

SPEAKERS:
Irene Kosturakis,
BMC Software, Inc.

Greg Porter,
Andrews Kurth

The Uniform Patch to Texas Trade Secret Law – TUTSA Overview and Best Practices

**ANDREWS
KURTH**

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The Uniform Patch to Texas Trade Secret Law–TUTSA Overview and Best Practices



"You spelled 'confidential' wrong."

Trade Secret Protection Around the World

- Many countries, including, remarkably, most in Europe do not have specific trade secrets laws.
- In such jurisdictions, trade secret owners must rely on protection under unfair competition laws and tort laws, file actions under breach of contract actions, and deal with a patchwork of fragmented laws found in labor, industrial property, and criminal codes.

Final Study April 2013 Prepared for the EU Contract #: MARKT/2011/128/D, Study on Trade Secrets and Confidential Business Information in the Internal Market, p.4, http://ec.europa.eu/internal_market/iprenforcement/docs/trade-secrets/130711_final-study_en.pdf (last visited Feb. 2, 2014).

Trade Secret Protection Around the World

- Study on Trade Secrets and Confidential Business Information in the Internal Market recommends that the EU Commission establish an initiative around trade secrets because it will foster economic growth, competitiveness, and innovation in the EU single market.

Id at p. 151.

Texas Common Law on Trade Secrets

- Based on Restatement (First) of Torts (1939), Restatement (Third) of Unfair Competition, and Texas Theft Liability Act
- Trade secret was “any formula, pattern, device or compilation of information which is used in one’s business and presents an opportunity to obtain an advantage over competitors who do not know or use it.” *Computer Assoc. Intern v. Altai*, 918 S.W.2d 453, 455 (Tex. 1994); *Hyde Corp. v. Huffines*, 314 S.W.2d 763, 776 (1958) (quoting Restatement of Torts § 757 (1939))

Texas Common Law on Trade Secrets – Frequent Issues

- Confidentiality, non-disclosure, and other contracts – companies unwilling to accept TX governing law.
- Litigation – under common law in case involving multi-state parties there was often extensive disputes about what state law applied –TX or a UTSA state.

What Texas Businesses Want

- In assessing what is considered a trade secret and constitutes misappropriation under the law:
 - Clarity
 - Consistency
 - Uniformity
 - Predictability
- Use Texas as governing law under Confidentiality and Nondisclosure Agreements
- More predictability and certainty in litigation

What is a Trade Secret Under Common Law?

- Information
- Has independent economic value
- Not generally known
 - To the public
 - To others who can obtain economic value from its disclosure or use
- Kept secret
- **Not readily ascertainable (TX)**

What is a Trade Secret under TUTSA?

- Customer List
 - UTSA and common law – per case law
 - TX – now per statute
- Financial Data
 - UTSA and common law – per case law
 - TX – now per statute

Texas Common Law on Trade Secrets – negative know-how

- Is R&D information, negative know-how, or prior pricing or bid information protected?
- Negative Know-How – “Hurst's information, while of some benefit provided only negative, ‘what not to do’, input to Hughes” and was held not to be a protectable trade secret. *Hurst v. Hughes Tool Co.*, 634 F.2d 895, 899 (5th Cir. 1981)
- Negative Know-How – a company’s competitive advantage from “trial and error of eliminating what did not work” was held to be protectable. *Mabrey v. Sandstream, Inc.*, 124 S.W.3d 302, 319 (Tex.App. - Fort Worth, 2003)

Texas Common Law on Trade Secrets – “continuous use”

- “Continuous use” requirement - *Hyde Corp. v. Huffines*, 314 S.W.2d at 776 (1958) (“A trade secret is a process or device for continuous use in the operation of the business.”)
- “Continuous use” requirement - *Bertotti v. C.E. Shepherd Co.*, 752 S.W.2d 648, 653 (Tex.App. - Houston [14th Dist.] 1988, no writ) (“The mere fact that a company is not utilizing information at the present time does not prevent that information from being a trade secret subject to protection.”)

Texas Common Law on Trade Secrets – “inevitable disclosure”

- Inevitable Disclosure Doctrine – “no Texas case [has] expressly adopt[ed] the inevitable disclosure doctrine, and it is unclear to what extent Texas courts might adopt it....” *Cardinal Health Staffing Network, Inc. v. Bowen*, 106 S.W.3d 230, 242 (Tex.App. - Houston [1st] 2003, no pet.)
- The mere fear or theoretical possibility that the defendant could use a trade secret against the plaintiff is not sufficient for injunctive relief. *EMSL Analytical, Inc. v. Younker*, 154 S.W.3d 693, 697 (Tex.App. - Houston [14th Dist.] 2004, no pet.)

Texas Common Law on Trade Secrets – “inevitable disclosure”

- Inevitable Disclosure Doctrine – *Conley v. DSC Communications Corp.*, No. 05-98-01051-CV, 1999 WL 89955, at *3-4 (Tex. App. Dallas Feb. 24, 1999, no pet.) (Enjoining an employee from using an employer’s confidential information is appropriate when it is probable that the former employee will use the confidential information for his benefit (or his new employer’s benefit) or to the detriment of his former employer)
- See also, *Rugen v. Interactive Bus. Sys., Inc.*, 864 S.W.2d 548, 552 (Tex. App. Dallas 1993, no writ) (Enjoining defendant who was is “in a position to use” the information and probably would)

Texas Uniform Trade Secret Act (TUTSA)

- The process of drafting, introducing, amending, and passing the TUTSA
 - Took effect September 1, 2013
 - Was passed 31-0 in Senate and 146-1 in House
 - Introduced by the Texas Business Law Foundation, with support by the Business Law Section and the Trade Secret Committee of the Intellectual Property Law Section
 - Letters of support to Governor

Texas Uniform Trade Secret Act (TUTSA)

- Texas enacted its version of the Uniform Trade Secret Act effective September 1, 2013 and has a criminal statute as well.
 - It was time Texas law became uniform with 46 other states' laws
 - Massachusetts has since introduced the UTSA in H.B. 27
 - New York relies on its common law
 - North Carolina enacted a modified version of the UTSA with many of its key principles. N.C. Gen. Stat. §§ 66-152 et seq.

What is a Trade Secret under TUTSA?

- Information, including a formula, pattern, device, compilation of information, program, method, technique, process, **financial data, or list of actual or potential customers or suppliers** that:
 - 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
 - is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

Tex. Civ. Prac. Rem. Code, §134A.002(6) (2013).

Non-Uniform Language in the Texas UTSA

- TUTSA's definition of "trade secret" includes "financial data" and a "list of actual or potential customers or suppliers"

Tex. Civ. Prac. Rem. Code, §134A.002(6) (2013).

Non-Uniform Language in the Texas UTSA

- Two additional definitions:
 - “Proper means” defined as “discovery by independent development, reverse engineering unless prohibited, or any other means that is not improper.”
Id. at §134A.002(4).
 - “Reverse engineering” means “the process of studying, analyzing, or disassembling a product or device to discover its design, structure, construction, or source code provided that the product or device was acquired lawfully or from a person having a legal right to convey it.”
Id. at §134A.002(5).

Non-Uniform Language in the Texas UTSA

- Finally, there is a presumption in favor of granting protective orders to preserve the secrecy of alleged trade secrets in litigation.
 - While included in UTSA this differs from prior TRCP.

Id. at §134A.006.

Language That Did Not Make the Original Bill and Amendments

- Requirement of trade secret identification with “reasonable particularity” before commencing discovery like California has.
- Fact finder for enhanced damages
- Standard for enhanced damages
- Texas trial lawyers and tort reform input

Misappropriation Under TUTSA

- acquisition of a trade secret of another by a person who knows or has reason to know that the trade secret was acquired by improper means; or
- disclosure or use of a trade secret of another without express or implied consent by a person who:
 - used improper means to acquire knowledge of the trade secret;

Misappropriation Under TUTSA

- at the time of disclosure or use, knew or had reason to know that the person's knowledge of the trade secret was:
 - derived from or through a person who had utilized improper means to acquire it; or
 - acquired under circumstances giving rise to a duty to maintain its secrecy or limit its use; or
 - derived from or through a person who owed a duty to the person seeking relief to maintain its secrecy or limit its use; or
 - before a material change of the person's position, knew or had reason to know

Threatened Misappropriation Under the TUTSA

- Actual or threatened misappropriation may be enjoined
- Different from inevitable disclosure

Detecting Misappropriation

- Reviewing departed employees' computers
 - “Sent” and “deleted” emails
 - Computer access prior to departure
- “Dummy names” on customer lists
- Strategic typos in documents or source code
- Monitoring computer systems
- Imaging and archiving hard drives and not reassigning computers

Common Defenses to Trade Secret Claims

- No protectable information (patent issues)
- Independent development
- Improper claim of inevitable disclosure
- Statute of limitations
- Preempted by federal law

TUTSA Civil Damages

- Compensatory Damages:
 - Actual loss caused by misappropriation
 - Unjust enrichment not taken into account in computing actual loss
 - Reasonable royalties for a misappropriator's unauthorized disclosure or use if neither damages nor unjust enrichment are provable
- Exemplary damages:
 - Willful and malicious misappropriation - not exceeding twice compensatory damages

TUTSA Civil Damages

Attorneys' fees

- Discretionary, reasonable plus court costs
- Willful and malicious misappropriation exists
- Claim made in bad faith
- A motion to terminate an injunction is made or resisted in bad faith

Criminal Actions Based on Trade Secret Misappropriation

- Courts also enforce trade secret laws through criminal proceedings
- Texas also allows for criminal penalties for theft of trade secret, which is considered a third-degree felony under Texas Penal Code Section 31.05(a)(4)
- Economic Espionage Act

Criminal Actions Based on Trade Secret Misappropriation—Economic Espionage Act (EEA)

- The EEA is the federal act providing criminal penalties for misappropriating the trade secrets or competitive information of US companies
- Enacted in October of 1996 to provide federal statute to prosecute economic espionage in a systematic manner other than the 1930's Interstate Transportation of Stolen Property Act
- The Uniform Trade Secrets Act and other state statutes provided no effective criminal response

Criminal Actions Based on Trade Secret Misappropriation–Economic Espionage Act (EEA)

- Two sections: 1831 and 1832
- Control acts committed outside the country
- EEA applies if the offender is a citizen or resident alien of the United States, or an organization organized under the laws of the United States or any state

Overview and Best Practices Economic Espionage Act (EEA) Section 1831

- Section 1831 applies when there is evidence of foreign government-sponsored or coordinated intelligence activity. The Government must prove that:
 - the defendant stole, or without the owner's authorization obtained, destroyed, or conveyed information that he knew or believed was a trade secret;
 - the information was a trade secret; and
 - the defendant intended or knew that the offense would benefit a foreign government, instrumentality, or agent

18 U.S.C. §1831

Economic Espionage Act (EEA) Section 1831

- The penalties of an individual convicted under Section 1831 are that the defendant can be imprisoned for up to 15 years and be fined up to \$5,000,000 USD, and an organization can be fined the greater of \$10,000,000 USD or three times the value of the trade secret to the organization, including expenses for research and development and other costs of reproducing the trade secret that the theft avoided.

Id.

Economic Espionage Act (EEA)

- Under Section 1832, the Government must prove beyond a reasonable doubt that:
 - the defendant stole, or without the owner's authorization obtained, sent, destroyed, or conveyed information that he knew or believed was a trade secret;
 - the information was in fact a trade secret;
 - the defendant intended to convert the trade secret to the economic benefit of somebody other than the owner;

Economic Espionage Act (EEA)

- the defendant knew or intended that the owner of the trade secret would be injured; and
- the trade secret was related to, or was included in, a product or service used in or intended for use in interstate or foreign commerce.

Economic Espionage Act (EEA) 18 U.S.C. 1832

- The penalties for individuals convicted under Section 1832 are imprisonment for up to ten years and a fine of up to \$250,000 USD, and an organization can be fined up to \$5,000,000 USD.

18 U.S.C. §1832.

Economic Espionage Act (EEA)

- Theft of Trade Secrets Clarification Act of 2012 enacted to clarify the scope of Section 1832 to reverse *United States v. Aleynikov*. 676 F.3d 71 (2d Cir. 2012)
- Changed the prior language which before the clarification stated that the trade secret be *“included in a product that is produced for or placed in interstate or foreign commerce ...”*
- In that manner, the enactment of the Theft of Trade Secrets Clarification Act of 2012 provided for the protection of wholly internal proprietary information if the information relates to products or services that are used in interstate or foreign commerce

Criminal vs. Civil – Practical Considerations

- Discovery Issues
- Fifth Amendment Issues
- Stays of Civil Case
- Settlement Complications

Weapon to Combat Overseas Theft of Trade Secrets

- Under Section 337 of the Tariff Act of 1930 the International Trade Commission can exclude imports when it finds “unfair methods of competition and unfair acts in the importation” (19 USC §1337)
- Any product manufactured overseas with the assistance of misappropriated trade secrets of a U.S. business can be refused entry into the U.S. even if theft occurred entirely on foreign soil

TianRui v. Int’l Trade Comm’n, No.2010-1395 (Fed. Cir. 2011)

Statutes Related to Trade Secrets

- Texas Uniform Trade Secrets Act - Civ. Prac. & Rem. C. § 134A.001, et. seq.
- Texas Penal Code § 31.05(a)(4)
- Texas Harmful Access By Computer - Civ. Prac. & Rem. C. § 143.001, et. seq.
- Texas Penal Code § 33A
- Federal Economic Espionage Act - 18 U.S.C. § 1831, et seq.
- Federal Computer Fraud and Abuse Act - 18 U.S.C. § 1030. et. seq.
- Federal Electronic Communications Privacy Act - 18 U.S.C. § 1030. et. seq.
- Tariff Act - 18 U.S.C. § 337 (*TianRui v. Int'l Trade Comm'n.*)

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Irene Kosturakis

Chief IP Counsel
BMC Software, Inc.
+1.713.918.2233
irene_kosturakis@bmc.com



Greg Porter

Partner
Andrews Kurth
+1.713.220.4621
GregPorter@andrewskurth.com