee of $1 on the sale of small widgets, $2 for medium widgets, and $3 for large widgets, an average of $2 under that deal would be inadequate to establish the value of a reasonable royalty for 3,000 widgets of varying sizes. What if XYZ only made small widgets? Depending on consideration of the other factors bearing on a reasonably royalty, the $2 average could vastly overstate the royalty a willing buyer and seller would negotiate."

COMMON LAW VS. STATUTORY TRADE SECRETS DAMAGES

Common-Law Misappropriation of Trade Secrets

- Technically no such thing, anymore, unless your claim accrued before Sep. 1, 2013.

  Note: *Sw. Energy Prod. Co. v. Berry-Helfand* was technically a common-law case.

- At any rate, same damages, for all intents and purposes, as those available under TUTSA (with lone exception of potential recovery of attorney's fees; could use Texas Theft Liability Act, but beware of fee-shifting).

- There is a hyper-technical argument to be made that actual damages, which are available under either TUTSA or common law, are measured differently under TUTSA, *see Sw. Energy Prod.*, 2016 WL 3212999 at *6, n. 7 (noting, as among the available remedies under TUTSA, "damages ***measured*** by actual loss [caused by misappropriation] plus unjust enrichment not included in computing actual loss"), but Courts continue to rely on common-law precedent to measure damages in TUTSA cases.

MEASURE OF ACTUAL DAMAGES FOR TRADE-SECRET MISAPPROPRIATION UNDER COMMON LAW (AND TUTSA, TOO?)

- "Flexible and imaginative approach" is used to calculate actual damages in trade-secret misappropriation cases. *Sw. Energy Prod. Co.*, 2016 WL 3212999 at *6.

- Trade-secret plaintiff may recover actual damages based on either:
  - the value of what plaintiff has lost as a result of the misappropriation;

  --OR--

  - the value of what defendant has gained as a result of the misappropriation. *Id.* at *7.

  [**Note**: Under TUTSA, plaintiff may technically recover *both*. *See* CPRC § 134A.004(a) ("actual loss caused by misappropriation *and* the unjust enrichment caused by misappropriation that is not taken into account in computing actual loss.")]

- So, actual damages can take several forms:
  - Value of plaintiff's lost profits (value of what Π has lost);
  - Defendant's actual profits from use of trade secret(s) a/k/a "unjust enrichment" (value of what Δ has gained);
  - Value a reasonably prudent investor would have paid for the trade secret(s) (value of what Δ has gained); or
  - The development costs the defendant avoided by misappropriation (value of what Δ has gained). *Id.*
- Absent proof of any of the types of damages above, plaintiff may recover a reasonable royalty, which is calculated by "what the parties would have agreed to as a fair price for licensing the defendant to put the trade secret to the use the defendant intended at the time the misappropriation took place." *Id.* It is based on a "fictional negotiation of what a willing licensor and licensee would have settled on as the value of the trade secret at the beginning of the infringement." *Id.*

THANKS FOR WATCHING!

QUESTIONS / COMMENTS?

Kelly Leonard: kelly.leonard@strasburger.com

Robert Ford: rford@fbfog.com

Zach Wolfe: www.fiveminutelaw.com