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Common Law V. UTSA: The Last States Standing

Law360, New York (April 02, 2012, 12:22 PM ET) -- On Jan. 9, 2012, New Jersey adopted its own version of the Uniform Trade Secrets Act, making New Jersey the 47th state to adopt the Uniform Act, and leaving only three states still holding on to their individualized state bodies of trade secret common law.

Although the common law jurisdictions are few in number, they are likely to be home to a comparatively large volume of trade secret litigation. With constant technological innovation driven by highly skilled and highly mobile employees, trade secret claims are becoming a frequent and costly occurrence.

Noting and planning for dissimilarities in the trade secret jurisprudence among different states is critical to ensuring compliance with trade secret law and successful litigation of trade secret claims.

The Uniform Trade Secret Act

The law protecting trade secrets against misappropriation began purely as state common law, with each state applying its own regime. In 1979, the National Conference of Commissions on Uniform State Law approved the Uniform Trade Secrets Act (UTSA), a model statute to be adopted by the states.

The UTSA aimed to unify trade secret law, and reduce uncertainty by avoiding states' diverse causes of action with distinct remedies and definitional criteria for what information was protected and under what circumstances.

In its goal of unity, the UTSA enjoyed a measure of success. Since inception, state legislatures in 47 states adopted the UTSA. Many states, however, have enacted modified versions of the model statute, implementing their own amendments, and thwarting the goal of unity.

Furthermore, state courts in UTSA states have subsequently adopted and promulgated varying interpretations of their respective state statutes. Therefore, although the UTSA limits some jurisdictional disparities, it does not provide the universal scheme enjoyed by other forms of intellectual property like patent law (the U.S. Patent Act) and trademark law (the Lanham Act).

Moreover, more than 30 years after UTSA's publication, three states — Massachusetts, New York and Texas — have yet to adopt any version of the UTSA. New York and Texas rely on common law alone and are guided by the Restatement (First) of Torts (1939), which provides an oft-cited definition of trade secrets.[1] Massachusetts, on the other hand, adopted its own trade secret statute based on common law and distinct from the UTSA.

Differences Between Common Law and UTSA Jurisdictions

The differences in trade secret law between UTSA and non-UTSA states are not as easy to spot as one might imagine, particularly because the trade secrets laws in UTSA states themselves are not particularly uniform.

For example, the UTSA instituted a three-year statute of limitations on trade secret claims. All three non-UTSA states (Massachusetts, New York and Texas), despite their refusal to accept the model act, similarly impose a three-year statute of limitations on trade secret claims.

Among states that have accepted their own version of the UTSA, though, the statutes of limitations for trade secrets claims vary between two and five years. A close comparison, however, between UTSA and non-UTSA states reveals a few important distinctions common among non-UTSA states.

Continuous Use

Although the general goal of the UTSA was to codify existing common law, the drafters of the uniform act acknowledged that they made at least one "reasonable departure" from common law. At common law, as is still the case in Massachusetts, New York and Texas, a piece of information must be in "continuous use" in the operation of a business to qualify as a trade secret.

The Restatement (First) of Torts, which governs New York and Texas, explicitly requires that "a trade secret is a process or device for continuous use in the operation of a business." Massachusetts courts agree with this limitation.

The UTSA, on the other hand, dispenses with the continuity requirement, resulting in an arguably wider class of protected trade secrets in UTSA jurisdictions, including, for example, a trade secret that has not yet been put to use or a trade secret that has been used and abandoned.

Threatened Misappropriation and Inevitable Disclosure

The UTSA provides that injunctive relief is a proper remedy to prevent "actual or threatened misappropriation" of trade secrets. Although UTSA states vary in defining "threatened misappropriation," some UTSA states interpret the "threatened misappropriation" language to implicate an "inevitable disclosure" doctrine, whereby a trade secret owner may obtain injunctive relief to prevent a former employee from working for a direct competitor, despite the trade secret owner's inability to prove actual or threatened misappropriation.

As a rationale for the doctrine, employers argue that unavoidable disclosure or use of trade secrets would occur if employees with knowledge of trade secrets entered the employ of competitors.

Even UTSA states apply the doctrine inconsistently, while non-UTSA states, lacking the benefit of the "threatened misappropriation" UTSA language, have even more reason to reject the inevitable disclosure doctrine.

Indeed, Massachusetts courts indicate that, because Massachusetts lacks the "threatened misappropriation" UTSA language, Massachusetts requires a showing of actual use of a trade secret, and does not adhere to the inevitable disclosure doctrine, favoring instead the public policy preference for employee mobility and freedom of employment.

Texas courts, although failing to squarely address the issue, have shown disfavor for the inevitable disclosure doctrine. New York courts, on the other hand, curiously adopted the inevitable disclosure doctrine, but note that it "treads an exceedingly narrow path through judicially disfavored territory," and should be "applied in only the rarest of cases."

In so noting, the New York court acknowledged that states that have accepted the inevitable disclosure doctrine are bound by the UTSA "threatened misappropriation" language, while New York is not so bound.

Attorneys' Fees

The UTSA expressly provides that attorneys' fees are available to a plaintiff where misappropriation was willful and malicious, and are available to a defendant where a claim of misappropriation was made in bad faith. The common law jurisdictions, on the other hand, do not authorize an award of attorneys' fees.

Because trade secret litigation is an increasingly utilized avenue of intellectual property protection, and attorneys' fee awards can reach into the millions of dollars, recovery of attorneys' fees is a valuable remedy, or potentially expensive risk, not available in the common law jurisdictions.

The Impact of the Holdouts

Although few in number, the common law states — Massachusetts, New York and Texas — account for 19 percent of the total U.S. gross domestic product (GDP), according to the U.S. Department of Commerce. New York and Texas both recently ranked in the top five jurisdictions in number of trade secret litigations, in both state and federal court. Texas was second only to California.

Also noteworthy are the industries concentrated in the common law states. Massachusetts, home of the first trade secret case, is a breeding ground of biotechnology and is certain to be home to more trade secret litigation.

In New York, Wall Street banks continue to grapple with trade secret protection for trading platforms and other proprietary financial tools. And Texas, a notoriously popular jurisdiction with respect to intellectual property, is known for its integrated circuit design and computer-related businesses.

In an age of technological innovation and widespread communication, the odds are high that such enterprises will find themselves pursuing or defending a trade secret misappropriation claim. Protection of trade secrets, including knowledge of the differences in each state's trade secret jurisprudence is imperative to corporate survival, particularly where certain jurisdiction-specific inconsistencies can come as a surprise to the unsuspecting litigant

The Future of the Holdouts

With New Jersey's recent UTSA adoption, the three UTSA holdouts have become the disparate minority. Whether or not they will continue to retain their grasp on common law remains to be seen. In Massachusetts, the UTSA's inroads are already in action. A bill to adopt UTSA was scheduled to be heard by the Massachusetts Joint Committee on the Judiciary in late February 2012.

But regardless of whether Massachusetts becomes the latest UTSA-adopter, companies protecting their trade secrets must be vigilant in investigating the law in the states where they operate, noting not only differences in common law jurisdictions versus UTSA states, but also acknowledging the even subtler differences among the UTSA-adopters as well.

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[1] Further complicating the trade secret landscape, the American Law Institute removed trade secret law from the Restatement (Second) of Torts. Trade secret law was instead transferred to the Restatement (Third) of Unfair Competition, a source upon which no state relies.