

# Trade Secrets – The Basic Principles and Issues

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## I. TRADE SECRETS DEFINED

Trade secret law is state-specific. As of this writing, all but two states have adopted the Uniform Trade Secrets Act. The remaining states (New York and Massachusetts) follow the Restatement of Torts or the Restatement (Third) of Unfair Competition. The definition of a trade secret for each of these sources is provided below.

### A. Uniform Trade Secrets Act

As of January 2014, the Uniform Trade Secrets Act (“UTSA”) has been enacted, in one form or another, by 48 states and the District of Columbia, Puerto Rico and the U.S. Virgin Islands.<sup>1</sup> The UTSA was completed by the Uniform Law Commissioners in 1979, and amended in 1985. The UTSA defines a trade secret as:

*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.*

UTSA § 1(4) (1985).

### B. Restatement of Torts

The Restatement of Torts provides the common law definition of trade secrets. “Despite UTSA’s widespread adoption, the Restatement definition retains vitality and is often referred to by courts during the course of their deliberations in applying UTSA.” Roger M. Milgrim, 1

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<sup>1</sup> <http://www.uniformlaws.org/LegislativeFactSheet.aspx?title=Trade%20Secrets%20Act>

*Milgrim on Trade Secrets* § 1.01[1]. Comment b of the Restatement of Torts, Section 757 provides the following definition:

*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 or other device, or a list of customers. It differs from other secret information in a business (see § 759) in that it is not simply information as to single or ephemeral events in the conduct of the business, as, for example, the amount or other terms of a secret bid for a contract or the salary of certain employees, or the security investments made or contemplated, or the date fixed for the announcement of a new policy or for bringing out a new model or the like. 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.*

Restatement (First) of Torts § 757 (1939).

C. **Restatement of Unfair Competition**

The Restatement of Unfair Competition defines a trade secret as follows:

*A trade secret is any information that can be used in the operation of a business or other enterprise and that is sufficiently valuable and secret to afford an actual or potential economic advantage over others.*

Restatement (Third) of Unfair Competition § 39 (1995).

D. **What Types of Information Can Be A Trade Secret?**

Trade secrets can be formulas, processes, methods and techniques (know-how), machines, products, plans designs, patterns, customer lists, and business information can be a trade secret. Roger M. Milgrim, 1 *Milgrim on Trade Secrets* § 1.09. The following are examples of information that have been found to be a trade secret:

1. The formula for the soft drink Coca-Cola. *Coca-Cola Bottling Co. of Shreveport, Inc. v. Coca-Cola Co.*, 107 F.R.D. 288, 289 (D. Del. 1985).
2. A formula for hair conditioner. *Thomas v. Soft Sheen Prod. Co.*, 500 N.Y.S.2d 108 (App. Div. 1986); *West v. Alberto Culver Co.*, 486 F.2d 459, 461 (10th Cir. 1973).
3. A process for manufacturing a vaccine. *Merck & Co. v. SmithKline Beecham Pharms. Co.*, C.A. No. 15443-NC, 1999 Del. Ch. LEXIS 242, \*50-\*63 (Del. Ch. August 5, 1999), *aff'd per curiam*, 746 A.2d 277 (Del.), *aff'd*, 766 A.2d 442 (Del. 2000).
4. A process for manufacturing synthetic diamonds. *General Elec. Co. v. Sung*, 843 F. Supp. 776, 778-9 (D. Mass. 1994).
5. Know-how such as operating procedures, training manuals and process standards for using equipment to make adhesive resin sheeting. *Minnesota Mining & Mfg. Co. v. Pribyl*, 259 F.3d 587, 595-96 (7th Cir. 2001).
6. A machine for manufacturing synthetic diamonds. *General Elec.*, 843 F. Supp. 776 at 779.

## II. PROTECTION OF TRADE SECRETS

### A. Both the Law and Nature of Trade Secrets Necessitates Protection

Trade secrets are protected under the UTSA and common law. Trade secret protection attaches automatically when information of value to the owner is kept secret by the owner. However, protection only endures as long as the requirements for protection – generally, value to the owner and secrecy – continue to be met. Trade secret protection is lost if owner fails to take reasonable steps to keep the information secret. Thus, it is necessary to protect trade secrets because once they are disclosed or no longer secret, their value is lost. Courts enforce the UTSA's requirement that a trade secret owner take reasonable measures to protect the secrecy of a trade secret.

### B. The Limits of Trade Secrets Protection

Trade secret owners have recourse only against the “misappropriation” of a trade secret. Discovery of protected information through independent research or reverse engineering is NOT misappropriation. In contrast, a patent owner may always prevent others from using a patented invention as long as the patent is valid and its term has not expired.

### C. Some Possible Protection Measures

Companies should implement procedures to protect their trade secrets. “The nature and character of the vigilance required of the owner to protect secrecy varies, depending upon a variety of factors. Among things to be considered are the size and character of the enterprise (generally, large, sophisticated enterprises are held to a higher ‘secrecy effort’ standard), the location of the enterprise (elaborate steps that may be required in an ‘industrially dense’ area may not be required in, say a rural area) and the nature and character of the enterprise’s staff.” Roger M. Milgrim, 1 *Milgrim on Trade Secrets* § 1.04. A company should conduct regular trade secret audits so that it is aware of its trade secrets and can take reasonable steps to protect them.

Employees with access to trade secret information should be made aware of the information’s status as a trade secret, and should be educated as to how to protect the trade secret information. Such information should be clearly marked as confidential or proprietary. Employment agreements may be used to protect trade secret information by including non-disclosure provisions for secret information, restricting the use of the trade secrets, and including non-compete provisions on termination of the employee.

Companies should use reasonable security methods to prevent unauthorized access to office facilities and computer systems containing trade secret information. Trade secret information should be kept under lock and key. Access to computer systems should be terminated and limited when appropriate. Companies should monitor computer usage of trade secret information and eliminate employees’ expectations of privacy with respect to computer usage. Physical access to trade secrets stored on computers should be controlled using computer passwords to manage access to the trade secrets.

Companies should implement exit procedures on the termination or departure of an employee who had access to trade secret information. For example, an information technology representative should review the employee’s pre-departure copying, downloading, and transfer of data; disable account and access privileges; disconnect the terminated employee’s computer; examine the employee’s computer and emails; and copy employee’s computer hard drive and personal digital assistant (e.g. smartphone, blackberry) before reissuing it.

Finally, trade secrets must be policed to remain protected. If any improper disclosure, theft or misappropriation is discovered, the company should take appropriate action as soon as possible.

#### D. **Non-Disclosure Agreements**

Non-Disclosure Agreements (NDAs), also referred to as Confidentiality Agreements, frequently are used to protect trade secret information. However, they may not be used to protect:

1. information already in the receiving party’s possession;

2. information that becomes generally available to the public other than as a result of disclosure by the recipient;
3. information that becomes available to the recipient on a non-confidential basis; or
4. information that was independently developed by the recipient.

NDA's should be in place before disclosure of trade secret information. Confidential and/or trade secret information should be conspicuously marked as confidential.

### III. SELECTED LITIGATION ISSUES IN TRADE SECRET LITIGATION

#### A. Identification of Trade Secrets

One of the most critical decisions in any trade secret lawsuit is the decision on what information or materials to claim as the trade secrets at issue in the case. Unlike other forms of intellectual property, a trade secret owner does not have to file an application or registration identifying or describing its trade secrets, so competitors, former employees or other alleged infringers often do not know exactly what a plaintiff will allege as its trade secrets prior to suit. How a plaintiff decides to claim and describe its trade secrets often can make the difference between winning and losing.

A trade secret plaintiff should be careful to focus only on information and materials that are truly secret or proprietary. Plaintiffs often claim that all business information to which a former employee might have had access constitutes trade secrets. This strategy, however, at best unduly complicates the lawsuit, and at worst can be used to undermine the plaintiff's claim by showing that much of the claimed information or material is not protectable as the trade secret. In addition, it helps if the plaintiff has identified the particular information or material as being confidential or proprietary in the normal course of its business or in connection with a specific disclosure under a non-disclosure agreement, rather than trying to make the argument for the first time in litigation. *See, e.g., Convolv, Inc. v. Compaq Computer Corp.*, 527 Fed. Appx. 910 (Fed. Cir. 2013) (affirming summary judgment to defendant because plaintiff did not identify alleged trade secrets disclosed under NDA as confidential).

The procedural aspect of identifying trade secrets in litigation also is important. There is always a tension in the discovery phase of trade secret litigation between the interests of the plaintiff and the defendant regarding the identification of trade secrets. A plaintiff normally will not want to identify its trade secrets in great detail at the outset of a lawsuit, and would prefer to obtain information or documents regarding the defendant's products or processes so the plaintiff can fashion as broad a claim as possible and tailor it to the defendant's uses. Defendants, on the other hand, usually want the plaintiff to identify early in the lawsuit exactly what trade secrets the plaintiff contends are at issue, and does not want to disclose to the plaintiff any more of its own proprietary information than is absolutely necessary. Obviously, a plaintiff need not

disclose the details of its trade secrets in a publicly filed complaint. Beyond that general proposition, statutes and case law vary in how to handle this issue.

Certain jurisdictions require a plaintiff to identify its trade secrets with reasonable particularity before being allowed to obtain discovery relating to the trade secret from the defendant. *See* Cal. Civ. Proc. Code §2019(d) (statutory requirement that plaintiff identify trade secrets with specificity before being allowed to obtain discovery); *DeRubeis v. Witten Techs., Inc.*, 244 F.R.D. 676 (N.D. Ga. 2007) (requiring plaintiff to identify trade secrets at issue “with reasonable particularity” before obtaining discovery from defendant); *Leucadia, Inc. v. Applied Extrusion Techs., Inc.*, 755 F. Supp. 635 (D. Del. 1991) (granting protective order allowing defendant first to take discovery of plaintiff’s trade secrets before requiring defendant to respond to plaintiff’s discovery requests). Even in the absence of a legal requirement for a plaintiff to identify trade secrets at issue before obtaining discovery, courts have dismissed trade secret claims or denied relief where the plaintiff failed to identify the alleged trade secrets with sufficient particularity during the discovery process. *See, e.g., Imax Corp. v. Cinema Technologies, Inc.*, 152 F.3d 1161 (9th Cir. 1998); *Dapco Industries, Inc. v. Matec Corp.*, 168 F.3d 1322 (Fed. Cir. 1998).

Here are some issues that a plaintiff should consider in determining what trade secrets to identify and how to describe them:

- what has the company already identified as confidential or secret in the materials themselves or in communications with others;
- how important or commercially valuable is the information or material to be claimed, including how could that information or material be used against the plaintiff by a competitor; and
- the extent of money or other resources required to develop or create the alleged trade secret and, conversely, how much would be required to recreate it.

**B. Proof of Misappropriation**

Trade secret law protects against the “misappropriation” of trade secrets. Section 1(2) of the Uniform Trade Secret Act defines misappropriation as:

(i) 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

(ii) disclosure or use of a trade secret of another without express or implied consent by a person who

(A) used improper means to acquire knowledge of the trade secret; or

(B) at the time of disclosure or use, knew or had reason to know that his knowledge of the trade secret was

(I) derived from or through a person who had utilized improper means to acquire it;

(II) acquired under circumstances giving rise to a duty to maintain its secrecy or limit its use; or

(III) derived from or through a person who owed a duty to the person seeking relief to maintain its secrecy or limit its use; or

(C) before a material change of his [or her] position, knew or had reason to know that it was a trade secret and that knowledge of it had been acquired by accident or mistake.

“Improper means,” therefore, is a key element of proof. This element can be established by, among other things, breach of an employee confidentiality agreement, breach of a commercial non-disclosure agreement, breach of a license agreement, improper inducement of another to breach confidentiality obligations, theft, or industrial espionage.

Trade secret law does not, however, protect against derivation of a company’s secret processes or information by independent or other legitimate means. For example, trade secret law does not prohibit reverse engineering, the process of starting with a known product and working backward to discern the process by which it was created or manufactured. *See, e.g., Bonito Boats, Inc. v. Thunder Craft Boats, Inc.*, 489 U.S. 141 (1989). Similarly, the sale of a product to a party not under any duty to maintain confidentiality generally will destroy any reasonable expectation of secrecy as to that product and may place that product or information about how it works in the public domain. *See, e.g., Roboserve, Ltd. v. Tom’s Foods Inc.*, 940 F.2d 1441 (11th Cir. 1991). Trade secret law also does not protect information that is available or can be readily discerned from public sources.

Trade secret law generally does not restrict an employee from applying the skills and knowledge she developed during the course of an employment or other business relationship. *See, e.g., Servicetrends, Inc. v. Siemens Medical Systems, Inc.*, 870 F. Supp. 1042 (N.D. Ga. 1994). One area of frequent litigation involves the protectability of customers and customer information in the memory of a former employee. Some states’ trade secret statutes expressly limit the protectability of customer information to a “list” that must be in tangible written or electronic form. *See, e.g., Ga. Code §10-1-761(4)*. Regardless, it is more challenging for a plaintiff to prove misappropriation by taking from memory without proof of misappropriation of documents, electronic files, or other tangible things. *See, e.g., Carpetmaster, Ltd. v. Dupont Flooring Sys. Inc.*, 12 F. Supp. 2d 257 (N.D.N.Y. 1998) (making distinction under NY law

between use through “casual memory” of customer information, which is generally not actionable, and “intentional memorization” of customer list).

C. **When Evidence of Actual Misappropriation is Lacking**

The UTSA protects both actual and “threatened” misappropriation of trade secrets. Thus, injunctive relief is available upon showing sufficient evidence of a threat of misappropriation without having to wait until “the horse is already out of the barn.” Threatened misappropriation, however, requires more than simply a plaintiff’s fear or generalized suspicion that the defendant took or might misuse its trade secrets. The concept of “threatened” misappropriation can be thought of as a spectrum of potential evidence ranging from mere fear or speculation (no specific evidence at all) to evidence of conduct establishing actual taking or unauthorized use. Scenarios that might be sufficient to obtain relief based on threatened misappropriation include proof that the defendant has possession or knowledge of the plaintiff’s trade secret combined with evidence that:

- the defendant has actually misused or disclosed trade secrets in the past;
- the defendant has refused without justification to return the trade secret materials to the owner;
- the defendant intends to use or disclose the trade secrets;
- the trade secrets are relevant to an imminent competitive opportunity involving the plaintiff and defendant (*e.g.*, open bidding); or
- the defendant’s improper acquisition of the trade secret was particularly egregious, such as copying or downloading materials shortly before resigning employment.

*See, e.g., Bimbo Bakeries USA, Inc. v. Botticella*, 613 F.3d 102 (3d Cir. 2010); *Central Valley General Hospital v. Smith*, 162 Cal. App. 4th 501 (5th Dist. 2008).

Some courts have recognized the theory of “inevitable disclosure” as sufficient to establish trade secret misappropriation. The inevitable disclosure doctrine allows a trade secret owner to obtain injunctive relief to prevent a former employee from working for a competitor upon proof that the employee’s new responsibilities are so similar to his former duties that his new position will “inevitably” require him to rely upon, use, or disclose the former employee’s trade secrets, without proof of actual misappropriation or specific evidence of threatened use or disclosure discussed above. The seminal case applying the inevitable disclosure doctrine is *PepsiCo v. Redmond*, 54 F.3d 1262 (7th Cir. 1995). Even in the absence of a non-competition agreement, the court enjoined Redmond from taking a similar position with a competitor of his former employer PepsiCo for a period of six months. The court based its decision on the facts that the defendant’s position involved substantially the same responsibilities for marketing and

strategic planning, PepsiCo and the defendant's new employer were direct competitors in the product categories for which the defendant would be responsible, and the defendant had been less than fully truthful and forthcoming in connection with his departure and representations regarding his new employment. New York is an important jurisdiction that also applies the inevitable disclosure doctrine in certain situations. *See, e.g., IBM v. Papermaster*, 2008 WL 4974508 (S.D.N.Y. Nov. 21, 2008) (court may enjoin former employee from working for competitor “[e]ven where a trade secret has not yet been disclosed, . . . [where] the movant competes directly with the prospective employer and the transient employee possesses highly confidential or technical knowledge concerning marketing strategies or the like”).

Other jurisdictions, however, have rejected the inevitable disclosure doctrine as constituting an improper “back door noncompete” for which the parties did not bargain. *See, e.g., Whyte v. Schlage Lock Co.*, 101 Cal. App. 4th 1443 (2002) (rejecting inevitable disclosure doctrine as contrary to California public policy); *cf. Holton v. Physician Oncology Servs., LP*, 742 S.E. 2d 702 (Ga. 2013) (rejecting inevitable disclosure doctrine as an independent cause of action). Even in states that do not recognize the inevitable disclosure doctrine as a separate basis for injunctive relief, a trade secret plaintiff may use similar facts as evidence of “threatened” misappropriation to obtain injunctive relief in a proper case.

#### D. Related Claims

In addition to statutory or common law claims specifically for trade secret misappropriation, other claims may be available under federal or state law. State law trade secret claims often are accompanied by claims under the federal Computer Fraud and Abuse Act (“CFAA”), 18 U.S.C. §1830 *et seq.* Originally enacted as a criminal statute to protect computer systems from traditional “hackers,” Congress later created a private cause of action where, among other things, a person (1) intentionally accesses a computer without authorization or exceeds authorized access and thereby obtains information from a “protected computer” involving an interstate or foreign communication, or (2) knowingly and with intent to defraud accesses a protected computer without authorization or exceeds authorized access and obtains anything of value in excess of the statutory minimum amount. Courts have split on the issue of whether an employee “exceeds authorized access” where she is authorized to access the employer’s computer or network but uses that access or the information obtained for an unauthorized purpose adverse to the employer’s interest – *e.g.*, to start or assist a competing business. In addition to the CFAA, some states have analogous statutes addressing improper access or other misconduct relating to computer systems or computer information.

Counsel also should also consider the availability of state contract and tort claims in connection with trade secret misappropriation. If an employee has signed an employment agreement, the employer might have claims to enforce a non-competition or non-solicitation covenant, a non-disclosure agreement, or an agreement to return all company information upon departure. Evidence that an employee misappropriated trade secrets or otherwise improperly competed against the employer while still an employee might support tort claims for breach of

fiduciary duty or the duty of loyalty. If a former employee uses trade secrets or confidential information to take business from her former employer, the former employer might have a claim for tortious interference with contract or business relations, or common law unfair competition. Further, some states recognize a cause of action for conversion based on misappropriation of trade secrets.

Most versions of the UTSA, however, contain a provision stating that the statute preempts or supersedes conflicting tort or other claims based on misappropriation of a trade secret. *See* Uniform Trade Secrets Act §7(a). Preemption generally does not apply to contract-based causes of action whether or not based on misappropriation of a trade secret, or other civil remedies that are not based specifically on misappropriation of a trade secret. State laws and judicial decisions vary regarding the extent to which the USTA preempts other causes of action, so practitioners should analyze carefully the applicable law in their jurisdiction.

Federal and state criminal statutes might cover conduct that also constitutes trade secret misappropriation. The Federal Economic Espionage Act, 18 U.S.C. §1831 *et seq.*, makes trade secret misappropriation a federal crime. This statute reaches conduct outside the United States if (1) the offender is either a citizen or permanent resident alien of the United States or a United States corporation, or (2) the offender has committed an act in furtherance of the offense in the United States. Several states also have statutes that make stealing or otherwise misappropriating trade secrets a crime. *See, e.g.*, Cal. Penal Code §490; Ga. Code §16-8-13.

#### E. **Protecting Trade Secrets in Litigation**

Trade secret plaintiffs must take care to protect the confidentiality of their trade secrets during the litigation process. Although a complaint must contain sufficient allegations to state a plausible claim that the plaintiff's information constitutes a trade secret, the plaintiff is not required to disclose its trade secrets in the complaint. Highly confidential and trade secret information must be produced, however, by both sides during the discovery process. Parties commonly negotiate, and courts routinely enter, confidentiality and protective orders establishing requirements to protect and maintain the confidentiality of such information during the litigation. Such protective orders generally include restrictions on the categories of people to whom confidential information can be disclosed, as well as restrictions on how such information must be marked and maintained. In some cases, protective orders will provide that particularly confidential or sensitive information may be designated "attorneys' eyes only," so such information cannot be disclosed to business or technical employees of the opposing party who might use it even inadvertently.

Parties involved in trade secret litigation also should be careful about disclosures to expert witnesses. Expert witnesses often work in the same field as the parties to the lawsuit, and sometimes they are actual or potential competitors. Protective orders sometimes restrict the type of expert who can receive confidential or trade secret information. This topic should be the subject of negotiation between counsel for the parties early in a trade secret case.

## F. Possible Defenses

Defenses to a trade secret case generally start with challenging each of the elements of a cause of action under the applicable trade secrets statute or common law. The first line of defense is to try to show that the information or material at issue is not a secret. Things to look for here include:

- the extent to which the information is known outside of the plaintiff's business;
- whether the information can be obtained or recreated using publicly available sources;
- whether the product or process can be reversed engineered;
- the value of the information to the plaintiffs or to competitors;
- the ease or difficulty with which the information could be properly acquired or recreated by others.

In addition, defendants often challenge whether the plaintiff has taken reasonable efforts to maintain the secrecy of its claimed trade secret information or materials. Although the USTA does not require that a plaintiff use every available method to protect secrecy, courts will deny trade secret protection if a party has not taken steps that are reasonable under the circumstances. Ways to challenge the secrecy element include evidence showing that the plaintiff:

- failed to mark documents and materials as "confidential;"
- failed to obtain confidentiality and non-disclosure agreements with employees, contractors, or suppliers;
- failed to maintain appropriate access restrictions to physical facilities or computer networks;
- made information or materials accessible to people who do not have a legitimate "need to know;" or
- failed to track or retrieve confidential information or materials, including to retrieve information and devices from departing employees.

Equitable defenses also might apply to defeat a trade secrets claim. Proof that the plaintiff itself obtained the alleged trade secrets through improper means might prevent enforcement under an unclean hands theory. As with other injunctive relief claims, a delay in

seeking relief can defeat the plaintiff's entitlement to an injunction and can also be evidence that the claimed trade secret is not as valuable or important as the plaintiff might contend.

Independent development is perhaps the strongest defense to a trade secret misappropriation claim. Important factors to establish an independent development defense include the timing of the development (preferably before the defendant allegedly had access to the plaintiff's trade secrets), the sources used by the defendant for its development (preferably its own employees and information, or information available through public sources), or the lack of access to the plaintiff's trade secrets. The strongest cases of independent development exist where the defendant can show through its own documents and records that it made no use of the plaintiff's information and developed its own information or processes in a "clean room" kind of environment.

#### **IV. TRADE SECRETS REMEDIES**

A trade secret plaintiff has a wide array of remedies from which to choose. In most trade secret cases, circumstances will dictate asking for a temporary restraining order (TRO), preliminary injunction, and/or other prophylactic relief at the start of the case, in addition to whatever damages and permanent injunctive relief the plaintiff intends to seek at trial. In other cases, strategic and legal considerations may make a request for such early relief unnecessary or undesirable. Identifying the most appropriate remedies and choosing the best stages of the case in which to request them involve some of the most important — and most difficult — strategic and legal choices that a trade secret plaintiff will make.

##### **A. Interlocutory Relief**

Requests for emergency prejudgment relief often play a major role in trade secret cases. This is due to the nature of trade secrets: once a trade secret has been disclosed, its value can be lost forever. If a trade secret owner believes that its trade secret is being misappropriated, waiting for trial and counting on a final judgment to prevent or stop the misappropriation is rarely a viable option. Indeed, such a failure to act may moot or jeopardize the plaintiff's chance of securing permanent injunctive relief at trial. If left unchecked, the defendant's conduct during the months (or perhaps years) before trial could destroy the very thing that the plaintiff's suit is seeking to protect. Trade secret plaintiffs therefore often seek emergency injunctive relief prior to trial. The most common types of interlocutory injunctive relief are temporary restraining orders and preliminary injunctions. While both TROs and preliminary injunctions are emergency remedies intended to preserve the status quo pending trial, they are treated differently by the courts and require different preparation and presentations by counsel.

##### **1. Temporary Restraining Orders**

Generally speaking, a TRO is very short-term emergency relief. The purpose of a TRO usually is prevent irreparable harm from occurring before an evidentiary hearing (usually a

preliminary injunction hearing) can be held. Although formulations of the TRO standard can vary in minor ways, a plaintiff seeking a TRO can be expected to show that it has a right or interest in need of protection and will suffer irreparable harm if the TRO is not issued for which there is no adequate remedy at law. In determining whether to issue a TRO, some courts will consider the last uncontested status quo between the parties.

A request for a TRO usually is made by motion at or near the time that the complaint is filed (or otherwise when the threat of irreparable harm becomes known) and is supported by a recitation of the facts establishing the nature of the trade secret, the actual or threatened misappropriation, the harm that will befall the plaintiff if a TRO is not issued, and the irreparable nature of this harm. These facts should be attested to by someone having personal knowledge of them, either by having a witness verify the complaint and/or by submitting affidavits in support of the TRO motion.

Because TRO practice can vary dramatically from one judge to another, it is important to learn as quickly as possible which judge has been assigned to the case and how this judge approaches and resolves TRO motions. It is also important to learn how quickly the judge will be available for a TRO hearing. Judicial calendars are sometimes so full that a particular judge is not available for several days or even weeks. If a plaintiff cannot wait that long, counsel should investigate possible options, such as seeking a hearing before whatever judge might be available to hear emergencies.

A plaintiff seeking a TRO may have the option of doing so on an “ex parte” basis (*i.e.*, without notice to or participation by the opposing party). An ex parte TRO is more difficult to get than one obtained with notice, and it might also be less desirable, depending on the exigencies of the particular situation. Many judges resist hearing TRO motions ex parte and will urge the plaintiff to give notice to the defense so that both parties can be present and be heard. Moreover, there are special requirements – and limitations -- for ex parte TROs. However, a plaintiff will want to consider seeking an ex parte TRO if there is a reasonable likelihood that providing notice to the defendant would further endanger the information at issue or otherwise prompt the defendant to moot the relief sought.

A TRO generally is not a final and appealable order. However, if a TRO extends beyond the limitations provided in the relevant statute or regulation, a court might consider the TRO to be a preliminary injunction order (which is appealable) for purposes of appeal.

## 2. Preliminary Injunctions

The purpose of a preliminary injunction is to prevent irreparable harm pending a trial on the merits. The standard for obtaining a preliminary injunction is similar to that for seeking a temporary restraining order. In most courts, the movant generally must establish (1) some likelihood of success, (2) irreparable harm (3) for which there is no adequate remedy at law, and

(4) that is greater than the irreparable harm the defendant will suffer if the injunction is granted, and also show that (5) granting the requested relief serves the public interest more so than denial.

Unlike TROs, preliminary injunctions generally may not be granted *ex parte*, e.g., notice to the opposing party must be given. Fed.R.Civ.P. 65(a)(1). This is consistent with the fundamental difference in the nature of the two proceedings: while a TRO is short-term emergency relief usually granted without an evidentiary hearing, a preliminary injunction generally will last until trial and usually is granted only after an evidentiary proceeding that is often very much like a trial.

However, the same rule of thumb applies to preliminary injunctions as to TROs: know your judge. Some judges will prefer to decide a motion for preliminary injunction on the basis of written submissions and deposition testimony, forgoing a live hearing. The most common practice, however, is to hold a hearing at which live witness testimony and documentary evidence are presented for the court's consideration.

Depending on the particular jurisdiction's rules, an evidentiary hearing on a motion for preliminary injunction may be required if fact issues have been joined (*i.e.*, if a verified answer has been filed denying the material allegations of the complaint). Therefore, it might be prudent to file a verified answer prior to disposition of a preliminary injunction motion in order to secure the opportunity to present evidence in opposition to the motion.

If and when a preliminary injunction issues, the order must be in writing and must comply with the numerous and specific requirements for injunctive relief generally. The party seeking to enforce a preliminary injunction also must comply with the rules regarding service of the injunction on those to be bound.

### 3. Some Issues Relating to Interlocutory Injunctions

#### a. Presumption of irreparable harm

Meeting the requirements for emergency injunctive relief in trade secret cases may be easier than with other types of claims if a bona fide trade secret truly is in danger. There is support for the proposition that, when injunctive relief is requested pursuant to a statute that explicitly authorizes such relief, a plaintiff need not show irreparable harm or the inadequacy of legal relief, and some courts have applied that rule to trade secrets cases. *See, e.g., Lucini Italia Co. v. Grappolini*, No. 01 C 6405, 2003 WL 1989605 at \*18 (N.D.Ill. Apr. 28, 2003) (“[W]here a statute expressly authorizes injunctive relief, a plaintiff need only show defendant’s violation of the Act and that plaintiff has standing to pursue the cause. . . . The general rules of equity requiring a showing of irreparable injury and a lack of an adequate remedy at law need not be shown.”) citations omitted. *But see Bedrossian v. Northwestern Memorial Hospital*, 409 F.3d 840 (7th Cir. 2005) (when statutory injunctive relief is permissive rather than mandatory, plaintiff must show irreparable harm). Even without such a waiver of the traditional equitable requirements, however, the “irreparable harm” and “inadequate remedy at law” prongs of the

injunction standard usually can be met without difficulty in trade secret cases since many courts readily find such injury upon a showing that a trade secret is in danger of being taken or disclosed. *See, e.g., OptionMonster Holdings, Inc. v. Tavant Technologies, Inc.*, 2010 WL 2639809 (N.D.Ill. June 29, 2010); *Ultraviolet Devices, Inc. v. Kubitz*, 2009 WL 3824724 (N.D.Ill. Nov. 13, 2009); *IDS Life Insurance Co. v. SunAmerica, Inc.*, 958 F. Supp. 1258, 1281 (N.D.Ill. 1997) (and cases cited therein), *aff'd in part and vacated in part on other grounds*, 136 F.3d 537 (7th Cir. 1998)); *IDS Financial Services, Inc. v. Smithson*, 843 F. Supp. 415, 418 – 419 (N.D.Ill. 1994); *Prentice Medical Corp. v. Todd*, 145 Ill.App.3d 692, 495 N.E.2d 1044, 1051, 99 Ill.Dec. 309 (1st Dist. 1986) (irreparable harm flows from transgression of continuing nature, such as ongoing damage to goodwill or loss of competitive position).

b. The Problem of “Non-Use” Injunctions – The Inevitable Disclosure Doctrine

A common remedy granted to the successful trade secret plaintiff is an injunction prohibiting use and disclosure of the trade secrets at issue. All too often, this relief is not enough. Once the trade secrets have been taken and used and once a competitor has received the benefit of the trade secrets, prohibitions on further use simply miss the point.

Some courts have been willing to address this problem by issuing injunctions prohibiting competition, even in the absence of a noncompete covenant, when trade secret misappropriation has been shown. The rationale behind some of these decisions is that compliance with a nonuse injunction would be too hard to police, especially with respect to a defendant that has shown himself to be untrustworthy, and that the courts view the burden posed by a broadened injunction as appropriately borne by the wrongdoer. *See Additive Controls & Measurement Systems, Inc. v. Flowdata, Inc.*, 1994 WL 749595 at \*13 (S.D.Tex. July 11, 1994) (noting that injunction’s stringent provisions illustrate adage that “those caught violating the law must expect some fencing in”).

A similar result has been reached by courts applying the “inevitable disclosure” doctrine. The inevitable disclosure doctrine recognizes that trade secrets can exist in someone’s mind and memory and that there are circumstances in which those trade secrets inevitably will be used or disclosed — even if the defendant credibly vows to keep the information confidential. Courts applying the doctrine have differed over its reach and the circumstances required for its application, but generally speaking the doctrine applies when a defendant has had access to trade secrets and then defects to the trade secret owner’s competition to perform duties so similar that the court believes that these duties cannot be performed without making use of trade secrets relating to the previous affiliation. *See, e.g., PepsiCo, Inc. v. Redmond*, 54 F.3d 1262 (7th Cir.), *aff’g PepsiCo, Inc. v. Redmond*, No. 94 C 6838, 1995 U.S. Dist. LEXIS 19437 (N.D.Ill. Jan. 26, 1995).

Section 2(a) of the Uniform Trade Secrets Act addresses this concept and expressly provides relief from “threatened” disclosure of trade secrets. “Misappropriation” is defined by

the UTSA to include not only disclosure of trade secrets but also “use” of these trade secrets. Courts applying the inevitable disclosure doctrine sometimes cite to the UTSA’s prohibition of threatened use as support for the doctrine. *See Teradyne, Inc. v. Clear Communications Corp.*, 707 F. Supp. 353, 356 – 357 (N.D.Ill. 1989).

Although some jurisdictions have embraced the inevitable disclosure doctrine, others have flatly rejected it as improperly conjuring a noncompete obligation in situations where the parties did not bargain for one. *LeJeune v. Coin Acceptors, Inc.*, 381 Md. 288, 849 A.2d 451 (App. 2004); *Whyte v. Schlage Lock Co.*, 101 Cal. App. 4th 1443, 125 Cal.Rptr.2d 277 (2002); *Del Monte Fresh Produce Co. v. Dole Food Co.*, 148 F. Supp. 2d 1326, 1337 (S.D. Fla. 2001). Consequently, practitioners must evaluate carefully which state’s law is likely to apply to an inevitable disclosure dispute.

## B. Injunctive Relief – “Permanent” and Temporary

A successful trade secrets plaintiff may obtain injunctive relief prohibiting further misappropriation. The following are some of the issues that must be addressed when seeking, or responding to requests for, injunctive relief.

### 1. The Order Must Be Specific

Federal Rule of Civil Procedure 65(d) and most states’ codes of civil procedure that an injunction specify the conduct to be restrained. Therefore, if the court is disposed to enter an injunction (whether a temporary restraining order, a preliminary injunction, or a posttrial injunction), it must enter a written order, and this order must clearly and specifically describe what conduct is either required or prohibited. Rule 65(d)’s specificity requirement extends to an injunction’s description of the off-limits trade secrets. *Patriot Homes, Inc. v. Forest River Housing, Inc.*, 512 F.3d 412 (7th Cir. 2008). However, there is an inherent tension between including sufficient detail to satisfy the procedural rules requiring specificity and not disclosing so much detail that the trade secret is revealed. Plaintiffs therefore often find it difficult to draft the operative language of a restraining order in a way that both satisfies the rules and protects the information at issue. *See, e.g., PepsiCo, Inc. v. Redmond*, 46 F.3d 29, 31 (7th Cir. 1995) (to avoid disclosure of trade secrets in litigation, district court should draft its opinion to refer to trade secrets indirectly, without disclosing these secrets, in order to avoid having to place entire opinion under seal). One possible approach is to draft an injunction that refers, very specifically, to *the type* of information at issue without actually disclosing the details of the information itself. For example, an injunction might describe trade secrets in the following ways:

- The manufacturing process and equipment used by plaintiff ACME to create a smooth cutting edge on the leading blade of its Model A widget; or
- ACME’s 2002 and 2003 sales forecasts for its Elixir<sup>®</sup> brand fruit beverage product and its 2002 and 2003 actual sales results for that product.

This type of description likely would be specific enough to satisfy the applicable rules without actually disclosing the secret at issue.

## 2. Who Is Bound By An Injunction?

One of the most important aspects of obtaining effective injunctive relief is making sure that the injunction is binding on all of the parties who might be in a position to disclose, use without authorization, or otherwise impair the plaintiff's trade secret. Service of the injunction order is the key to enforcement. Most jurisdictions' procedural rules provide that injunctions (including temporary restraining orders and preliminary injunctions) are "binding only upon the parties to the action, their officers, agents, employees, and attorneys, and upon those persons in active concert or participation with them who receive actual notice of the order by personal service or otherwise." Fed.R.Civ.P. 65(d) contains a similar provision.

Therefore it is usually not necessary to name as a defendant every person or entity who has participated in the misappropriation. Indeed, strategic considerations often cause a plaintiff to consider not suing all possible defendants. In such cases, these other persons and entities "in active concert or participation" with the defendants will be bound by the injunction as long as they have actual notice of it. While the rules do not require personal service in order for someone to have "actual notice" of the injunction, it is the surest way to ensure and prove notice, and personal service should be effected whenever possible on those who have participated or who might participate in the conduct of the defendants.

## 3. Duration of Injunctive Relief

One of the common methods of determining the duration of an injunction was to measure the time in which the defendant could have developed the trade secret legitimately and independently. *See e.g., Syntex Ophthalmics, Inc. v. Novicky*, 745 F.2d 1423, 1435 (Fed. Cir. 1984) (and cases cited therein at n.23), *vacated on other grounds*, 105 S.Ct. 1740 (1985). However, this method has an obvious flaw since it assumes that the trade secret could have and would have been developed independently. In fact, a trade secret might elude development and last forever. The Uniform Act requires that injunctions must terminate when the information ceases to be a trade secret, with the addition of extra time to compensate for a wrongfully gained commercial advantage. Uniform Trade Secrets Act with 1985 Amendments §2(a), 14 U.L.A. 433, 449 (1985). This concept of a "head start" is discussed in *Sokol Crystal Products, Inc. v. DSC Communications Corp.*, 15 F.3d 1427 (7th Cir. 1994).

## 4. Bond

TROs and preliminary injunctions are often contingent on the posting of a bond. In a federal case, Fed.R.Civ.P. 65(c) makes the posting of a bond mandatory. While left to the court's discretion under some states' procedural rules, a bond usually is required in state court as well. A plaintiff seeking interlocutory injunctive relief therefore should make the necessary arrangements

for a bond in advance of the hearing (e.g., through its insurance company or through a bonding agency). When days (or even hours) are of critical importance, a plaintiff who has successfully obtained a TRO or a preliminary injunction will not want to delay the enforcement of the order while making the necessary arrangements to post a bond.

Each party should be prepared to address at the injunction hearing the bond amount that it believes is most appropriate. The purpose of a bond is to guaranty the availability of funds with which to compensate the defendant if the interlocutory injunction turns out to have been improvidently granted. In determining the amount of the bond, courts generally consider the costs and other damages that a defendant can be expected to incur as a result of complying with the injunction. It is important for defendants to obtain the highest bond that the situation will support. Damages for an improvidently granted injunction are generally limited to the amount of the bond. *See Mead Johnson & Co. v. Abbott Laboratories*, 209 F.3d 1032, 1033 (7th Cir. 2000) (“compensation for harm caused by the injunction cannot exceed the amount of the bond”).

### C. Damages and Unjust Enrichment

Section 3 of the UTSA provides plaintiffs with several possible measures of compensatory damages. Specifically, a plaintiff can recover both its actual loss caused by the misappropriation and the unjust enrichment gained by the defendant to the extent that this unjust enrichment is not taken into account in computing actual loss. Some state statutes authorize the court to award “a reasonable royalty” as payment for the defendant’s “unauthorized disclosure or use of a trade secret.” 765 ILCS 1065/4(a).

#### 1. Plaintiff’s Actual Loss

There are many ways in which a trade secret plaintiff might be harmed by the unauthorized use or disclosure of its trade secret, and, therefore, there are many ways for such a plaintiff to show its “actual loss.” As one trade secret opinion has explained, “[E]very case requires a flexible and imaginative approach to the problem of damages [and] the cases reveal that most courts adjust the measure of damages to accord with the commercial setting of the injury, the likely future consequences of the misappropriation, and the nature and extent of the use the defendant put the trade secret to after misappropriation.” *University Computing Co. v. Lykes-Youngstown Corp.*, 504 F.2d 518, 538, *reh’g denied*, 505 F.2d 1304 (5th Cir. 1974). As noted by the drafters of the Restatement (Third) of Unfair Competition, “The general rules relating to the recovery of compensatory damages in tort actions apply in actions for the appropriation of trade secrets.” Restatement (Third) of Unfair Competition §45, cmt. a (1995). *See also* Restatement (Second) of Torts §§902 – 903 (1979) (defining “damages” and “compensatory damages” for tort claims in general).

A trade secret plaintiff often is damaged through the loss of profits that the plaintiff would have earned but for the misappropriation. These lost profits usually take the form of the profits on sales that the plaintiff would have made but for the misappropriation. *See Roton*

*Barrier, Inc. v. Stanley Works*, 79 F.3d 1112 (Fed. Cir. 1996). A plaintiff proving actual loss might also seek damages based on “price erosion,” or the amount that the plaintiff was compelled to reduce its prices as a result of the misappropriation, as well as for loss of market share. See *Roton Barrier, supra*, 79 F.3d at 1120; *Mangren Research & Development Corp. v. National Chemical Co.*, 87 F.3d 937 (7th Cir. 1996); Restatement (Third) of Unfair Competition §45, cmt. e. Another measure of actual loss might be based on the plaintiff’s lost sales caused by the defendant’s distribution of defective products that incorporate the trade secrets. See *Micro Data Base Systems, Inc. v. Dharma Systems, Inc.*, 148 F.3d 649 (7th Cir. 1998).

Finally, if the trade secret has been “lost,” that is, if its secrecy has been destroyed, the plaintiff may be entitled to receive compensation for the loss of the secret itself. Some courts have measured this by adding up the plaintiff’s investment in the trade secret. *Smith v. Dravo Corp.*, 208 F.2d 388, 392 – 393 (7th Cir. 1953) (measuring damages by amount of plaintiff’s capital investment in trade secret).

The trade secret plaintiff bears the burden of proving its loss, including the amount of the loss and the cause of the loss. However, a trade secret plaintiff need not pinpoint the exact amount of damages with absolute certainty. Rather, the plaintiff generally “is required to prove the amount of such loss with only as much certainty as is reasonable under the circumstances.” Restatement (Third) of Unfair Competition §45, cmt. b. See also Restatement (Second) of Torts §912 (discussing requirement of “certainty” in calculating damages). This flexibility accorded to a trade secret plaintiff is grounded in the notion that a wrongdoer should not benefit from the plaintiff’s inability to prove the precise amount of damages. However, while damages need not be proven with “mathematical precision,” they “cannot be based upon conjecture or sheer speculation,” and it is “necessary that the evidence afford a reasonable basis for the computation of damages.” *Midland Hotel Corp. v. Reuben H. Donnelley Corp.*, 118 Ill.2d 306, 515 N.E.2d 61, 66, 113 Ill. Dec. 252 (1987).

## 2. Defendant’s Unjust Enrichment

A trade secret plaintiff also may recover the profits earned by the defendant as a result of its misappropriation of the trade secret, *i.e.*, the defendant’s “unjust enrichment.” Under the Uniform Trade Secrets Act, a plaintiff is entitled to recover both its own actual loss and the defendant’s unjust enrichment to the extent that the defendant’s gain is not taken into account when calculating actual loss. Uniform Trade Secrets Act with 1985 Amendments §3, 14 U.L.A. 433, 455 (1985). This rationale for recovery is based on the premise that a wrongdoer should not derive a benefit from its wrongdoing.

“Unjust enrichment” measures exactly that — the amount by which a defendant has been unjustly enriched. The appropriate amount of unjust enrichment damages is the amount by which the defendant actually benefited. See, *e.g.*, *Creative Demos, Inc. v. Wal-Mart Stores, Inc.*, 142 F.3d 367, 371 – 373 (7th Cir. 1998) (vacating and remanding unjust enrichment damages award because not based on actual benefit received by defendant). Consequently, a successful plaintiff

may be entitled to recover only the net profits derived by the defendant from the misappropriation, not all revenues obtained by the wrongdoer. *See* Restatement (Third) of Unfair Competition §45, cmt. f (1995). Most courts, however, require the plaintiff to prove only the defendant's gross sales, while the defendant must establish the amount of costs and expenses to be deducted from the gross sales numbers in order to reach net profits. *Id.*

When calculating the plaintiff's damages based on the defendant's unjust enrichment, the damages must be based on the defendant's actual financial performance, not on projected profits. The Federal Circuit has reversed a trial court decision allowing the plaintiff in a trade secret case to base its claim for unjust enrichment on the projected profits anticipated in an early business plan authored by the defendant rather than on evidence of what the defendant actually gained. *See Litton Systems, Inc. v. Ssangyong Cement Industrial Co.*, 107 F.3d 30 (Fed. Cir. 1997) (text available in Westlaw). The *Litton Systems* court explained, "The district court's theory of unjust enrichment as encompassing *unrealized expected gain* . . . is unsupported in the law of unfair competition and cannot serve as a valid basis for an award of damages." (emphasis added 1997 WL 59360 at \*8.)

Another possible measure of the defendant's unjust enrichment could be the savings that it achieved as a result of the misappropriation. *See Web Communications Group, Inc. v. Gateway 2000, Inc.*, 1995 WL 23535 at \*2 (N.D.Ill. Jan. 17, 1995).

#### D. **Exemplary / Punitive Damages and Attorneys' Fees**

Section 3(b) of the UTSA also provides for "exemplary damages" if "willful and malicious" misappropriation is found. The case law in the various jurisdictions interpreting this provision is not uniform. For example, the Seventh Circuit ruled in *Mangren Research & Development Corp. v. National Chemical Co.*, 87 F.3d 937 (7th Cir. 1996), that exemplary damages are limited to cases in which the act of misappropriation (*i.e.*, the use or the disclosure of trade secrets) was intentional and was committed with conscious disregard of the rights of another. *See also RKI, Inc. v. Grimes*, 200 F. Supp. 2d 916 (N.D.Ill. 2002). At least one decision issued from the Northern District of Illinois has applied a more relaxed standard, holding that a defendant's liability for exemplary damages is controlled by what the defendant "should have known." *Chemetall GmbH v. ZR Energy, Inc.*, 2001 WL 1104604 at \*\*9 – 10 (N.D.Ill. Sept. 18, 2001). At the other end of the spectrum is the Federal Circuit's decision in *Roton Barrier, Inc. v. Stanley Works*, 79 F.3d 1112 (Fed. Cir. 1996), which interpreted the ITSA to say that misappropriation motivated by malice justified an award of punitive damages while misappropriation motivated by competition did not.

The statute makes two things clear, however. First, it limits exemplary damages to not more than twice the amount of compensatory and restitutionary damages. Second, it states that "the court *may* award exemplary damages," indicating both that these damages are discretionary and that the decision to award them is made by the judge, not a jury.

The Uniform Act also specifically authorizes (but does not require) the court to award attorneys' fees to the prevailing party in a trade secret action "[i]f (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 (1985). Under this standard, a plaintiff's entitlement to attorneys' fees appears to be similar to that required to obtain exemplary damages. *See RKL, Inc. v. Grimes*, 200 F. Supp. 2d 916, 928 (N.D.Ill. 2002) ("malicious and willful" conduct merits award of fees). *See also* 4 Roger M. Milgrim, *Milgrim on Trade Secrets* §15.02[3][k], p. 15-214 n.162 (2004), citing cases in which courts awarded attorneys' fees under the UTSA and other state law theories.