SUBJECT: Adoption of the Uniform Trade Secrets Act

COMMITTEE: Technology — committee substitute recommended

VOTE: 4 ayes — Elkins, Button, Fallon, Gonzales

0 nays

1 absent — Reynolds

WITNESSES: For — Joseph Cleveland, Greg Porter

Against — None

BACKGROUND: The Uniform Trade Secrets Act (UTSA) was promulgated in 1979 and amended in 1985 by the Uniform Law Commissioners, a national group of law professors and lawyers. It aimed to codify the existing common law on misappropriation of trade secrets by providing key definitions and remedies. States are not required to pass the act exactly as it is, and there is some variation from state to state. Texas has not adopted the UTSA.

Civil Practice and Remedies Code, ch. 134, the Texas Theft Liability Act (TTLA), provides civil remedies for unlawfully appropriating property, including theft of trade secrets as defined in Penal Code, sec. 31.05.

DIGEST: CSHB 1894 would create the Texas Uniform Trade Secrets Act, based on the model UTSA, with some adjustments. It would define terms, provide for injunctive relief, damages, and attorney's fees, and establish a presumption in favor of protective orders to preserve the secrecy of trade secrets.

Definitions. The bill would define several terms relating to trade secret misappropriation.

"Trade secret" would mean information, including a formula, pattern, compilation, program, device, method, technique, process, financial data, or list of actual or potential customers or suppliers that:

- derived independent economic value from not being generally

known to and not being readily ascertainable by proper means by others who could obtain economic value from its disclosure or use, and

- was the subject of reasonable efforts under the circumstances to maintain its secrecy.

"Proper means" would mean discovery by independent development, reverse engineering unless prohibited, or other means that were not improper. "Reverse engineering" would mean the process of studying, analyzing, or disassembling a product or device to discover its design, structure, construction, or source code if the product or device were acquired lawfully.

"Misappropriation" would mean acquisition, disclosure, or use of a trade secret that was acquired by improper means or disclosure or use of a trade secret of another without consent by a person who knew or had reason to know that their knowledge of the trade secret was:

- derived from a person who had used improper means to acquire it;
- 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 maintain its secrecy or limit its use.

It would include disclosure or use without consent by a person who, before a material change of the person's position, knew or had reason to know it was a trade secret and that knowledge of it had been acquired by accident or mistake.

"Improper means" would include theft, bribery, misrepresentation, breach or inducement of a breach of a duty to maintain secrecy, limit use, or prohibit discovery of a trade secret, or espionage.

Injunctive relief. Injunctive relief for actual or threatened misappropriation would be available under the bill. The injunction would be terminated when the trade secret ceased to exist but could be continued for an additional reasonable period of time in order to eliminate a commercial advantage. In exceptional circumstances, an injunction could condition future use upon payment of a reasonable royalty for no longer than the time for which the use could have been prohibited.

Damages. Under CSHB 1894, a claimant could recover damages in addition to or in lieu of injunctive relief. Damages could include actual loss caused by misappropriation of trade secrets and unjust enrichment not taken into account in actual loss. In lieu of damages measured by other methods, damages could be measured by calculating a reasonable royalty for unauthorized disclosure of a trade secret. If willful and malicious misappropriation were proven by clear and convincing evidence, exemplary damages not exceeding twice the initial award of damages would be available.

Attorney's fees. Payment of attorney's fees would be available to a prevailing party under the bill if a claim were made in bad faith, if a motion to terminate an injunction were made or resisted in bad faith, or if the misappropriation were found to be willful and malicious.

Preservation of secrecy. The bill would create a presumption in favor of granting protective orders to preserve the secrecy of trade secrets. Courts would be required to preserve alleged trade secrets by reasonable means. Protective orders could include provisions sealing records, holding in-camera hearings, limiting access to confidential information to only the attorneys and experts, and issuing orders preventing disclosure.

Effect on other law. CSHB 1894 would displace conflicting existing law providing civil remedies for misappropriation of trade secrets. It would control in conflicts with the rules of civil procedure but would not affect existing contractual or criminal remedies.

The bill would remove the Penal Code provision on theft of trade secrets from the definition of "theft" under the Texas Theft Liability Act.

CSHB 1894 would not affect disclosure of information by a governmental body under the Public Information Act.

The bill would take effect September 1, 2013, and would apply only to misappropriation of a trade secret made on or after that date.

SUPPORTERS SAY:

CSHB 1894 would harmonize and update the practice of trade secret misappropriation cases in Texas. Texas is one of only four states that have not adopted the UTSA, and adopting it would put the state in step with virtually every other jurisdiction throughout the country. Texas currently follows the First Restatement of Torts published in 1939 and common law

in this area. This means that Texas practice is decades behind current law in an area that is heavily affected by technological advancements. Texas needs to adopt the UTSA to bring trade secrets practice into the 21st century and in line with the rest of the nation. CSHB 1894 would not undermine common law. Instead, the existing common law, to the extent that it is not inconsistent, would serve to inform the meaning of the statute.

CSHB 1894 would strengthen the economy by attracting businesses to Texas and would benefit businesses already operating in Texas that rely on trade secret protection for their innovation. The fact that Texas is one of the last remaining states without the UTSA in place is a disincentive for businesses with trade secrets to do business in the state. Protection provided by current law is unclear and difficult to understand. By creating a presumption in favor of protective orders to protect the secrecy of alleged trade secrets, CSHB 1894 would ensure that the protection afforded to business was not only clear but strong. Adoption of the UTSA would provide consistent and predictable laws for trade secret protection and make it clear to businesses that Texas law would protect their interests if their trade secrets were misappropriated.

With the adoption of the UTSA, Texas lawyers would have an easier time practicing trade secrets law. The UTSA would clarify and combine the prevailing law in one section of code and eliminate uncertainties and inconsistencies, such as the definition of a trade secret and the elements of misappropriation. It also would clarify that certain legitimate business activities, such as reverse engineering, would not constitute misappropriation of trade secrets. Courts still would address the specific facts and situations presented by each case. Adoption of CSHB 1894 and the certainty provided by a specific definition of trade secrets would make it more likely that different courts presented with the same facts and situations would reach similar results.

Effect on courts and award of attorney's fees. CSHB 1894 would ease the burden on courts by providing more certainty to both potential plaintiffs and defendants. It would allow speedier resolution of cases and prevent lawsuits with no basis under the UTSA from being filed. It would provide disincentives for those making claims in bad faith and would not encourage unnecessary litigation. The provisions in the bill would make it easier to litigate legitimate claims of misappropriation by making the outcomes more predictable and consistent, without encouraging bad faith or unneeded litigiousness. The availability of attorney's fees when a claim

was made in bad faith would decrease the number of claims made without sufficient merit.

CSHB 1894 would decrease the cost for a business to litigate a trade secret case by providing simpler standards for relief, while offering an avenue for recovering attorney's fees against willful and malicious actors and eliminating excessive non-economic damages. Currently, bringing a separate action through the TTLA is one of the only ways to recover attorney's fees in a trade secrets misappropriation case, and trade secrets cases often involve attorney's fees in the six-figure range. Allowing for recovery of attorney's fees without requiring separate causes of action under other areas of law would help protect those who brought legitimate claims from having to pay these fees to protect secrets from someone else's malicious actions.

Customer lists. The inclusion of customer lists in the bill's definition of trade secret would not lead to more litigation or cause problems for executives changing employers. The UTSA's definition of trade secret requires that the information not be readily ascertainable by proper means. Thus, to the extent a compilation of customer identities could be easily ascertained through publicly available means, the compilation would not be a trade secret and would not be subject to litigation.

Prevailing parties. It is not necessary to define "prevailing party" in the bill. A court could look to Texas common law and the common law of the other 46 states that have adopted the UTSA in determining who was a prevailing party for purposes of recovering attorney's fees.

OPPONENTS SAY:

CSHB 1894 would change the way trade secret misappropriation was litigated in Texas. Currently, trade secret litigation is argued on a case-by-case basis, allowing for courts to address the specific facts and situations presented by each case. Adoption of the UTSA would displace and undermine existing common law by which this area is governed.

Effect on courts and award of attorney's fees. CSHB 1894 would make companies more likely to pursue trade secret litigation. It would expand the amount of material protected as trade secrets, allow courts to protect alleged trade secrets in a case, and provide for recovery of attorney's fees. Current law discourages businesses from clogging the courts with unnecessary lawsuits, and lowering these standards could increase the amount of trade secret litigation that came before Texas courts.

Customer lists. The bill's inclusion of customer lists in the definition of trade secrets would change the way the law is practiced in Texas and nationally. Both Texas common law and the model UTSA require an intensive inquiry to determine whether specific customer lists are worthy of trade secret protection. In the modern age, customer identities are often easily ascertained through publicly available means such as Google or LinkedIn. Explicitly including these lists in the definition of trade secret could cause problems for executives or others who changed employers and might want to use knowledge of their previous employers' customers in some fashion. CSHB 1894 would open these executives up to trade secret litigation for using information that might actually be easily ascertainable.

Prevailing parties. The term "prevailing party" is used in reference to recovery of attorney's fees but is not defined in the bill. Under the TTLA, parties obtaining injunctions but not damages are unable to recover attorney's fees. It is unclear how these parties would be treated under the UTSA.

NOTES:

CSHB 1894 differs from HB 1894 as filed in that the committee substitute would require that willful and malicious misappropriation be proven by clear and convincing evidence and specify that the act did not affect disclosure by a governmental body under the Public Information Act.

The companion bill, SB 953 by Carona, was passed by the Senate and reported favorably by the House Committee on Technology on April 18.