

New Jersey Law Journal

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Legal Implications of the N.J. Trade Secrets Act

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New Jersey Law Journal

04-11-2013

Signed into law last year by Gov. Chris Christie, the New Jersey Trade Secrets Act, N.J.S.A. § 56:15-1 through 15-9 (NJTSA), went into effect on Jan. 9, 2012. The NJTSA's implementation made New Jersey one of the last states to adopt the provisions of the Uniform Trade Secrets Act, which, in turn, allows New Jersey businesses to benefit from uniform application and understanding of trade secret protections.

The passing of the NJTSA into law has created several legal implications for businesses and employers in New Jersey. Notably, the state legislature provided that the NJTSA and its provisions do not apply retroactively, even when continuing misappropriation occurs after the effective date. Claims under the NJTSA must be brought within three years — a change from the previous six years afforded under common law — after a trade secret holder discovers, or should have discovered by reasonable diligence, that a misappropriation has occurred.

The NJTSA and its effects have not yet been analyzed by the courts, but prior court holdings related to misappropriation claims, as well as how other jurisdictions treat this highly fact-sensitive area of business tort law, will provide guidance in the future. Indeed, in December 2012, in a case of first impression, the Superior Court of New Jersey, Chancery Division, looked to several court holdings in other jurisdictions in reviewing the NJTSA's pre-emption provision, which provides that the act shall supersede conflicting tort, restitutionary and other state laws providing civil remedies for misappropriation of a trade secret.

In *SCS Healthcare Mktg. v. Allergan USA* (unpublished), the court held that the legislature intended the NJTSA to be cumulative, rather than restrictive, of the rights and remedies provided under the common law. So while the common-law classifications, definitions and provisions relating to trade secret misappropriation claims may be pre-empted by conflicting provisions in the NJTSA, it appears as though there are scenarios in which a claim based on dissemination of confidential information would not be pre-empted by the act. As misappropriation cases now begin to make their way through the state appellate courts, the relationship between common and statutory law will surely continue to be fleshed out.

While the NJTSA has essentially codified existing common law, it provides a more comprehensive set of protections and provides consistency in determining what information constitutes a trade secret, what conduct gives rise to misappropriation and what remedies are available to proprietors. Initially, the NJTSA provides an expansive definition of "trade secret," incorporating elements of the Uniform Act as well as New Jersey common law. A trade secret has always been treated by the courts as information — in essentially any form imaginable — that has value to the proprietor in creating a competitive edge in the marketplace, and that the proprietor takes measures to keep a secret.

Under the NJTSA, the definition includes formulas, patterns, business data compilations, programs, devices, methods, techniques, designs, diagrams, drawings, inventions, plans, procedures, prototypes or processes, so long as the information: (1) derives independent economic value, actual or potential, from not being generally known or ascertainable through proper means by other persons who can obtain economic value from its disclosure or use; and (2) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy. An important analysis to make is that of competitive advantage. A business can make every effort to safeguard the information, but if it does not provide a competitive benefit in the marketplace, it will not be afforded trade secret protection. As noted above, a company's confidential information may not necessarily be deemed a trade secret. Many matters in business dealings are confidential, but to be deemed a trade secret, there must be a demonstrable competitive advantage to afford protection of the NJTSA.

The definition of “misappropriation” has not significantly changed from the courts’ application in common law prior to the enactment of the NJTSA. The legislature prohibits the acquisition of a trade secret if the user acquires the information through improper means, either directly or indirectly (i.e., if the user knows its source acquired the information through improper means). Improper means can be theft, bribery, misrepresentation, espionage, unauthorized access, breach of a duty to maintain the secret, or any other means that violate a person’s rights under the laws of New Jersey. A continuing misappropriation constitutes a single claim under the NJTSA.

The act does not, of course, prohibit reverse engineering or discovery through other proper means, such as discovery under a license agreement with the trade secret owner, observation of the information in public use or on public display, or obtaining the trade secret through published literature. Just because there existed proper means to discover the trade secret when it was acquired, however, will not excuse misappropriation if the user discovers the information through improper means. Indeed, the availability of proper acquisition is not a defense under the NJTSA.

The statutory framework provides several remedies to combat prohibited conduct. Initially, a business may seek injunctive relief for either actual or threatened misappropriation. The NJTSA contains a royalty provision which allows an injunction to condition future use upon payment of a reasonable royalty for the period of time when the use of the information could have been prohibited. The royalty provision only arises in “exceptional circumstances,” such as when a prohibited user’s acquisition of the protected information constitutes a material and prejudicial change which would render a prohibitive injunction inequitable.

Damages for a misappropriation claim can include both the actual loss caused by misappropriation and the unjust enrichment that is not considered in computing actual loss. Punitive damages are available should the court find the prohibited user’s conduct to be willful and malicious. Such damages, however, would be limited to twice that awarded for actual loss and unjust enrichment.

A hurdle to initiating litigation has always been the threat of having to reveal the very secret information a business has been attempting to protect in litigation discovery. Proprietors will undoubtedly be leery of responding to exhaustive discovery requests relating to the nature of the protected information. In response, the statutory framework provides that the courts must preserve the secrecy of alleged trade secrets in litigation by reasonable means. Most likely, and depending on the nature of the matter, this will involve protective orders, limitations on inspections, the use of neutral review and court overview of forensic analysis and inspections — something the courts will be familiar with as they routinely balance the interests between the right to relevant information and the risk of disclosing sensitive information.

One last perk under the NJTSA? The potential for an award of legal fees and costs, including expert fees. The express provision for expert fees is critical, as calculation of damages, including the provision for a reasonable royalty, can be heavily dependent on expert opinion testimony. Indeed, those in a particular industry, rather than attorneys or judges, are generally in the best position to determine the value of the protectable information and whether the means by which an owner protects the information are reasonable. This fee-shifting provision can be a powerful tool in forcing an opponent’s hand — but beware, as attorney fees are also available for a successful claim that a misappropriation action was brought in bad faith or was frivolous.

A year after the enactment of the NJTSA, we have yet to see exactly how the act will play out in the courts. The act does, however, provide important guidelines to employers and business owners in a position to safeguard protectable information. Clearly the statutory structure is designed to be highly flexible, and the specific factual circumstances of the conflict must be thoroughly analyzed and developed before seeking any relief from the courts.

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