Three Key Distinctions Between the Uniform Trade Secrets Act and the Common Law

By Gregory S. Bombard – January 26, 2016

Only two states, New York and Massachusetts, have yet to adopt some form of the Uniform Trade Secrets Act (UTSA). Those states are commercial and biotechnology hubs that account for a significant amount of trade secrets litigation. As such, practitioners who handle trade secrets litigation should be aware of the key differences between the UTSA and the common law of Massachusetts and New York.

In Massachusetts and New York, trade secret protections are a mix of common law and limited statutory law. This means that there are significant differences between the familiar UTSA and trade secrets law in Massachusetts and New York. First, and most importantly, the types of information that qualify for trade secret protection differ. One key distinction is that Massachusetts and New York both require "continuous use" of a trade secret to qualify for protection. Second, Massachusetts and New York common law does not allow for the liberal cost-shifting provisions of the UTSA. Third, Massachusetts and New York are hesitant to apply the "inevitable disclosure" doctrine to enjoin the threatened misappropriation of trade secrets held by a former employee.

The Definition of a Protectable Trade Secret

Both New York and Massachusetts use a multifactor balancing test to determine whether information qualifies as a "trade secret." In theory, this distinction has the potential to cover more information than the UTSA definition. In practice, the most significant distinction between the UTSA and the common law is the common-law requirement of continuous use.

Under UTSA section 1(4), a "trade secret" is:

> information . . . that (i) derives independent economic value . . . 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.

New York common law defines a trade secret using a complex, six-factor balancing test. The general definition of a trade secret is "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." *Ashland Mgmt. Inc. v. Janien*, 624 N.E.2d 1007, 1013 (N.Y. 1993). This definition includes a six-factor balancing test, but the lack of a single factor is not fatal to a claim of trade secrets:

> "(1) the extent to which the information is known outside of [the] business; (2) the extent to which it is known by employees and others involved in [the] business; (3) the extent of

> measures taken by [the business] to guard the secrecy of the information; (4) the value of the information to [the business] and [its] competitors; (5) the amount of effort or money expended by [the business] in developing the information; (6) the ease or difficulty with which the information could be properly acquired or duplicated by others."

Ashland, 624 N.E.2d at 1013 (alterations in original) (quoting *Restatement of Torts* § 757 cmt. b).

Because none of these factors is intended to be dispositive, it is theoretically possible that something could qualify for the New York common-law definition of trade secret without the holder taking the reasonable efforts to keep the information secret that is required by the UTSA. In reality, though, four of the six factors listed relate to the protection of the secrecy of the information, so it is unlikely that a court would consider information a trade secret even under New York common law if the holder did not take reasonable steps to protect the secrecy.

Massachusetts has adopted the same six-factor test from the Restatement. *Jet Spray Cooler, Inc. v. Crampton*, 282 N.E.2d 921, 925 (Mass. 1972). But Massachusetts common law goes a step further when it comes to the confidentiality of the information. Like the UTSA, the Massachusetts Supreme Judicial Court expressly requires the information subject to trade secret protection be kept confidential: "The crucial issue to be determined in cases involving trade secrets . . . is whether the information sought to be protected is, in fact and in law, confidential." *Jet Spray Cooler*, 282 N.E.2d at 925. Like the UTSA, Massachusetts does not require "heroic measures" to preserve trade secrets, just "proper and reasonable steps." *USM Corp. v. Marson Fastener Corp.*, 393 N.E.2d 895, 902 (Mass. 1979) (quoting *J.T. Healy & Son v. James A. Murphy & Son*, 260 N.E.2d 723, 730 (Mass. 1970)).

In practice, the most commonly cited distinction between the UTSA and the laws of Massachusetts and New York is the so-called "continuous use" requirement. Under the UTSA, a trade secret is any information that derives independent economic value from not being generally known. UTSA § 1(4). This definition includes information that is not actually in use. For example, the UTSA would protect the formula not only for Coca Cola, but also for New Coke. While Coca Cola is, mercifully, no longer marketing New Coke, the secret recipe is still considered valuable. It therefore qualifies as a trade secret under the UTSA.

Not so under the common law. The definitions of "trade secret" under both Massachusetts and New York law require that the protected information be "used in one's business." *J.T. Healy*, 260 N.E.2d at 729; *Ashland*, 624 N.E.2d at 1013. *But see* *Storage Tech. Corp. v. Custom Hardware Eng'g & Consulting, Ltd.*, No. 02-12102, 2006 WL 1766434, at *10 (D. Mass. June 28, 2006) (questioning continuing validity of "continuous use" requirement). This distinction requires that secret information be currently in use in order to qualify for trade secret protection. Therefore, under the common law, the most famous example of a trade secret, the Coca Cola formula remains protected but the formula for New Coke does not unless it is still "used in [Coca Cola's] business."

Availability of Attorney Fees
The UTSA contains a powerful fee-shifting provision that authorizes courts to award attorney fees where "(i) a claim of misappropriation is made in bad faith, (ii) a motion to terminate an injunction is made or resisted in bad faith, or (iii) willful and malicious misappropriation exists." UTSA § 4. This provision adds an additional deterrent not only against misappropriation, but also against the filing of a bad-faith suit against an alleged misappropriator.

In the common-law states, the potential for fee shifting is much more limited. Under New York law, courts will not award attorney fees absent a contractual or statutory provision requiring the award. *Levine v. Infidelity, Inc.*, 770 N.Y.S.2d 83, 84 (App. Div. 2003). New York courts recognize a limited exception to this rule, and allow awards of attorney fees to prevailing parties where the plaintiff's damages "have been proximately related to the malicious acts and the acts themselves must have been entirely motivated by disinterested malevolence on [the defendant's] part." *Brook Shopping Ctrs., Inc. v. Bass*, 483 N.Y.S.2d 1021, 1022 (App. Div. 1985). In a trade secrets case, this exception is unlikely to arise because, generally speaking, the defendant's motivation is to profit from the theft of the trade secrets, not just to harm the plaintiff. The New York courts recognize a further exception where the fees are the result of the frivolous conduct of the other party. N.Y. Uniform Trial Ct. R. § 130-1.1.

Under Massachusetts law, theft of trade secrets is a per se violation of the Massachusetts Consumer Protection Act, chapter 93A. The plaintiff in an action brought under that statute may recover attorney fees. Mass. Gen. L. ch. 93A, § 11. But the section does not contain any provision that would allow the *defendant* to recover fees in an action wrongfully brought against him or her. Massachusetts law generally provides for fee shifting in only limited circumstances, where the court makes a finding that "all or substantially all of the claims . . . were wholly insubstantial, frivolous, and not advanced in good faith." Mass. Gen. L. ch. 231, § 6F. A successful motion under this statute requires a much higher burden of proof than the UTSA. Not only must a claim be "not advanced in good faith," it also must be found to be "wholly insubstantial" and "frivolous." In order for a defendant to succeed on such a claim, he or she must show an utter "absence of legal or factual basis for the claim." *Demoulas Super Mkts., Inc. v. Ryan,* 873 N.E.2d 1168, 1175–76 (Mass. App. Ct. 2007).

Inevitable Disclosure Doctrine
The UTSA allows the owner of a trade secret to obtain an injunction against "threatened disclosure" of a trade secret as well as its actual disclosure. This distinction is a departure from common law where the plaintiff must demonstrate a reasonable likelihood of success on the merits to obtain an injunction. In the employment context, courts have interpreted the UTSA's "threatened disclosure" language to create a sort of de facto noncompete. The common-law jurisdictions remain hesitant to impose such restrictions.

The UTSA provides that "[a]ctual *or threatened* misappropriation may be enjoined." UTSA § 2(a) (emphasis added). Some courts interpret this language to mean that the court may fashion an injunction against a former employee's work at a competitor where the disclosure of trade secrets would be inevitable. The leading case on this issue is *PepsiCo, Inc. v. Redmond*, 54 F.3d 1262 (7th Cir. 1995), in which a high-ranking Pepsi executive quit to work for Pepsi's "fierce" then-competitor Quaker. Pepsi obtained an injunction against the employee's continued employment with Quaker because the district court found that the employee's disclosure of confidential marketing and development strategies was inevitable. The Seventh Circuit affirmed, expressly overruling common law, on the basis of the "threatened misappropriation" language of the Illinois Uniform Trade Secrets Act. The court was motivated, in part, by the employee's lack of candor when leaving his employment with Pepsi. Since the *PepsiCo* ruling, the majority of UTSA jurisdictions to consider the issue have adopted some form of this "inevitable disclosure" agreement. *See* *Whyte v. Schlage Lock Co.*, 125 Cal. Rptr. 2d 277, 291 (Ct. App. 2002) ("Our survey confirms the majority of jurisdictions addressing the issue have adopted some form of the inevitable disclosure doctrine.").

The common-law states have struggled with whether to apply the doctrine. No New York appellate court has expressly adopted the doctrine. *See* *Marietta Corp. v. Fairhurst*, 754 N.Y.S.2d 62, 65 (App. Div. 2003). Some lower courts have applied the doctrine, *see, e.g.*, *Payment Alliance Int'l, Inc. v. Ferreira*, 530 F. Supp. 2d 477, 482 (S.D.N.Y. 2007), but there appears to be a recent backlash against the application of the doctrine. For example, in *Janus et Cie v. Kahnke*, No. 12 Civ. 7201 (S.D.N.Y. Aug. 29, 2013), the United States District Court for the Southern District of New York ruled that applying the doctrine in the absence of a bargained-for noncompete agreement would be inappropriate. *See also Marietta*, 754 N.Y.S.2d at 65–66 (expressing similar reluctance to apply the inevitable disclosure doctrine as a result of its "implied-in-fact restrictive covenant").

Massachusetts courts have also struggled with whether to apply the doctrine. For example, in *Architext, Inc. v. Kikuchi*, No. 0500600, 2005 WL 2864244 at *3 (Mass. Super. Ct. May 19, 2005), the Massachusetts Superior Court cited the doctrine of inevitable disclosure, noted that it had not been adopted by any Massachusetts appellate court, and ultimately ruled that it would not apply the doctrine because the defendants in that case were not working for a direct competitor. Similarly, the Superior Court appeared to reject the doctrine in *CSC Consulting, Inc. v. Arnold*, No. 001800, 2001 WL 1174183, at *3 (Mass. Super. Ct. July 12, 2001), ruling that, "If this Court followed the plaintiff's reasoning, any employee who was exposed to confidential information during his or her employment would be barred from working for a competitor, regardless of contractual obligations, based on the mere threat of misappropriation." On the other hand, the United States District Court for the District of Massachusetts frequently applies the doctrine, albeit somewhat inconsistently. *See, e.g.,* *Corporate Techs., Inc. v. Harnett*, 943 F. Supp. 2d 233, 241 (D. Mass. 2013) (discussing whether prior case law considered "inevitable disclosure" to be an element of the plaintiff's likelihood of success on the merits or irreparable harm under injunction analysis).

Conclusion

Trade secret practitioners must be aware of the distinctions between the familiar UTSA protections and the common law of Massachusetts and New York. Those jurisdictions have a well-developed common-law protection of trade secrets that differs in significant ways from the UTSA. Massachusetts and New York require that a secret be in continuous use to qualify for protection, they reject the UTSA's liberal fee-shifting provisions, and they are hesitant to apply the inevitable disclosure doctrine to bar a former employee from working for a competitor.

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Gregory S. Bombard is an associate with Duane Morris LLP in Boston, Massachusetts.