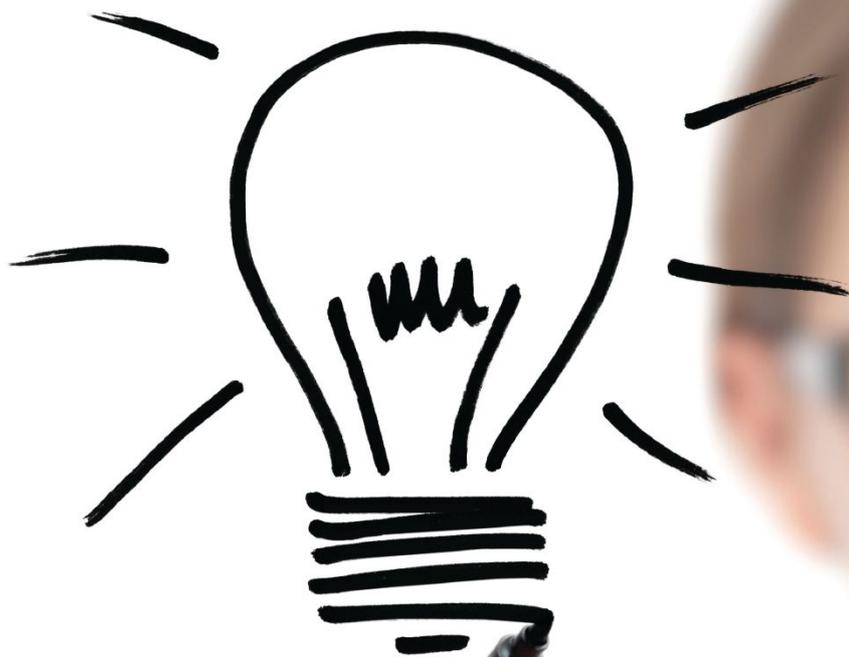


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# What's the Big Idea? The New N.J. Trade Secrets Act

By Richard L. Ravin

Effective Jan. 5, Gov. Christie signed into law *A-921*, the New Jersey Trade Secrets Act (NJTSA), codified as N.J.S.A. 56:15-1 et seq. The act is modeled after the Uniform Trade Secrets Act (UTSA). Only New York, Texas and Massachusetts have not adopted a version of the uniform law, although Massachusetts has a bill pending. The NJTSA supercedes any conflicting New Jersey common-law tort actions

## Trade Secret

The new act defines a “trade secret” as “information held by one or more people, without regard to form... [that] [d]erives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, others persons who can obtain economic value from its disclosure or use...” Examples of forms given in the act are: a formula, pattern, business data compilation, program, device, method, technique, design, diagram, drawing, invention, plan, procedure, prototype or process.

Further, the trade secrets must be the “subject of efforts that are reasonable under the circumstances to maintain its secrecy.” Thus, sending unencrypted or nonpassword protected documents containing trade secrets via e-mail

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could be used as evidence to defeat the secrecy element. On the other hand, absolute secrecy is not required, and presumably, the hacking of computer servers containing trade secrets, despite the employment of reasonable security measures, would not necessarily be



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fatal to proving reasonable secrecy efforts.

To maintain the secrecy element, the trade secret must be communicated to others under a duty of secrecy. Such an obligation could be created by the receiving party simply agreeing (not necessarily in writing) to keeping the information confidential, or may arise as a result of a relationship, such as employer-employee, if the receiving person has reason to know the information is a trade secret. In this regard, stamping documents as “trade secret” or “confidential” etc., puts the recipi-

ent on notice that the documents contain proprietary information, and shows that the owners took precautions to maintain secrecy.

## Ideas and Negative Information

Prior to the act, New Jersey case law had required that the information be in actual use by the business to be protectable. This limitation mirrored the *Restatement*, which required that the information be continuously used in one's business to be protected. Comment b, *Restatement (First) of Torts*, § 757 (1939). The NJTSA, how-

ever, follows the UTSA in expanding the scope of a trade secret to include information of “actual or potential” economic value.

Thus, under the act, an idea or information not yet in use is protectable, if it derives actual or potential economic value from not being generally known, and not readily ascertainable by proper means (by those who could derive economic value from its disclosure or use), and which is the subject of reasonable efforts to maintain secrecy. So-called “negative information” — knowledge about what

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# What's the Big Idea? The New N.J. Trade Secrets Act

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formulas or processes do not work — would also be protectable.

## Misappropriation

In contrast to New Jersey common law, the definition of “misappropriation” under the NJTSA, in addition to use and disclosure, includes the mere “acquisition” of a trade secret by one who has reason to know that it was acquired by improper means. “Improper means” includes, (i) theft, bribery misrepresentation, breach or inducement to breach an express or

er means. The NJTSA expressly prohibits the defense “that proper means to acquire the trade secret existed at the time of the misappropriation.” This defense is in tension with the act’s definition of “trade secrets,” which states that a trade secret shall not be “readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use.” While the prohibition may prevent the defendant from proving that it could have discovered the trade secret through proper means, it would not prevent proof that the

means is established by the less-burdensome objective standard. Liability for unintentional conduct may trigger insurance coverage under some policies.

## Reasonable Royalty Alternative to Proscriptive Injunction

The NJTSA differs from the common law as to the scope of remedies available. The act provides that in “exceptional circumstances,” an injunction may condition future use of the trade secret on payment of a “reasonable royalty.” Exceptional circumstances include, without limitation, “a material and prejudicial change of position prior to acquiring knowledge or reason to know of misappropriation that renders a prohibitive injunction inequitable.” This provision contemplates a situation where a defendant made a significant investment in developing a product prior to learning that it was the result of the misappropriation of a trade secret belonging to another.

## Reasonable Royalty as a Measure of Damages

The NJTSA allows a reasonable royalty to be used as a measure of compensation for the defendant’s past use of the trade secret, in lieu of other damages, such as the plaintiff’s lost profits or the defendant’s unjust enrichment. Reasonable royalties can be difficult to determine, however, and can be the source of substantial discovery and litigation (such as in patent and copyright infringement cases). Evidence of prior licensing of the subject technology by either party may be relevant, but often such royalties are part of a complex licensing arrangement involving other terms, covenants and conditions that may make it difficult to quantify the royalty component for the subject technology. The concept of reasonable royalty becomes particularly problematic when the misappropriator is a competitor, to whom the plaintiff would never have licensed the technology in the first place.

## Attorney Fees and Punitive Damages

The act provides for attorney

## As a result of the act's expansion of liability for misappropriation of trade secrets in New Jersey, greater due diligence is indicated.

implied duty to keep secret or limit the use or disclosure, (ii) espionage through electronic or other means, (iii) access that is unauthorized or exceeds the scope of authorization, or (iv) other violation of state law.

As with New Jersey common law, it is a defense to misappropriation under the NJTSA if the trade secret was discovered by proper means. The act defines “proper means” as discovery by independent invention; reverse engineering; use under a license by the owner or any public use, display or publication of the trade secret; or any other means that are not improper.

However, in a significant departure from both the New Jersey common law and the UTSA, the act disallows the defense that the defendant *could have* discovered the trade secret through proper

information was readily ascertainable by proper means by others who can obtain economic value from its disclosure or use, and thereby disproving the existence of a trade secret in the first place.

## No Intent Required

Under the NJTSA, any misrepresentation, not only intentional or negligent, made by the receiving party in connection with the acquisition of the trade secret is considered acquisition by “improper means.” Thus learning of a trade secret as a result of an innocent misrepresentation would be actionable in and of itself.

The act includes liability for one who “knows or *has reason to know*” that the trade secret was misappropriated. Whereas actual knowledge is a subjective standard, “reason to know” that the trade secret was acquired by improper

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fees and costs, including expert witness fees if the misappropriation is willful and malicious, the claim for misappropriation is brought in bad faith, or a motion to terminate an injunction is made or resisted in bad faith. The common law provided no fee-shifting provision.

The act also provides that "punitive damages" may be awarded up to twice the amount of damages awarded (for actual damages and for unjust enrichment). Arguably, the Punitive Damage Act is applicable. (N.J.S.A. 2A:15-5.9 et seq.).

#### Confidentiality Agreements

With enactment of the NJTSA, attorneys should re-examine both the drafting of confidentiality agreements and the advice given to clients who regularly receive confidential information from third parties while entering into such agreements. A simple oral agreement by the receiving party to keep the information confidential may be all that is needed to give rise to a cause of action if that information is disclosed or used by the receiving party. Thus, a written agreement may be advisable for each of the parties, albeit for different reasons.

For the disclosing party, an obligation of secrecy from the receiving party is important to maintain the trade-secret status of the information. The disclosing party may also want to state in the agreement that it reserves all its rights and remedies under the NJTSA. On the other hand, the receiving party may seek to expressly limit the rights and remedies of the parties to those included in the agreement in lieu of those provided in the NJTSA. In negotiating such agreements, counsel should consider whether, and to what extent, a party can avoid liability imposed by statute for intentional misconduct. In any event, it seems the parties could agree to no NJTSA liability for innocent or negligent misrepresentations in connection with acquiring the trade secret.

When drafting confidential-

ity agreements, especially in the context of an employee-employer relationship, it is critical that the sweep of the definition of the information being protected is not so broad as to be adjudged unenforceable as an unreasonable restraint on competition. Such is the case if a confidentiality agreement seeks to protect against disclosure or use of any information related to the plaintiff's business, irrespective of whether the information would be deemed confidential, material or important, and without any restriction as to duration, scope or geographic area, thereby depriving a former employee the ability to work in his chosen profession. *Grow Co. v. Chokshi*, 2012 WL 715978 (N.J. App. Div. March 7, 2012).

As a result of the act's expansion of liability for misappropriation of trade secrets in New Jersey, greater due diligence is indicated in connection with

the acquisition of companies or their assets, comprising significant trade secrets or technology, when meeting with prospective business partners to discuss trade secrets and when hiring employees. Non-use and nondisclosure agreements may need to be re-evaluated and tailored to accommodate a client's particular situation in light of the NJTSA. Similarly, confidentiality provisions contained within agreements of all kinds should likewise be reconsidered. Counsel should consider whether the definition of "confidential information" should include or be limited to "trade secret" as defined in the act, and whether any of the rights or remedies available in the act should be waived or reserved. Finally, choice of law and forum selection clauses (e.g. New York's common law as opposed to New Jersey's NJTSA) may have important consequences. ■

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