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§ 199:75. Executive summary for clients regarding US trade secret law and practice

Client Executive Summary on U.S. Trade Secret Law and Practice

§ 1. Introduction

For many companies, trade secret laws, which are typically a combination of statutory language and interpretations by the courts, have become a preferred form of intellectual property protection, even in cases where the subject matter might otherwise be an “invention” eligible for patent protection. Although there is no universally accepted definition of a trade secret, the list of possible items can extend to almost any device or information, including formulas, databases, methods of operation, or materials that are used in a business and provide the owner with a competitive advantage over others who do not know or use the trade secret, provided that the trade secret is maintained in secret by the owner. The length of trade secret protection is not finite, as is the case with patents and copyrights, and may extend for so long as each of the essential elements for characterization as a trade secret, such as value and secrecy, continue to exist. In particular, one of the key elements of perfecting legal rights in trade secrets is the person’s ability to establish and maintain an effective trade secret protection program.

In addition, it is important to understand how trade secret rights are created and protected in the context of the employment relationship. Procedures should be implemented to inform employees what information is to be treated as a trade secret and to secure written agreements from key workers to maintain such information in confidence, not to use it for their own benefit, and not to disclose it to others without proper authority. This usually involves establishing a program of meetings, notices and publications to remind all of employees of items that the company considers a trade secret. It may also involve the use of pre-employment investigations, written confidentiality and noncompetition agreements, employment exit interviews and post-employment communications. Although most, if not all, employees should be included in procedures relating to the protection of trade secrets, the overall security program should restrict the employees who access such information to those with a “need-to-know.”

As a general rule, a trade secret is considered property in the hands of its owner and, as such, creates rights that may be exercised by the owner. For example, a trade secret owner has the right to sell the secrets or to transfer less than all of his ownership of a trade secret in a licensing arrangement where the licensee is permitted to use the trade secret while the licensor retains title. This permits the licensor to intervene in litigation when the licensee is a party and the trade secret might be revealed. Trade secrets can also serve as consideration for stock, can serve as *res* for a trust, are considered property in bankruptcy proceedings, and can be conveyed by testate and interstate transfers.

Unlike the patent law, trade secret law does not create a legal monopoly in favor of the trade secret owner. Instead, the trade secret owner only has a cause of action against any party who wrongfully appropriates the trade secret, as well as a cause of action against persons who utilize any illegal or unethical methods to acquire the secret information. A trade secret owner cannot prevent others from independently developing the trade secret, even by reverse engineering, and thereafter practicing the trade secret as their own. In fact, in most cases, proof of lawful independent development and use of a device or information by another party will terminate the rights of the first owner to proceed against any other user of the secret.

In contrast to patents and copyrights, the legal protections for trade secrets, often referred to as “know how,” are far from uniform around the world. While trade secret protection is well established in the United States and many other common law countries, trade secrets are not recognized in many countries, and no international convention or treaty exists with respect to the subject matter. Even in those cases where trade secrets are recognized, the scope of the subject matter that qualifies for protection can vary significantly from country to country and there are also substantial differences around the world with respect to the duration of trade secret protection, the ability of trade secret owners to enforce their rights against persons with whom they are not in privity of contract, protection of trade secrets in the employment relationship and the vigor of local law officials in conducting enforcement actions. In large part, variations in the treatment of trade secrets and other confidential information in foreign countries are a function of fundamental differences in cultural attitudes regarding ownership and use of valuable business information, as well as economic and political objectives of the local governments with respect to diffusion of technical information and ensuring free mobility of labor.

The lack of uniformity in the trade secrets area means that disclosure of proprietary information into any new foreign market must be preceded by a careful analysis of a number of factors. In particular, the trade secret owner must examine the statutory and, if relevant, case law relating to trade secrets in the foreign country; the restrictions which might be imposed on clauses which may be included in contractual agreements with respect to the use and protection of trade secrets; cultural factors which might lead to the unwanted dissemination of trade secrets, whether or not the disclosures are prescribed by local law; any other local government regulations impacting the technology transfer; and the enforcement history in the country with respect to any laws which do exist regarding trade secret protection. Specific issues to consider are illustrated in the following sections which focus on the law of trade secrets in the United States; however, companies should assume that answers to key questions such as “what is considered to be a trade secret” and “what steps need to be taken to protect and enforce trade secrets” may be quite different in other countries. Since “secrecy” is a universal requirement for legal protection of trade secrets the final sections have been included to provide valuable guidance on establishing and maintaining a trade secret protection program.

§ 2. Definitions of trade secrets

There is no uniform definition of a “trade secret” globally accepted. Even within the United States, where trade secret law is largely a function of *state* regulation rather than federal law (federal law being the basis of the patent laws), variations exist around the country. Trade secret law originally arose from the common law, which was based upon the Restatement of Torts (1939) (the “Restatement”), which incorporated the results of a long line of cases and decisions to set out general principles of tort law. In Comment b to Restatement § 757, the following definition of a trade secret was articulated:

A trade secret may consist of any formula, pattern, device or compilation of information which is used in one’s business, and which gives him an opportunity to obtain an advantage over competitors who do not know or use it. It may be a formula for a chemical compound, a process of manufacturing, treating or preserving materials, a pattern for a machine other device, or a list of customers. It differs from other secrets in a business (see § 759) in that it is not simply information as to single or ephemeral events in the conduct of the business. For example, the amount or terms of a sealed contract bid; employee salaries; security investments made or contemplated; the date fixed for the announcement of a new policy or for bringing out a new model may all be trade secrets. A trade secret is a process or device for continuous use in the operation of the business. Generally it relates to the production of goods, as, for example, a machine or formula for the production of an article. It may, however, relate to the sale of goods or to other operations in the business, such as a code for determining discounts, rebates or other concessions in a price list or catalogue, or a list of specialized customers, or a method of bookkeeping or other office management.

The general definition of the types of items that might be eligible for trade secret protection was supplemented by a list of factors generally were important in determining the existence of a trade secret, including the:

- Extent to which the information is known outside of [the] business;
- Extent to which it is known by employees and others involved in [the] business;
- Extent of measures taken ... to guard the secrecy of the information;
- Value of the information to *[name of owner]* and to *[his/her]* competitors;
- Amount of effort or money expended by *[name of owner]* in developing the information; and
- Ease or difficulty with which the information can be properly acquired or duplicated by others.

Most states now follow the Uniform Trade Secrets Act (“Uniform Act”), which was drafted by the National Conference of Commissions on Uniform State Laws and adopted in 1979. The definition of trade secrets in the Uniform Act includes any

information, including a formula, pattern, compilation, program, device, method, technique, or process, that (i) derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use, and (ii) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy

In the states that have followed the Uniform Act, the legislature has passed statutes defining the scope of trade secret protection based on the Uniform Act; however, they have sometimes adopted significant deviations from the text of the Uniform Act and the Restatement remains an important influence on the definition of a trade secret and the rights of a trade secret owner. A small number of states either continue to apply the common law to trade secret issues, often looking to the Restatement definition for guidance, or have adopted their own legislation regarding trade secret protection that differs materially from both the Restatement and the Uniform Act.

Many states adopting the Uniform Act have modified the Act’s definition of “trade secret.” For example, states such as Illinois, Maine, Virginia, and West Virginia have adopted an expansive approach by prefacing the listing in the initial paragraph with the phrase “including, but not limited to.” Washington uses the definition in the Uniform Act “unless the context clearly requires otherwise.” On the other hand, the statute in Alabama takes a more restrictive and mechanical approach, providing that the information must fall into one of the designated categories to qualify as a protectable trade secret. Many states have supplemented the Uniform Act’s language in their own statutes by including other items that would qualify for trade secret protection, including drawings, computer data, and customer lists. For example, the following states include various types of information: Alabama (computer software and drawings); Colorado (scientific or technical information, confidential business or financial information, listing of names, addresses, or telephone numbers); Connecticut (drawings, cost data, customer lists); Georgia (nontechnical data, financial plans, product plans); Illinois (technical or non-technical data, drawings, financial data, list of customers, or suppliers); Montana (customer software); Nebraska (drawings); and Oregon (cost data, customer list).

In addition, definitions of trade secrets have been prescribed or judicially developed in relation to various federal statutes such as the federal Trade Secrets Act, the Freedom of Information Act, the Toxic Substances Control Act, the Economic Espionage Act of 1996, the Computer Fraud and Abuse Act, the National Stolen Property Act, federal mail fraud and wire fraud statutes, and the Racketeer Influenced and Corrupt Organizations Act. Reference should also be made to state statutes that impose civil and criminal liability for theft of property, including trade secrets.

§ 3. Scope of subject matter eligible for trade secret protection

In most cases, the technical information will take the form of a specific product, process, or working model, thereby eliminating any question as to whether the trade secret is sufficiently delineated; however, a physical embodiment will not be required if the information is otherwise concrete. In other cases, the question will be less clear, and the legitimate interests of the defendant may become a factor in determining the degree of definiteness. For example, a court may require greater specificity when the plaintiff's claim involves information that is closely integrated with the general skill and knowledge retained by former employees. The relationship between the plaintiff and defendant will also be relevant, and courts examining situations where the defendant was previously engaged by the trade owner in an agency relationship will tend to consider the extent to which the parties' relationship was confidential or fiduciary; the method by which the former agent acquired the alleged secret; and any unfair advantage that would or has accrued to the former agent by using the alleged secret.

Trade secret protection may be available for machine drawings, flow-charts, and blueprints; marketing plans, strategic plans and financial statements; business methods; pricing methods; customer lists; computer programs and data bases; manufacturing, technological, and scientific processes; personnel and employment records; employee, training or other company manuals; ingredients in foods, drugs and cosmetics; marketing techniques; capabilities of suppliers; sales data; product, manufacturing and testing specifications; geological and geophysical maps; engineering reports; publication schedules and contents of publications; and a company's Twitter account password and subscribers.

A trade secret may also exist in a "combination of characteristics or components," each of which is itself in the public domain, but together create a "unique combination" that affords a competitive advantage. Trade secret status is available involving ingredients which all have been disclosed to the public, provided that the quantities of each of the ingredients have not been disclosed and cannot be easily ascertained and it is this secret combination of the ingredients which is of economic value to the owner. In such situations, it is the method of combining the ingredients which produces a product that is superior to that of competitors. This holds true not only when the ingredients have never been combined before but, also, when the same ingredients have been recomposed in some manner different than any existing combinations.

The Uniform Act protects information regarding technical aspects of a production process which do *not* work, since this knowledge may be valuable to someone seeking to independently develop the process without the delays caused by pursuing knowingly meritless ideas. A trade secret can include technical information that is patentable, although a decision may be made not to seek a patent to avoid disclosing the information in the patent application.

Unlike patent law, which limits the patentable subject matter to processes, machines, manufactures or compositions of matter, there is no requirement that information exist in some tangible format to be a trade secret. Even though the Restatement definition of "process or device" reflects the traditional requirement that a trade secret must be something more than a mere idea, theory or possibility, the Uniform Act makes no mention of the concept of concreteness. Therefore, courts are free to accept or reject any requirement that the protected subject matter exists at some minimum level of tangibility, although if the item is too abstract it may become difficult for the plaintiff to demonstrate economic value. A lack of definitiveness may also adversely impact attempts to prove secrecy and failure to sufficiently particularize the trade secret may make it impossible for the court to formulate appropriate relief for the plaintiff.

The universe of trade secret cases in the United States is extensive and a full survey is beyond the scope of this publication. Persons seeking to rely on trade secret protection should be particularly mindful of the need for careful analysis of case law when the subject matter includes processes, methods, machines and devices; business information, particularly business plans and financial information; customer lists, which often raise trade secret issues when an employee leaves the employment of an employer and begins to compete with the former employer; submitted ideas, which companies often address by requiring submitting parties to execute and deliver a "reverse confidentiality" agreement; software programs, which are now routinely held to be entitled to trade secret protection; and knowledge, experience, memories, and skills gained by an employee during the course of employment (while "general" knowledge is not entitled to trade secret protection the employee may have learned of protectable "know-how" which is unique to the specific business and, therefore, eligible for trade secret status).

§ 4. Secrecy requirement

Under both the Restatement and the Uniform Act, “secrecy” is the most important factor in determining whether information is to be considered a trade secret. As one court noted, under trade secret law, secrecy is “the threshold issue in every case.” While courts have often upheld the existence of a trade secret absent a showing of “continuous use” or “competitive advantage,” there are no exceptions to the rule that a trade secret must be “secret,” and one court has noted that the failure to take substantial measures to maintain the secrecy of the purported trade secret is “fatal” to finding the existence of the trade secret. Although the secrecy requirement is quite clear, both the Restatement and the Uniform Act, as well as the cases that have dealt with issue, make it clear that absolute secrecy is not required, and that the owner may disclose the information to others, such as employees, co-venturers, and suppliers, without losing the protection of trade secret law, provided that some substantial element of secrecy remains after disclosure.

Neither the Restatement nor the Uniform Act contains a definitive definition of “secrecy.” However, the issue is one which has occupied the courts for many years. In general, the amount and sufficiency of secrecy in a given case will be judged in light of a variety of factors. The most common of these factors include the extent to which the information is generally known to other persons outside of the business; the extent of the measures taken by the trade secret owner to maintain the secrecy of the information; and the ease or difficulty with which the information can be acquired or duplicated by others without using improper means. In addition to these three major considerations, courts, in applying equity, may well look to other facts and circumstances which might influence the decision in a particular case. For example, the offensiveness of the conduct of a party alleged to have engaged in misappropriation may be relevant to the court’s assessment of the measures taken by the owner to protect the trade secret. Also, as one might imagine, the analysis of the sufficiency of the owner’s efforts to maintain the requisite secrecy must take into account not only the form of such measures, but the substance of the owner’s actual enforcement of the secrecy measures. Finally, a court will likely be influenced by the nature of the information for which protection is sought, particularly the amount of effort or money expended by the trade secret owner in developing the information and the value of the information to him or her and to his or her competitors.

§ 5. Economic value and use requirements

Like secrecy, use of the trade secret in the owner’s business is a fundamental condition for protection. The Restatement explicitly incorporates a use requirement as part of its definition when it stated that a “trade secret may consist of any formula, pattern, device or compilation of information which is used in one’s business” and Comment b to Restatement § 757 explained that “a trade secret is a process or device for continuous use in the operation of the business.” The use requirement emerged in several early cases. However, the Uniform Act did not include a reference to “use in business,” apparently to make it clear that protection could be available to a plaintiff who has not yet had an opportunity or acquired the means to put a trade secret to use. The Uniform Act’s position is consistent with other cases that rejected any requirement of use by the trade secret owner. The Uniform Act also allows protection of negative information which by its very nature is not actively used in the business, and information that relates “to single or ephemeral events.”

The economic value requirement for trade secret protection means that the information must have sufficient value in the operation of the business to provide the owner or user with an actual or potential economic or competitive advantage over others who do not have the information. The “independent economic value” requirement included as part of the Uniform Act has been interpreted as merely codifying the long-standing common law requirement that the trade secret must afford the owner with a competitive advantage. It is not necessary that the trade secret create a *significant* economic advantage; however, it must have more than trivial value and such value should not be “too speculative.” The economic value requirement has, in light of the changes made in the Uniform Act, supplanted the use requirement in some states, since certain information (e.g., negative information) has the requisite value even though it is not directly used in the business.

While issues of proof are an evidentiary challenge, it is not necessary for the trade secret owner to derive actual financial benefits in order for the information to be eligible for protection. In fact, what is required is only that the trade secret offers “an opportunity to obtain an advantage.” This is particularly important where an innovator has expended time and effort to develop a trade secret that may generate revenues from future use, but the innovator lacks the current resources necessary for

commercialization. Similarly, a marketing plan covering future products and services may have economic value, as will technology and manufacturing expertise embodied in plans for the future introduction of products.

§ 6. Use and enforcement of trade secret rights

As a general rule, a trade secret is considered property in the hands of its owner and, as with any property, creates a group of associated rights which may be exercised by the owner. For example, a trade secret owner has the right to sell the secrets or to transfer less than all of his or her ownership of a trade secret in a licensing arrangement in which the licensee is permitted to use the trade secret while the licensor retains title thereto, thereby permitting the licensor to intervene in litigation when the licensee is a party and the trade secret might be revealed. Trade secrets can also serve as consideration for stock, can serve as a res for a trust, are considered property in bankruptcy proceedings, and can be conveyed by testate and interstate transfers.

In general, trade secrets are entitled to protection for as long they remain secret and the other requirements for protection remain satisfied. This contrasts strongly to the limited duration of exclusivity available to inventions that are protected under the patent laws. In light of the potential unlimited period of protection for trade secrets a valid confidentiality agreement prohibiting disclosure of trade secrets is not subject to the limitations on duration and scope that are imposed on noncompetition agreements.

Both the Restatement and the Uniform Act contain provisions imposing liability when a trade secret is acquired by improper means. The Uniform Act defined “improper means” to include “theft, bribery, misrepresentation, breach or inducement of a breach of a duty to maintain secrecy, or espionage through electronic or other means.” For its part, the Restatement, while stating that “a complete catalog of improper means is not possible,” did provide some guidance by noting that the following acts constituted proper methods of discovering or obtaining the trade secrets of another: (1) discovery of the trade secret by independent invention; (2) discovery of the trade secret by “reverse engineering”; (3) discovery of the trade secret under a license from the owner of the trade secret; (4) observation of the item in public use or on public display; and (5) obtaining the trade secret from published literature.

A trade secret owner asserting a claim for misappropriation must be prepared to prove each of the following elements: (1) the existence of a trade secret; (2) disclosure of the trade secret to the defendant in confidence, or the wrongful taking of the trade secret by the defendant without the plaintiff’s authorization; and (3) the use or disclosure of the knowledge or information so obtained in violation of the confidence, or in a wrongful manner, to the injury of the plaintiff. An exclusive licensee of a trade secret has the same standing as the owner of the trade secret to assert a claim for misappropriation.

Injunctive relief is available with respect to any actual or threatened misappropriation of a trade secret. In order to obtain such relief, proof must be provided by the plaintiff that a valuable trade secret owned by the plaintiff was communicated to another under circumstances making it inequitable for the recipient to use or disclose it and that use or disclosure either is occurring or is threatened. In addition to or in lieu of injunctive relief, a trade secret owner may recover damages for wrongful misappropriation of the trade secret information. Courts have computed and awarded damages to a trade secret owner based upon at least one of the following measures: (1) the trade secret owner’s probable losses attributable to the misappropriation; (2) the misappropriator’s benefits, profits or advantages; or (3) a reasonable royalty. In cases involving willful and malicious misappropriation, punitive or exemplary damages may be awardable in an amount not exceeding twice any award for actual loss and unjust enrichment.

Disclosure of trade secrets may also give rise to criminal liability in certain circumstances. The Federal Trade Secrets Act makes it a crime for any employee of the United States or any agency thereof, to the extent not authorized by law, to publish, divulge, or disclose information that constitutes a trade secret. Criminal sanctions may also be available under the Economic Espionage Act of 1996, [18 U.S.C.A. § 1831](#), which creates a crime of wrongfully copying or otherwise controlling trade secrets and is not limited to acts of governmental agencies or employees. In addition, most states have criminal statutes that under proper circumstances may apply to the theft of trade secrets; however, these laws typically are limited to trade secrets that are embodied in some physical form (e.g., a document or drawing). Another remedy to consider is asserting a private civil cause of action for trade secret misappropriation under the federal Defend Trade Secrets Act of 2016.