

## [Primer on Pennsylvania Trade Secret Law Following Enactment of the Uniform Trade Secrets Act](#)

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### INTRODUCTION

Pennsylvania adopted the Uniform Trade Secrets Act ("UTSA") on February 19, 2004.<sup>1</sup> The PAUTSA became effective in Pennsylvania on April 19, 2004.<sup>2</sup> This article provides an overview of the PAUTSA's statutory scheme and distinguishes those areas where the PAUTSA has departed from the UTSA. Further, it discusses some key areas of Pennsylvania trade secret law that have been changed by Pennsylvania's adoption of the UTSA. Finally, it sets forth a few of the areas where the PAUTSA has expanded upon existing trade secret law in Pennsylvania.

### OVERVIEW OF PAUTSA

#### *Definitions*

Under the PAUTSA, actual or threatened misappropriation of a trade secret is actionable.<sup>3</sup> Section 5302 of the PAUTSA contains comprehensive definitions of what is considered a trade secret and what conduct constitutes misappropriation.

A trade secret is "information, including a formula, drawing, pattern, compilation including a customer list, program, device, method, technique or process that: (1) 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] (2) [i]s the subject of efforts that are reasonable under the circumstances to maintain its secrecy."<sup>4</sup>

Misappropriation is defined to include:

(1) 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 (2) disclosure or use of a trade secret of another without express or implied consent by a person who (i) used improper means to acquire knowledge of the trade secret; (ii) at the time of the disclosure or use, knew or had reason to know that his knowledge of the trade secret was: (A) derived from or through a person who had utilized improper means to acquire it; (B) acquired under circumstances giving rise to a duty to maintain its secrecy or limit its use; or (C) derived from or through a person who owed a duty to the person seeking relief to maintain its secrecy or limit its use; (iii) before a material change of his 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.<sup>5</sup>

The phrase "improper means" as used in the definition of misappropriation also is a term of art. It "[i]ncludes, but is not limited to, theft, bribery, misrepresentation, breach or inducement of a breach of a duty to maintain secrecy or espionage through electronic or other means."<sup>6</sup>

### *Remedies*

Under the PAUTSA, there are several sections that address what remedies are available if a plaintiff demonstrates that actual or threatened misappropriation has occurred. Section 5303 provides that a court may issue an injunction and identifies how long such an injunction may issue.<sup>7</sup> Section 5303(a) states: "Upon application to the court, an injunction shall be terminated when the trade secret has ceased to exist, but the injunction may be continued for an additional period of time in order to eliminate commercial advantage that otherwise would be derived from the misappropriation."<sup>8</sup>

Section 5303(b) provides that in "exceptional circumstances," a court, when granting an injunction, may condition "future use upon payment of a reasonable royalty for no longer than the period of time for which use could have been prohibited."<sup>9</sup> Exceptional circumstances are defined to include but are not limited to "a material and prejudicial change of position prior to acquiring knowledge or reason to know of misappropriation that renders a prohibitive injunction inequitable."<sup>10</sup> Finally, there is a "catch-all" provision allowing a court, as part of any injunctive relief ordered, to compel other "affirmative acts."<sup>11</sup> By adopting the catch-all provision contained in the UTSA, Pennsylvania ensured that a court would not be constrained by principles that injunctions should only issue to preserve the status quo.<sup>12</sup>

In addition to injunctive relief, a plaintiff may also recover monetary and exemplary damages.<sup>13</sup> Monetary damages recoverable "can include both the actual loss caused by the misappropriation and the unjust enrichment caused by misappropriation that is not taken into account in computing actual loss."<sup>14</sup> Another damage measure that can be used is to impose liability for a "reasonable royalty for the misappropriator's unauthorized disclosure or use of a trade secret."<sup>15</sup>

Although the PAUTSA does permit a court (as opposed to a jury) to award exemplary damages "if willful and malicious misappropriation exists," such award may not exceed "twice any award" of monetary damages.<sup>16</sup> This limitation departs from existing jurisprudence concerning the relationship between compensatory and punitive damages.<sup>17</sup> Such a limitation also is a significant departure because it assigns at least the amount of any punitive damage award to the court as opposed to a jury.<sup>18</sup>

An obvious benefit of Pennsylvania's adoption of the UTSA is the provision for the award of attorneys' fees. Reasonable attorneys' fees, expenses and costs may be awarded by the court to the prevailing party under the following circumstances: (1) if a claim of misappropriation is made in bad faith; (2) a motion to terminate an injunction is made or resisted in bad faith; or (3) willful and malicious misappropriation exists.<sup>19</sup>

In actions that are brought under this statute, a court is required to "preserve the secrecy of any alleged trade secret by reasonable means which may include, but are not limited to, granting protective orders in connection with discovery proceedings, holding in camera hearings, sealing

the records of the action and ordering any person involved in the litigation not to disclose an alleged trade secret without prior court approval."<sup>20</sup>

### *Statute of Limitations and Impact on Other Laws*

Actions under the PAUTSA must be brought within three years "after the misappropriation was discovered or by the exercise of reasonable diligence should have been discovered."<sup>21</sup>

Another important aspect of the PAUTSA is its impact on other laws. Section 5308 provides, with a few exceptions, that the statute "displaces conflicting tort, restitutionary and other laws of this Commonwealth providing for civil remedies for misappropriation of a trade secret."<sup>22</sup>

### **DISTINCTIONS BETWEEN PAUTSA AND UTSA**

Pennsylvania adopted all material sections of the UTSA.<sup>23</sup> Pennsylvania did not adopt section 8, which addresses uniformity of application and construction, and section 10, which addresses severability.<sup>24</sup> Although technically not adopting section 11 of UTSA, the time of taking effect, the substance of this section is addressed in the commentary accompanying Pennsylvania's adoption of section 9 of the UTSA.<sup>25</sup>

In adopting the definitions contained in section 1 of the UTSA, Pennsylvania made some slight modifications. Theoretically, Pennsylvania expanded the definition of "improper means" by stating that "improper means includes *but is not limited to*."<sup>26</sup>

To the UTSA's definition of a trade secret, Pennsylvania added drawings and customer lists.<sup>27</sup> The inclusion of these specific kinds of information is consistent with prior case law defining what constitutes a trade secret under Pennsylvania law.<sup>28</sup>

Pennsylvania also added a new definition for "willful and malicious" (which is referenced in the exemplary damage and attorneys' fees sections) that does not appear in the UTSA. "Willful and malicious" is defined by the PAUTSA as "[s]uch intentional acts or gross neglect of duty as to evince a reckless indifference of the rights of others on the part of the wrongdoer, and an entire want of care so as to raise the presumption that the person at fault is conscious of the consequences of his carelessness."<sup>29</sup> Such a definition echoes the language used by the Pennsylvania courts in describing the type of conduct that would warrant a fact finder to award punitive damages.<sup>30</sup>

To the attorneys' fees provision of the UTSA, PAUTSA also added that a court also may award expenses and costs.<sup>31</sup> With respect to the section of the UTSA addressing the power of the court to preserve the secrecy of a trade secret, Pennsylvania made clear that the enumerated powers were not exclusive by adding to the word "includes," the phrase "but are not limited to."<sup>32</sup>

Although Pennsylvania did not alter the three-year statute of limitations that are applicable to such actions, it did omit the last sentence of Section 6 of the UTSA which provides "[f]or purposes of this section, a continuing misappropriation constitutes a single claim."<sup>33</sup>

## DEPARTURES FROM PRIOR CASE LAW

The most significant departures from prior case law that are contained in the PAUTSA concern the application of a three-year statute of limitations, the specific limitation that a punitive damage award may not exceed two times any compensatory damage award, and the ability of a prevailing party to recover attorneys' fees.

### *Statute of Limitations*

Before the adoption of the PAUTSA, the statute of limitations applicable to a misappropriation of trade secrets claim was two years.<sup>34</sup> Although a two-year limitation period is relatively short, misappropriation of a trade secret was considered "a continuing tort" under Pennsylvania law.<sup>35</sup> Consequently, the statute of limitations began to run with each wrongful use.<sup>36</sup> Practically, this had the effect of allowing claims that might otherwise be time-barred to proceed. The true impact of the limitations period, therefore, was to operate as a cap on the damages that could be recoverable as opposed to an absolute bar from bringing a claim.<sup>37</sup>

With the adoption of the UTSA's statute of limitations section without modification, Pennsylvania has changed existing law by rejecting its prior subscription to the continuing wrong approach. Section 5307's commentary is particularly instructive:

There presently is a conflict of authority as to whether a trade secret misappropriation is a continuing wrong.

\* \* \* \*

The Act rejects a continuing wrong approach to the statute of limitations but delays the commencement of the limitations period until an aggrieved person discovers or reasonably should have discovered the existence of misappropriation. If objectively reasonable notice of misappropriation exists, three years is sufficient time to vindicate one's legal rights.<sup>38</sup>

Under Pennsylvania law then, a plaintiff needs to diligently pursue a misappropriation claim or risk having such a claim be completely time-barred.

### *Exemplary Damages*

Pennsylvania's adoption of the UTSA's 2-1 punitive/compensatory damage ratio represents a meaningful departure from existing jurisprudence concerning the relationship between compensatory and punitive damages. Under Pennsylvania law, there was no specific ratio limitation imposed on punitive damage awards. To the extent a fact finder determined that punitive damages were warranted, such damages needed only to bear "a reasonable relationship between the amount of the award and the twin goals of punishment and deterrence, the character of the tortious act, the nature and extent of the harm suffered by plaintiff, and the wealth of the defendant."<sup>39</sup> Mathematical proportionality was not required between punitive and compensatory damages.<sup>40</sup> *Id.*

The United States Supreme Court recently provided considerable guidance to state and federal courts concerning the appropriate relationship between compensatory and punitive damages in *State Farm Mutual Automobile Ins. Co. v. Campbell*.<sup>41</sup> The Court admonished that in order to comport with due process, the relationship between a punitive damage award and compensatory damage award could rarely exceed "a single-digit ratio."<sup>42</sup> Although the Court suggested that an award of more than four times the amount of compensatory damages might be close to the line of constitutional impropriety, it declined to "impose a bright-line ratio which a punitive damages award cannot exceed." *Id.* Under the current jurisprudence, therefore, there was nothing to suggest that a 2-1 ratio ought to be the relationship between punitive and compensatory damages.

Nevertheless, despite this jurisprudence, Pennsylvania elected to follow the UTSA's guidance in this area. Not surprisingly, this is one aspect of the UTSA that has not been adopted uniformly by the states. Michigan, Mississippi, Nebraska and Vermont have not imposed an express limitation on the amount of exemplary damages that may be awarded.<sup>43</sup> In contrast, Ohio allows exemplary damages to be awarded up to three times the amount of any compensatory damages.<sup>44</sup> While other states like Colorado and Virginia have lowered the punitive/compensatory damage ratio.<sup>45</sup>

### *Attorneys' Fees*

Prior to Pennsylvania's adoption of the UTSA, attorneys' fees generally could not be recovered in a misappropriation of trade secrets case.<sup>46</sup> Attorneys' fees now can be recovered. However, as the statute reveals, recovery of attorneys' fees may be sought by either a prevailing plaintiff or a prevailing defendant under three specific scenarios.<sup>47</sup> The reference to what constitutes a "prevailing party" is an explicit reference to how a judge decides who is a prevailing party under patent law.<sup>48</sup> The attorney fees provision of Title 35 of the United States Code provides that "the court in exceptional cases may award reasonable attorney fees to the prevailing party."<sup>49</sup> As several circuit courts have articulated, the purpose of this section is to provide courts with discretion in those situations where it would be "grossly unjust that the winner be left to bear the burden of his own counsel which prevailing litigants normally bear."<sup>50</sup>

## **EXPANSION OF PRIOR CASE LAW**

There are several areas where PAUTSA has expanded existing case law. Under existing case law, misappropriation was considered to include either improper disclosure or improper use.<sup>51</sup> Now that definition has been expanded to include "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."<sup>52</sup> Thus, in theory, a plaintiff need not wait to bring a misappropriation claim until there is some evidence that a defendant has improperly used a trade secret.

Another expansion area of trade secret law concerns what constitutes a trade secret. Under Pennsylvania law and consistent with the *First Restatement*, in order for information to be classified as a trade secret, the information needed to be used in a person's business.<sup>53</sup> PAUTSA's trade secret definition represents a departure from the *First Restatement* by requiring only that a trade secret "derive[ ] independent economic value, actual or potential."<sup>54</sup> The uniform

comments which accompany the definitions, and which Pennsylvania has adopted, clarify why requiring continuous use can be problematic in defining what constitutes a trade secret.

The definition of "trade secret" contains a reasonable departure from the Restatement of Torts (First) definition which required that a trade secret be "continuously used in one's business." The broader definition in the proposed Act extends protection to a plaintiff who has not yet had an opportunity or acquired the means to put a trade secret to use. The definition includes information that has commercial value from a negative view point, for example the results of lengthy and expensive research which proves that a certain process will *not* work could be of great value to a competitor.<sup>55</sup>

Damage measures also have expanded as a result of the adoption of the PAUTSA. Consistent with existing Pennsylvania trade secret law, the PAUTSA sanctions the calculation of damages based upon a complainant's actual loss<sup>56</sup> or a defendant's unjust enrichment or benefit as a result of the misappropriation.<sup>57</sup> Now a plaintiff may use a reasonable royalty measure as a way of calculating damages.<sup>58</sup> Such a methodology had not been previously accepted as measure of damages under Pennsylvania law for misappropriation.<sup>59</sup>

The notes accompanying Pennsylvania's adoption regarding a reasonable royalty provide little guidance concerning how such a measure ought to be employed. The notes distinguish how reasonable royalty damages differ from a royalty order injunction and provide "[i]n order to justify this alternative measure of damages, there must be competent evidence of the amount of a reasonable royalty."<sup>60</sup>

Cases from other jurisdictions, however, are instructive. In *Forest Laboratories, Inc. v. Formulations, Inc.*<sup>61</sup> explained that a reasonable royalty is used as a way of determining what the parties would have agreed upon in terms of a licensing fee if they were to try to reach an agreement.<sup>62</sup> Some of the factors that are used in determining a reasonable royalty include:

The resulting and foreseeable changes in the parties' competitive posture; the prices past purchasees or licensees may have paid; the total value of the secret to plaintiff, including the plaintiff's development costs and the importance of the secret to the plaintiff's business; the nature or extent of the use the defendant intended for the secret; and finally whatever other unique factors in the particular case which might have affected the parties' agreement, such as the ready availability of alternative processes.<sup>63</sup>

The cases in this arena, therefore, make clear that a prevailing party is not automatically entitled to attorneys' fees.<sup>64</sup> Although it is often clear who is a winner where all of a party's requested relief is either granted or denied, determining who is a prevailing party becomes more difficult where there has been partial success. In such situations, it is not uncommon for a court to determine that, under the circumstances, no one is entitled to attorneys' fees.<sup>65</sup> Other courts, however, have considered a party to be a prevailing party in the situation where a party "prevailed on more of litigated issues than plaintiff,"<sup>66</sup> or where a party obtained most of the relief demanded in the case.<sup>67</sup>

<sup>1</sup> 12 Pa. C.S.A. §§ 5301-5308. As used in this article, PAUTSA refers to Pennsylvania's Uniform Trade Secrets Act. In contrast, UTSA refers to the Uniform Trade Secrets Act.

<sup>2</sup> 12 Pa. C.S.A. § 5301, notes. The PAUTSA does not apply to "misappropriation occurring prior to the effective date of the act, including continuing misappropriation that began prior to the effective date of the act and which continues to occur after the effective date of this act." *Id.*, notes. Consequently, Pennsylvania case law is relevant both in providing the substantive law in existing and future lawsuits as well as clarifying those issues in Pennsylvania trade secret law that are not addressed by the PAUTSA.

<sup>3</sup> *Id.* §§ 5302-5304.

<sup>4</sup> *Id.* § 5302.

<sup>5</sup> *Id.*

<sup>6</sup> *Id.*

<sup>7</sup> *Id.* § 5303(a)

<sup>8</sup> *Id.*

<sup>9</sup> *Id.* § 5303(b).

<sup>10</sup> *Id.*

<sup>11</sup> *Id.* § 5303(c).

<sup>12</sup> *See Keystone Guild, Inc. v. Pappas*, 159 A.2d 681, 683 (Pa. 1960) (injunctions should restore the parties to the status quo before the wrongful conduct occurred).

<sup>13</sup> *Id.* § 5304.

<sup>14</sup> *Id.* § 5304(a).

<sup>15</sup> *Id.*

<sup>16</sup> *Id.* § 5304(b).

<sup>17</sup> *See infra* pp. 7-9.

<sup>18</sup> *See, e.g., Delahanty v. First Pennsylvania Bank, N.A.*, 464 A.2d 1243, 1263 (Pa. Super. 1983) ("It is well settled law in Pennsylvania that the decision of whether to award punitive damages and **the amount to be awarded are within the discretion of the fact finder.**") (emphasis added).

<sup>19</sup> *Id.* § 5305.

<sup>20</sup> *Id.* § 5306.

<sup>21</sup> *Id.* § 5307.

<sup>22</sup> *Id.* § 5308(a). The exceptions enumerated in the statute are: (1) contractual remedies, whether or not based upon misappropriation of a trade secret; (2) other civil remedies that are not based upon misappropriation of a trade secret; or (3) criminal remedies, whether or not based upon misappropriation of a trade secret. *Id.* § 5308(b).

<sup>23</sup> Pennsylvania adopted Sections 1-7 & 9 of the UTSA. 12 Pa. C.S.A §§ 5301-5308 & notes.

<sup>24</sup> *Id.*

<sup>25</sup> 12 Pa. C.S.A. § 5301.

<sup>26</sup> ULA Trade Secrets § 1, cmt. (emphasis added).

<sup>27</sup> *Id.*

<sup>28</sup> *Ecolaire Inc. v. Crissman*, 542 F. Supp. 196 (E.D. Pa. 1982) (drawings); *Felmlee v. Lockett*, 351 A.2d 273, 277 (Pa. 1976) (customer lists); *Air Prods. & Chem., Inc. v. Johnson*, 442 A.2d 1114, 1121 (Pa. Super. 1982) (customer lists).

<sup>29</sup> Pa. C.S.A. § 5302.

<sup>30</sup> *See, e.g., Delahanty v. First Pennsylvania Bank, N.A.*, 464 A.2d 1243, 1262 (Pa. Super. 1983) (describing that punitive damages are permissible where a defendant's conduct has involved bad motive or reckless indifference, or conduct that is willful, malicious, wanton, reckless or oppressive).

<sup>31</sup> ULA Trade Secrets § 4, cmt.

<sup>32</sup> ULA Trade Secrets § 5, cmt..

<sup>33</sup> ULA Trade Secrets § 6, cmt.

<sup>34</sup> *Frank W. Winne & Son, Inc. v. Palmer*, 1991 WL 155819 (E.D. Pa. Aug. 7, 1991); 42 Pa. Cons. Stat. Ann. § 5524.

<sup>35</sup> *Palmer*, 1991 WL 155819, at \*4.

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*

<sup>38</sup> 12 Pa C.S.A. § 5307, notes.

<sup>39</sup> *Pioneer Commercial Funding Corp. v. American Financial Mortgage Corp.* , 797 A.2d 269, 292 (Pa. Super. 2002).

<sup>40</sup> *Id.*

<sup>41</sup> 538 U.S. 408 (2003).

<sup>42</sup> *Id.* at 425.

<sup>43</sup> ULA Trade Secr. § 3, notes. Further, Michigan and Nebraska has not relegated the determination of punitive damage amounts to the court.

<sup>44</sup> *Id.*

<sup>45</sup> Colorado provides that "a court or jury may award exemplary damages in an amount not exceeding the award made under the [compensatory damage] Section." Virginia provides "the court may award punitive damages in an amount not exceeding twice any award made under Subsection A of this Section, or \$350,000 whichever amount is less."

<sup>46</sup> *See, e.g., Greenberg v. Croydon Plastics Co.* , 378 F. Supp. 806, 817-818 (E.D. Pa. 1974) (discussing the reasons why courts do not award attorneys' fees even in trade secret cases).

<sup>47</sup> Reasonable attorneys' fees, expenses and costs may be awarded by the court to the prevailing party under the following circumstances: (1) if a claim of misappropriation is made in bad faith; (2) a motion to terminate an injunction is made or resisted in bad faith; or (3) willful and malicious misappropriation exists. 12 Pa. C.S.A. § 5307.

<sup>48</sup> 12 Pa. C.S.A. § 5305, cmt. (referencing 35 U.S.C. § 285).

<sup>49</sup> 35 U.S.C. § 285.

<sup>50</sup> *Badalamenti v. Dunham's Inc.* , 896 F.2d 1359, *cert. Denied* ; 498 U.S. 851 (Fed. Cir. 1990); *see also Central Soya Co. v. Geo. A. Homul & Co.* , 723 F.2d 1573 (Fed. Cir. 1983); *Pennsylvania Crusher Co. v. Bethlehem Steel Co.* , 193 F.2d 445 (3d Cir. 1951).

<sup>51</sup> *Van Prod. Co. v. General Welding & Fabricating Co.* , 213 A.2d 769, 774-75 n.3 (Pa. 1965).

<sup>52</sup> 12 Pa. C.S.A. § 5302.

<sup>53</sup> *See Felmlee v. Lockett* , 351 A.2d 273, 277 (Pa. 1976) (adopting *Restatement (First) of Torts* § 75 cmt. B (1939)).

<sup>54</sup> 12 Pa. C.S.A. § 5302.

<sup>55</sup> *Id.* , notes (emphasis added).

<sup>56</sup> *Greenberg v. Croydon Plastics Co.* , 378 F. Supp. 806, 816-17 (E.D. Pa. 1974) (stating that damages sustained by victim, the traditional common law remedy, is one method for assessing damages).

<sup>57</sup> *SI Handling Systems v. Heisley*, 658 F. Supp. 362, 371 (E.D. Pa. 1986); *Reinforced Molding Corp. v. General Electric Co.* , 592 F. Supp. 1083, 1088-89 (W.D. Pa. 1984) ("The appropriate measure of damages, by analogy to patent infringement, is not what the Plaintiff lost but rather the benefits, profits or advantages gained by Defendant in the use of the trade secret.")

<sup>58</sup> 12 Pa. C.S.A. § 5304.

<sup>59</sup>

<sup>60</sup> 12 Pa. C.S.A. § 5304, notes.

<sup>61</sup> 320 F. Supp. 211 (E.D. Wis. 1970).

<sup>62</sup> *Id.* at 212.

<sup>63</sup> *University Computing Co. v. Lykes-Youngstown Corp.* , 504 F.2d 538, 539 (1974).

<sup>64</sup> *See e.g., Oiness v. Walgreen Co.* , 774 F. Supp. 1277 (D. Co. 1991) ("that plaintiffs prevail in patent infringement case does not automatically entitle them to attorney fees").

<sup>65</sup> *Consolidated Aluminum Corp. v. Foseco Int'l Ltd.* , 910 F.2d 804 (1990).

<sup>66</sup> *Dixie Cup Co. v. Paper Container Mfg. Co.* , 169 F.2d 645 (1948).

<sup>67</sup> *Schmidt v. Zazzara* , 544 F.2d 412 (1976).