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Trade Secrets Alert

Congress Passes the Defend Trade Secrets Act

By Christopher Cox, Bambo Obaro, An Tran

On April 27, 2016, the U.S. House of Representatives voted 410-2 to pass the Defend Trade Secrets Act ("DTSA"). The House adopted the Senate version of the Bill, which was passed on April 4, 2016 in an 87-0 vote. President Obama has offered strong support for this legislation, which is certain to become law. The DTSA, which would allow companies for the first time to file civil lawsuits for trade secrets theft under the federal Economic Espionage Act, represents a sea change in trade secret law, which has been governed historically through a patchwork of civil state laws. Trade secrets represent the last category of intellectual property (joining patents, copyrights, and trademarks) to come under civil federal protection.

A Paradigm Shift In Trade Secret Litigation

The DTSA changes how trade secrets cases will be litigated. Historically, civil actions aimed at preventing or redressing actual or threatened trade secret misappropriation were governed by state common law. The Uniform Trade Secrets Act (the "UTSA"), published by the Uniform Law Commission in 1979 and amended in 1985, was promulgated to provide a legal framework to foster uniformity among state trade secret laws, codifying "the basic principles of common law trade secret protection." UTSA with 1985 Amendments, Prefatory Note 1 (Unif. Law Comm'n 1985). As of today, 48 of 50 states have adopted some variation of the UTSA, but significant substantive and procedural differences often exist among the specific trade secret statutes enacted in these states.

Given the lack of uniformity in state law, litigating trade secret cases in different jurisdictions often proves cumbersome, costly, and ineffective. Federal courts sitting in diversity are required to apply the state trade secret statutes of their local jurisdictions, often navigating quasi-procedural protections that potentially conflict with federal procedure. The result is a lack of uniformity in federal and state jurisprudence and a lack of predictability for companies engaged in interstate commerce. The DTSA seeks to provide the uniformity intended by, but ultimately not achieved through, the UTSA.

Similarities To The UTSA

In furtherance of its stated goal of "harmonizing" the national patchwork of trade secret protection laws, the DTSA defines the terms "trade secret" and

"misappropriation" as those terms are typically defined in the UTSA. Like the UTSA, the DTSA defines trade secrets as information that derives independent economic value from not being generally known and which the owner has taken reasonable measures to keep secret. Misappropriation is defined as: (1) the 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 use; or (2) the disclosure or use of a trade secret of another by a person who used improper means to acquire knowledge of the trade secret or at the time of disclosure or use knew or had reason to know that the knowledge of the trade secret was acquired by improper means. DTSA (S. 1890, 114th Cong.), § 2(b) (2015-2016).

The DTSA, like the UTSA, expressly permits aggrieved trade secret owners to obtain an injunction to prevent actual or threatened misappropriation and damages for any misappropriation—measured either by actual loss, unjust enrichment, and/or a reasonable royalty for the use of the stolen trade secret. The DTSA also provides for a potential award of exemplary damages, not more than two times compensatory damages, if the misappropriation is found to be "willful" and "malicious." DTSA (S. 1890, 114th Cong.), § 2(a) (2015-2016).

While the UTSA expressly states that it displaces conflicting tort, restitutionary, and other state law civil remedies for misappropriation of a trade secret, the DTSA expressly provides that it does not "preempt any other provision of law." DTSA (S. 1890, 114th Cong.), § 2(f) (2015-2016). Because it is not preempted, state statutory and common trade secret law will continue to exist side-by-side with the DTSA.

The Seizure Provision

Although the DTSA borrows heavily from the UTSA, it includes provisions that represent a significant departure from established state trade secret law. The most significant new provision allows a plaintiff to request, through an ex parte proceeding, seizure of any property "necessary to prevent the propagation or dissemination of the trade secret that is subject to the action." The seizure provision may be used "only in extraordinary" circumstances, and any seizure order must be narrowly tailored to avoid interrupting the legitimate business operations of the accused misappropriator, and only when other forms of equitable relief are inadequate. DTSA (S. 1890, 114th Cong.), § 2(a) (2015-2016). The DTSA also provides that the court shall take appropriate measures to protect the confidentiality of seized materials that are unrelated to the trade secret information ordered seized unless the person against whom the order is entered consents to disclosure of the material.

Due to the potential draconian effect of a seizure, the burden for obtaining a seizure under the DTSA is high. The plaintiff must first show that "the harm to the applicant of denying the application outweighs the harm to the legitimate interests of the person against whom seizure would be ordered" and "substantially outweighs the harm to any third parties who may be harmed by such seizure." A plaintiff must also show that "the person against whom seizure would be ordered, or persons acting in concert with such person, would destroy, move, hide, or otherwise make such matter inaccessible to the court, if the applicant were to proceed on notice to such person." DTSA (S. 1890, 114th Cong.), § 2(a) (2015-2016).

The DTSA also provides that, if a seizure is ordered, the order must "direct that the seizure be conducted in a manner that minimizes any interruption of the business operation of third parties and, to the extent possible, does not interrupt the legitimate business operations of the person accused of misappropriating the trade secret that are unrelated to the trade secret that has allegedly been misappropriated." The seizure itself must be carried out by a federal law enforcement officer. While the DTSA notes that a court may allow state or local law enforcement officials to participate in the seizure, the court may not permit the applicant or any agent of the applicant to participate in the seizure. Further, at the request of law enforcement officials, the court may allow a technical expert who is unaffiliated with the applicant and who is bound by a court-approved non-disclosure agreement to participate in the seizure if the court determines that the participation of the expert will aid the efficient execution of and minimize the burden of the seizure. DTSA (S. 1890, 114th Cong.), § 2(a) (2015-2016).

If a seizure order is issued, a hearing must also be scheduled within seven days where the defendant will have an opportunity to be heard. A defendant who suffers damages by reason of a wrongful or excessive seizure has a cause of action against the applicant and can recover damages including lost profits and punitive damages. Although the seizure provision is new to this area of the law, the current language seeks to balance a legitimate need to protect information with protections against seizures procured through bad faith.

Jurisdiction Questions

Importantly, unlike patent or copyright law, federal jurisdiction through the DTSA is limited to cases arising under the commerce clause of the U.S. Constitution. Specifically, to trigger federal question jurisdiction for actual or threatened trade secret misappropriation, the trade secret must be "related to a product or service used in, or intended for use in, interstate or foreign commerce." DTSA (S. 1890, 114th Cong.), § 2(a) (2015-2016). This provision has raised the question of over how courts will interpret the term "related" to a product or service used in or intended to be used in interstate or foreign commerce. If a trade secret does not "relate" to a product or service involved in interstate commerce, a federal court sitting in diversity would arguably be required to apply state substantive laws to a trade secret misappropriation claim despite the enactment of the DTSA. Conversely, defendants who prefer the state forum will seek dismissal based on lack of federal question jurisdiction on the grounds that a trade secret does not implicate interstate commerce. In determining whether an activity has a "substantial relation to interstate commerce," the Supreme Court has held that the proper test is whether the activity "substantially affects" interstate commerce. *U.S. v. Lopez*, 514 U.S. 549, 559 (1995). Although there are infinite fact patterns, we should expect a fairly broad interpretation of the "related" language to effectuate federal jurisdiction.

Conclusion

Now that the DTSA has passed through both houses of Congress, given President Obama's support for the legislation, it should be signed into law soon. Thus, we should expect this new federal civil cause of action to be available this year, and it is important that practitioners be well-versed in the key provisions of this legislation and for companies to consider it as another weapon to protect their trade secrets.

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Editors:

Christopher Cox (SV)	Bio Page	chris.cox@weil.com	+1 650 802 3029

Contributing Authors:

Christopher Cox (SV)	Bio Page	chris.cox@weil.com	+1 650 802 3029
Bambo Obaro (SV)	Bio Page	bambo.obaro@weil.com	+1 650 802 3083
An Tran (SV)	Bio Page	an.tran@weil.com	+1 650 802 3098