

# VIRGINIA BUSINESS TORTS

## Virginia Uniform Trade Secrets Act<sup>1</sup>

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"Your secret is your property."<sup>3</sup>

### I. Introduction

The Uniform Trade Secrets Act (hereinafter "Uniform Act")<sup>4</sup> was originally proposed in the United States by the National Conference of Commissioners on Uniform State Laws over twenty years ago and has now been enacted in most of the individual states<sup>5</sup> of the United States. The Virginia Uniform Trade Secrets Act (hereinafter "Virginia Act")<sup>6</sup> was enacted in Virginia with some modifications to the Uniform Act and became effective on July 1, 1986. The purpose of this document is to: (1) briefly review the historic background of trade secret law; (2) critically summarize the significant provisions of the Virginia Act; (3) identify some differences between the Virginia Act and the Uniform Act; and (4) review some of the significant published case law in Virginia concerning the Virginia Act. This document does not cover the federal 1996 Economic Espionage Act<sup>7</sup>, criminal penalties for the theft of a trade secret<sup>8</sup> and the Inevitable Disclosure

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<sup>1</sup> This document is derived from a law review article entitled "The Virginia Uniform Trade Secret Act: A Critical Summary of the Act and Case Law", published by the University of Virginia Journal of Law and Technology and a speech entitled "The Uniform Trade Secrets Act in the United States" given by the author in Kitzbuhel, Austria on March 21, 2000, at a Conference on the International Protection of Intellectual Property, which was sponsored by the Center for International Legal Studies and co-sponsored by the American Bar Association's Section on International Law. This document is also derived from a law review article entitled "The Maryland Uniform Trade Secret Act: A Critical Summary of the Act and Case Law", 32 no2 Univ. of Balt. L. R. 181, Spring 2002.

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<sup>3</sup> *Proverbs, Maxims and Phrases of All Ages* (Robert Christy ed., G.P. Putnam's Sons 1996), quoting Rothschild.

<sup>4</sup> Unif. Trade Secrets Act, 14 U.L.A. 437, *et seq.* (1985).

<sup>5</sup> New Jersey, New York, Texas, and Wyoming have not adopted a uniform trade secrets act. In New York, a bill has passed the Senate. Alabama and Massachusetts have their own acts.

<sup>6</sup> Va. Code Ann. §§ 59.1-336 - 343 (Michie 2000).

<sup>7</sup> Electronic Espionage Act, Pub.L. No. 104-294. *See* J. Derek Mason et al., "The Economic Espionage Act: Federal Protection for Corporate Trade Secrets," 16 No. 3 COMPUTER LAW, Mar. 1999 at 14.

Doctrine<sup>9</sup> which has been specifically rejected in Virginia,<sup>10</sup> Maryland<sup>11</sup> and some other jurisdictions.

## II. Historical Development of Trade Secrets Law

Epigraphical and literary sources clearly establish that trade secrets have commonly existed for a very long time. Early businesses had trade secrets, such as customer lists, secret formulae (*e.g.*, dyeing), methods of production (*e.g.*, pottery), vital business and financial records, etc. Those early businessmen must have attempted to protect their trade secrets. After all, their trade secrets gave them a competitive advantage. Surprisingly however, trade secret law does not seem to have a long history. There is a debate amongst classical Greek and Roman scholars as to whether there was any legal protection of trade secrets even in that era when sophisticated Greek and Roman businesses flourished and traded throughout the then known world.<sup>12</sup> One commentator, who cites Justinian and Gaius, makes the argument that under Roman law during the time of the late Republic and early Empire, there was a specific Roman cause of action named *actio servi corrupti* which prohibited a slave from stealing a trade secret of his master and giving it to a competitor.<sup>13</sup> As late as the Middle Ages in Europe, there does not appear to be any protection of trade secrets through the application of any unified body of trade secret law.<sup>14</sup> At that time, trade secrets were protected, if at all, through the application of unfair competition laws.

Trade secret law only began to develop with the newfound mobility of labor in the Industrial

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<sup>8</sup> Nevada added a section to its trade secret act imposing criminal penalties for theft of a trade secret. Nevada Code, Section 600 A.035. South Carolina did the same. Code of South Carolina, Section 39-8-90.

<sup>9</sup> For note, *Inevitable Disclosure Through an Internet Lens: Is the Doctrine's Demise Truly Inevitable*, see 45 Wm. & Mary L. Rev. 395 (2003).

<sup>10</sup> *GTSE, Inc. v. Intellisys. Tech. Corp.*, 51 Va. Cir. 55 (1999).

<sup>11</sup> *Lejeune v. Coin Acceptors, Inc.*, Md. Ct. App. No. 111, Sept. Term, 2003; *Padco Advisors, Inc. v. Omdahl*, 179 F.Supp.2d 600, 611 (D.Md. 2002).

<sup>12</sup> A. Arthur Schiller, *Trade Secrets and the Roman Law; The Actio Servi Corruptio*, Colum. L.R., vol. XXX, p. 837 and 838 and footnotes cited therein (1930).

<sup>13</sup> *Id.*

<sup>14</sup> *Id.*

Revolution in Europe.<sup>15</sup> A few early trade secret cases were published in the 19th Century in England.<sup>16</sup> In the 1851 English case of *Morison v. Moat*,<sup>17</sup> plaintiff sought and was granted an injunction to restrain the defendant from using a secret for compounding a medicine, “Morison’s Universal Medicine,” which was not the subject of a patent, and to restrain the sale of this medicine by the defendant, who acquired knowledge of the secret in violation of a contract and in breach of “trust and confidence.” However, this case was hardly the first trade secret case. The Vice-Chancellor, who rendered the opinion in this case, noted therein that by 1851 the Court had already heard trade secret cases, stating, “[t]hat the Court has exercised jurisdiction in cases of this nature does not, I think, admit of any question.”<sup>18</sup>

Possibly the first reported American case involving trade secrets was the 1837 case of *Vickery v. Welch*.<sup>19</sup> It is a simple but fundamental case involving the 1836 sale of a chocolate mill in Braintree, Massachusetts. In the sales agreement for the mill, the seller agreed to sell the mill, convey to the buyer the secret as to how to make the chocolate and deliver a written assurance that he would not give the secret to anyone else, all for the consideration of \$2000 and eight annual payments of \$7500. Two or three other persons in the company had knowledge of the seller’s secret, but they had given a written oath not to divulge it. The buyer tendered the money. However, upon advice of counsel, the seller refused to tender to the buyer the written promise not to convey his secret or art to others. The seller argued that if he so bound himself, it would be an unlawful restraint of trade. The Massachusetts court upheld the terms of the contract and ordered the seller not to disclose the secret to others. The court reached the conclusion that there was no restraint of trade in this case since it was “...of no consequence to

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15 The relationship between current trade secret law and the mobility of employees is discussed in Edmund Kitch, *The Expansion of Trade Secrecy Protection and the Mobility of Management Employees: A New Problem for the Law*, 47 S.C. L. REV. 659 (1996).

16 For a brief discussion of some of these cases, see JERRY COHEN & ALAN S. GUTTERMAN *TRADE SECRETS PROTECTION AND EXPLOITATION* (BNA Books 1998).

17 68 Eng. Rep. 492, 9 HARE 241 (1851).

18 *Id.* at 498.

19 36 Mass. 523 (1837).

the public whether the secret art be used by the plaintiff or defendant.”<sup>20</sup>

Possibly the earliest reported case in the Commonwealth of Virginia involving a trade secret was decided on the basis of contract law. In the 1940 case of *American Chlorophyll, Inc. v. Frank M. Schwartz*,<sup>21</sup> an inventor of a process to extract chlorophyll, carotene and xanthophyll from vegetable leaf matter licensed the process to the company in 1935 for a royalty of 5% of net sales, payable quarterly. Thereafter, the company refused to pay him any royalty. The inventor did not notify the defendant of the breach of the contract, as required by the license agreement. Instead the inventor caused an article to be published in a trade journal known as the “Industrial and Engineering Chemistry,” disclosing the process. In deciding the case, the Court simply applied traditional contract law and concluded that the plaintiff had elected to continue the contract by not exercising his right under the contract to terminate it. Since the contract remained in effect, his disclosure of the trade secret constituted a violation of the license agreement since the agreement contained a specific provision prohibiting disclosure.

Throughout these early cases the judiciary attempted to formulate a unified comprehensive legal theory to justify the protection of trade secrets. In the previously cited 1851 case of *Morison v. Moat*, this English court was already focusing on the theoretical basis for the protection of trade secrets:

Different grounds indeed have been assigned for the exercise of that jurisdiction. In some cases it has been referred to property, in others to contract, and in others, again, it has been treated as founded upon trust or confidence, meaning, as I conceive, that the Court fastens the obligation on the conscience of the party, and enforces it against him in the same manner as it enforces against a party to whom a benefit is given the obligation of performing a promise on the faith of which the benefit has been conferred; but, upon whatever grounds the jurisdiction is founded, the authorities leave no doubt as to the exercise of it.<sup>22</sup>

Even today, there does not appear to be any singular underlying legal theory to justify the

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<sup>20</sup> *Id.* at 527.

<sup>21</sup> 11 S.E.2d 625 (Va. 1940).

<sup>22</sup> 68 Eng. Rep. at 498.

protection of trade secrets. While the need for the protection of such secrets is virtually uncontroverted in most Western countries, the several legal theories used to justify trade secret legislation do so only partially and inadequately. Early trade secret cases, and even some current cases, still justify the protection of trade secrets as a property right of the owner of the trade secret. However, this theory does not work in all cases. For example, trade secret law provides that the owner of a trade secret has no right to protect it if that secret is acquired by others who develop it on their own by proper means. Also, protection of a trade secret will be lost, and others will be able to exploit it, if the secret is inadvertently or even improperly disclosed to the public or enters the public domain. Clearly, these examples are inconsistent with the concept of protection of a trade secret based on a property right in the trade secret.

Another theoretical basis advanced for the protection of trade secrets is contract theory. However, this theory has very limited applicability. In many cases a written contract will not be in place between the trade secret owner and the misappropriator of the trade secret. A frequent example involves a departing employee who misappropriates a trade secret from his employer and the employee has not executed a non-disclosure of proprietary information agreement. Recognizing the obvious inadequacies of the use of the property theory and the contract theory to justify the protection of trade secrets, law professors and jurists advanced the theory that the protection of trade secrets is justified on the basis of a general duty of good faith. That is, it is fair to protect someone who has a trade secret from someone who misappropriates it by improper or unlawful means. Finally, it has been argued that trade secret protection is justified, like patents, to encourage inventors and investors to create, innovate and develop new technologies by protecting their inventions and investments and allowing them to profit thereby.

Regardless of the absence of a comprehensive underlying theory justifying the protection of trade secrets, by the early 20th Century, the number of trade secret cases had begun to substantially increase in the United States. Concurrently, prominent American professors of law and jurists began to publish the First Restatement of Torts in which they set forth what they considered to be general principles of law to be considered by the various states of the United States and others to foster uniformity in the laws of the various states. In 1939, in recognition of this growing body of trade secret case law, the First Restatement included an important new

definition of a trade secret. Comment b of the First Restatement of Torts defined a trade secret as any “formula, pattern, process, device, or compilation of information used in a business that gives the user an opportunity to obtain an advantage over nonusers.”<sup>23</sup>

After the publication of the First Restatement’s definition, it was widely applied by the judiciary to ever increasing numbers of trade secret cases in the United States. In light of the success of this definition, a consensus began to develop that there was a need for a unified, distinct and comprehensive trade secrets law. In 1969, the United States National Conference of Commissioners on Uniform State Laws (hereinafter “the Conference”) organized a committee to develop a uniform trade secrets act. The committee considered the definition<sup>24</sup> of a trade secret used in the First Restatement and formulated the Uniform Act’s definition of a trade secret, relying heavily on the definition found in the First Restatement. In 1979, the Conference adopted the Uniform Trade Secrets Act and in 1985, it made important amendments to the Uniform Act.

The Uniform Act quickly became widely and favorably recognized in the various states as a model for legislation. Currently, 44 of the 50 states have enacted a version of the Uniform Act, each state varying its legislation to some degree from the Uniform Act.<sup>25</sup> Since its adoption by

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23 See RESTATEMENT (FIRST) OF TORTS ch. 36, § 757b (1939).

24 For a discussion of the evolution of the various definitions of trade secrets in the Restatements since the 1939 First Restatement, see Kitch, 47 S.C. L. REV. 660-663.

<sup>25</sup>The effective dates of each of the state statutes and the citation to the act in the state code are: Alabama Code, Section 8-27-1 to 8-27-6 (1957) (entered effect August 12, 1987); Alaska (9/2/88), ALASKA STAT. Sections 45.50, 910-45 (Michie 1994) (entered effect Sept. 12, 1988); ARIZ REV. STAT. Sections 44-401-407 (2000) (entered effect April 11, 1990); ARK. CODE ANN. Sections 4-75-601-607 (Michie 1999) (entered effect Mar. 12, 1981); CAL. CIV. CODE ANN. Sections 3426 *et seq.* (Deering 2000) (entered effect Jan. 1, 1985); COLO.REV.STAT.ANN. Sections 7-74-101 *et seq.* (West 2000) (entered effect July 1, 1986); CONN. GEN. STAT.ANN. sections 35-50 to 58 (1999); DEL. CODE TIT. 6, Sections 2001-09 (entered effect April 15, 1982); D.C. CODE ANN. Section 48-50 *et seq.* (2000) (entered effect March 16, 1989); FLA. STAT. ch. 688.001-009 (2000) (entered effect Oct. 10, 1988); GA CODE ANN. Sections 10-1-760 to 767 (entered effect July 1, 1990); HAW. REV. STAT. Sections 482B-1 to -9 (2000) (entered effect July 1, 1989); IDAHO CODE Sections 48-801 to -807 (1999) (entered effect 1989); ILL. COMP. STAT. Sections 1065/1 to /9 (West 2000) (entered effect Jan. 1, 1988); IND. CODE Sections 24-2-3-1 to 24-2-3-8 (1998) (entered effect Feb. 25, 1982); IOWA CODE Sections 550-1 – 8 (1999) (entered effect April 27, 1990); KAN. STAT ANN. Sections 60-3320 to -3330 (1999) (entered effect July 1, 1981); KY. REV. STAT. ANN. Section 365-880 to -900 (Michie 1998) (entered effect April 6, 1990); LA.REV. STAT. ANN. Sections 51:1431 to :1439 (West 2000) (entered effect July 19, 1981); ME. REV. STA. ANN tit. 10, Sections 1541-48 (West 1999) (entered effect May 22, 1987); MD. CODE ANN. , COM LAW Sections 11-201 *et seq.* (1999) (entered effect July 1, 1989); Michigan M.C.L.A., Sections 445.1901 to 445.1910 (entered effect Oct. 1, 1998); MINN. STAT. Sections 325C.01-08 (1999) (entered effect Jan. 1, 1981); MISS. CODE ANN.

the Conference and enactment by various states, courts of the various enacting states have decided and published numerous cases under their respective versions of the Uniform Act, interpreting the various provisions and enhancing our understanding of the Act. Since the Virginia Act's effective date in the Commonwealth of Virginia on July 1, 1986, Virginia courts have decided numerous published and unpublished trade secret cases. Of course, many more Virginia trade secret cases have been mediated, arbitrated or settled by the parties.

Other countries, as well, are adopting some form of trade secrets law.<sup>26</sup> Some of those countries are following the format and concepts of the Uniform Act.<sup>27</sup> By contrast, some of the United States' major trading partners, such as Canada and the United Kingdom, do not protect their citizens' trade secrets by a distinct and unified body of law, such as our Uniform Act. They have simply applied their existing unfair competition laws to protect their citizens' trade secrets.

Further, while it is frequently said that there is no international treaty concerning the protection and exploitation of trade secrets, the United States is a signatory to the Agreement on Trade Related Aspects of Intellectual Property Rights of GATT which requires each signatory to enact legislation for the protection of information. The Agreement describes the required legislation

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Sections 75-26-1 to -19 (2000) (entered effect July 1, 1989); MO. REV. STAT. Sections 417.450 to 467 (1999) (entered effect Oct. 6, 1995); MONT. CODE ANN. Sections 30-14-401 to -409 (1999) (entered effect 1985); NEB. REV. STAT. ANN. Sections 87-501 to -507 (2000) (entered effect July 8, 1988); NEV. REV. STAT. Sections 600A.010 to -.100 (2000) (entered effect Mar. 15, 1987); N.H. REV. STAT. ANN. Sections 350-B.1-.9 (2000) (entered effect Jan. 1, 1990); N.M. STAT. ANN. Sections 57-3A-1 to -7 (Michie 2000) (entered effect April 3, 1989); N.D. CENT. CODE Sections 47-25.1-01 to -08 (2000) (entered effect July 1, 1983); OHIO REV. CODE ANN. Section 1333.61-.69 (Anderson 2000) (entered effect July 20, 1994); OKLA. STAT. tit. 78, Sections 85-94 (1999) (entered effect Jan. 1, 1986); OR. REV. STAT. Sections 646.461-.475 (1999) (entered effect Jan. 1, 1988); R.I. GEN. LAWS Sections 6-41-1 to -11 (2000) (entered effect July 1, 1986); S.C. CODE ANN. Section 39-8-10 to -120 (1999) (entered effect May 21, 1997); S.D. CODIFIED LAWS Section 37-29-1 to -11 (Michie 2000) (entered effect July 1, 1988); UTAH CODE ANN. Section 13-24-1 to -9 (2000) (entered effect May 1, 1989); VA. CODE ANN. Sections 59.1-336 to 343 (2000) (entered effect July 1, 1986); VT. STAT. ANN. Tit. 9, Sections 4602-4609 (2000) (entered effect July 1, 1996); WASH. REV. CODE ANN. Sections 19.108.010 to .060, 19.108.900 top .940 (West 2000) (entered effect Jan. 1, 1989); W. VA CODE ANN. Sections 44-22-1 to -10 (Michie 2000) (entered effect July 1, 1986); WIS. STAT. Sections 134.90 (1999) (entered effect April 24, 1986).

<sup>26</sup> Compare, e.g., Yuan Cheng, *Legal Protection of Trade Secrets in the People's Republic of China*, 5 PAC. RIM L. & POL'Y J. (1996); with Anuja Rajbhandary, *Protecting Trade Secrets Through Family Businesses: A Case Study on Nepal*, 16 INT'L REV. L. & ECON. 483 (1996).

<sup>27</sup> For example, the Czech and Slovak Republics have enacted trade secret laws closely following the Uniform Act. See Jennifer Felicia Swiller, *The Secrets of Success: Confidential Business Information in the Czech and Slovak Republics*, 7 TRANSNAT'L LAW 497, (1994).

using language very similar, if not identical in some respects, to the Uniform Act.<sup>28</sup> Other than the Agreement, there are no international treaties concerning the protection and exploitation of trade secrets. The lack of international treaties may not be surprising because modern trade secrets law is still new and developing. However, this may change someday. Governments of industrial countries with multinational businesses engaged in transnational transactions and foreign governments of less developed countries which desire to promote investments in their country all have good reasons to seek the international protection of trade secrets.

### **III. The Virginia Uniform Trade Secrets Act**

The Virginia Act regulating trade secrets does not violate the U.S. Constitution. While patents, trademarks and copyrights are regulated by federal law, the Court of Appeals for the Fourth Circuit has found that state regulation of trade secrets does not violate the supremacy clause. In *Sears v. Gottschalk*,<sup>29</sup> relying on *Kewanee Oil v. Bicron Corp.*,<sup>30</sup> the Court concluded that “... the states may protect trades secrets, and we perceive no violation of the fifth amendment in federal forbearance to permit that power to be exercised.”

#### **A. Definition of “Trade Secret”**

Commentators of the First Restatement clearly recognized that “an exact definition of a trade secret is not possible.”<sup>31</sup> In recognition of this difficulty, the Uniform and Virginia Act’s definition of a trade secret is not specific. In Section 59.1-336 of the Virginia Act, a trade secret is defined as “information, including but not limited to, a formula, pattern, compilation, program,

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<sup>28</sup> The U.S. is a signatory to the Agreement on Trade Related Aspects of Intellectual Property Rights, April 15, 1994, 33 I.L.M. 1197, 1212 (entered into force January 1, 1995). Article 39 of this Agreement requires the United States and other signatories to provide legal protection for undisclosed information of private parties when disclosed or used contrary to “honest commercial practices.” Since the uniform trade secret acts of the various states of the United States are state and not federal law, United States compliance with the Agreement is based on state, not federal, law.

<sup>29</sup> 502 F.2d 122, 132 (4th Cir. 1974).

<sup>30</sup> 416 U.S. 470, 485 (1974).

<sup>31</sup> See, Restatement of Torts, § 757, cmt b.

device, method, technique or process.”<sup>32</sup> Obviously, this definition is very broad and is very similar to the definition found in the First Restatement which defined a trade secret as any “formula, pattern, device or compilation of information used in one’s business, and which gives him an opportunity to obtain an advantage over competitors who do not know or use it”.<sup>33</sup>

It is significant to note that the Virginia Act’s, the Uniform Act’s and the First Restatement’s definition do not only cover high tech secrets. In fact in the case law in Virginia, the Virginia Act is frequently used to protect “low tech” secrets. Some common examples of low-tech trade secrets in published cases are: customer lists<sup>34</sup>, pricing information<sup>35</sup>, business leads, financial information<sup>36</sup>, marketing strategies, sales techniques, methods of conducting business<sup>37</sup> and even artwork<sup>38</sup>. The definitions of trade secrets in the Virginia Act, Uniform Act and the Restatement are significant in several other respects as well. These definitions do not require that the information exist in some tangible format, as is the case in patent law. It can be a computer file<sup>39</sup>. In fact, the information need not be more than an idea, theory or concept. Further, these definitions do not require that the trade secret be novel.<sup>40</sup> Several courts have stated that novelty is not a requirement for a trade secret but that maintaining its secrecy is necessary.<sup>41</sup> In addition, there is no requirement of continuous use of

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32 The Uniform Act does not contain the words “but not limited to.” Illinois, Maine and West Virginia have added the same phrase as Virginia. Compare Alabama, which requires that information specifically fit within one of its designated categories.

33 *Supra* note 40.

<sup>34</sup> *American Sales Corp. v. Adventure Travel, Inc.*, 862 F.Supp. 1476 (E.D. Va. 1994); *Alan J. Zuccari, Inc. v. Adams*, 42 Va. Cir. 132 (Fairfax 1997); *Physicians Interactive v. Lathian Sys.*, -- F.Supp. --, 2003 U.S. Dist. LEXIS 22868 (E.D. Va. 2003).

<sup>35</sup> *Int’l Paper Co. v. Gilliam*, -- Va. Cir. --, 2003 Va. Cir. LEXIS 249 (Roanoke Dec. 23, 2003).

<sup>36</sup> *Eden Hannon & Co. v. Sumitomo Trust & Banking Co.*, 914 F.2d 556 (4<sup>th</sup> Cir. 1990).

37 *See Religious Tech. Ctr.*, 897 F.Supp. 260.

<sup>38</sup> *Reynolds & Reynolds Co. v. Hardee*, 932 F.Supp. 149 (E.D. Va. 1996).

<sup>39</sup> *Avtec Sys. Inc. v. Peiffer*, 805 F.Supp. 1312 (E.D. Va.), *aff’d in part and vacated in part*, 21 F.3d 568 (4<sup>th</sup> Cir. 1994).

40 *Sperry Rand Corp. v. Electronic Concepts, Inc.*, 325 F.Supp. 1209; *Avtec Sys. v. Peiffer*, 21 F.3d 568 (4<sup>th</sup> Cir. 1994); *Dionne v. Southeast Foam Converting & Packaging*, 240 Va. 297 (1990); and *Kewanee Oil Co. V. Bicron Corp.*, 416 U.S. 470, 181 USPQ 673 (1974).

41 *See Avtec Sys. v. Peiffer*, 21 F.3d 568 (4<sup>th</sup> Cir. 1994); *Dionne*, 390 S.E.2d 110; and *Kewanee Oil Co.*, 416 U.S. 470.

the trade secret in business or even any use at all (unlike the definition of trade secret in the First Restatement). This protects the trade secret of an owner who has not yet begun business, not yet had the opportunity or acquired the means to put the trade secret to use, has temporarily stopped use or has determined that the secret process or method does not work and wants to protect that negative information as a trade secret. While patents may be protected by statute for twenty years, trade secrets may be protected as long as their secrecy is maintained, they are not generally known and they are not readily ascertainable. The Virginia Act and the Uniform Act do not require a profit motive for the misappropriation.<sup>42</sup>

Significantly under the Virginia Act, the Uniform Act and the Restatement, the right to a trade secret, unlike patent law, need not be exclusive. It seems that this concept has been accepted from the very beginning of trade secret case law. Even the 1851 English case of *Morison v. Moat*<sup>43</sup> refers to the non-exclusivity of trade secrets. By non-exclusivity it is meant that two entities, which concurrently but independently develop the same trade secret, may both acquire rights to it. Thus, a business in Roanoke, Virginia may develop a technique to produce multiple clones of a renowned Virginia law professor in order to provide uniform legal instruction throughout the Commonwealth. That business may seek to protect that technique as a trade secret. Another business in Fairfax, Virginia may subsequently and independently develop the very same technique<sup>44</sup> and also seek to protect it as a trade secret. The Fairfax company's acquisition, use and disclosure of that technique is not a violation of the Roanoke company's trade secret and both companies can protect their secret. If at some point, however, the secret becomes known to more and more people to the point of becoming generally known, as discussed below, the right to protect the secret is lost. Similarly, if the secrecy of the trade secret is not maintained or if the trade secret becomes readily ascertainable, as discussed below, the right to protect the secret is lost.

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<sup>42</sup> See *Am. Sales Corp. v. Adventure Travel, Inc.*, 862 F. Supp. 1476 (E.D. Va. 1994). See also *Am. Sales Corp. v. Adventure Travel, Inc.*, 867 F. Supp. 378 (E.D. Va. 1994).

<sup>43</sup> 68 Engl. Rep at 500, 9 HARE at 259.

<sup>44</sup> Assume that the differences in linguistic style and sartorial resplendence between the Roanoke and Fairfax clones are unrelated to the cloning technique itself and the technique to create both versions of the clones is the same for both versions.

In many, if not most, trade secret cases, the size of the trade secret is not a factor in the case since the trade secret at issue is specific, singular and limited, such as a manufacturing process<sup>45</sup>, computer software,<sup>46</sup> source code, object code<sup>47</sup>, new technology<sup>48</sup>, or customer or patient list.<sup>49</sup> However, many trade secret owners would like to maximize the amount of information they can protect from departing and competing employees. Franchisor/franchisee trade secret cases can be illustrative. They sometimes involve large amounts of information, even whole franchise systems. In *ServiceMaster v. Pletcher*,<sup>50</sup> ServiceMaster, a large national franchisor of cleaning businesses claimed its whole “Business System” was a trade secret. ServiceMaster required its franchisees to use this Business System to conduct their cleaning business. This Business System was comprised of dozens of three inch, three ring manuals, altogether consisting of thousands of pages of text and numerous video tapes. The Business System also consisted of numerous periodic magazines and newsletters, technical bulletins, training materials, training seminars, workshops, promotional materials, advertising materials, marketing materials, sales materials, invoices, and even correspondence with third parties. These materials covered virtually every aspect of forming, operating and maintaining a cleaning business. These materials not only covered how to clean things but also how to keep business books and records, run an office and even first aid. See also, *Precision Tune Auto Care, Inc. v. Pinole Auto Care, Inc.*,<sup>51</sup> *Big O Tires, Inc. v. Granada Enterprises Corp., et al.*,<sup>52</sup> and *Gold Messenger, Inc. v. McGuay*<sup>53</sup>

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<sup>45</sup> *Dionne v. Southwest Foam Converting & Pkg.*, 240 Va. 297 (1990), compressed packaging material.

<sup>46</sup> *Avtec Sys. Inc. v. Peiffer*, 805 F.Supp. 1312 (E.D. Va.), aff’d in part and vacated in part, 21 F.3d 568 (4<sup>th</sup> Cir. 1994).

<sup>47</sup> *Trandes Corp. v. Guy F. Atkinson Co.*, 996 F.2d 655 (4<sup>th</sup> Cir.1993), regarding software to dig tunnels.

<sup>48</sup> *Swedish Civil Aviation Admin. V. Project Mgmt. Enter., Inc.*, 190 F.Supp.2d 785 (D.Md. 2002), regarding new technology to transmit aircraft location.

<sup>49</sup> *American Sales Corp. v. Adventure Travel*, 862 F. Supp. 1476, 1481 (E.D. Va. 1994).), regarding a list of customers.

<sup>50</sup> Civil Action No. 00-942-A in the US District Court for the Eastern District of Virginia. There is no confidentiality clause in the Settlement Agreement and Mutual Release executed in this case.

<sup>51</sup> -- F.Supp.2d --, 2001 U.S. Dist. LEXIS 24840 (E.D. Va. Oct. 15, 2001). Former franchisee retained and refused to return trade secrets in franchisor policy and procedure manual after franchise agreement terminated.

<sup>52</sup> Business Franchise Guide (CCH) Paragraph 11, 607 (C.D. Cal. 1990), Case No. CV98-2298DT. The Court upheld plaintiff’s claim that its whole “Big O System”, comprised of “techniques, systems, details as to the Big O system, theory and practices, supplier lists, equipment standards, specials uses of equipment and equipment supplier lists” is a trade secret.

<sup>53</sup> 937 P.2d 907 (Ct. App. Co. 1997). A franchisor developed a comprehensive system for setting up and operating an advertising circular business. This system was compiled in an apparently voluminous manual. Plaintiff sought to enforce its written covenant not to compete against defendant in Colorado which statutorily voided such agreements unless it is to

Such broad systems can be put on a website which is password protected, available only to franchisees. Not only does this dramatically reduce the cost of assembling and distributing the alleged trade secret, it also allows the franchisor to argue that they have taken reasonable measure to maintain the secrecy of such a large body of information.

There are substantial legal arguments to support the interpretation that all of such information should be protected as a trade secret. The statute itself defines a trade secret as any “information.” The statute does not set forth any limitation on the amount of information which may be a trade secret. Further, the statutory definition specifically provides that “compilations” can be trade secrets. There is a great deal of case law that stands for the proposition that compilations and combinations of even generally known information, readily ascertainable information or both, can be a trade secret. In *Comprehensive Tech. v. Software Artisans*,<sup>54</sup> the Court stated “...although a trade secret can not subsist in information in the public domain, it can subsist in a combination of such information, as long as the combination is itself secret.” (Emphasis in original.) In *Motor City Bagels, LLC v. American Bagel Co.*<sup>55</sup> the court found that a business plan was a trade secret even though the business plan contained some facts ascertainable from the market place and some public information. In this case, two recent MBA’s were investigating and negotiating the purchase of a bagel franchise and prepared an extensive business plan assessing the viability of a bagel franchise. The franchisor with whom they were negotiating disclosed the plan to other prospective franchisees. The court held that while the business plan at issue did contain some public information and facts ascertainable from the marketplace, it likewise included personal insights and analysis brought to bear through diligent research and by marshaling a large volume of information. The Court found that an attempt to independently duplicate the plaintiff’s efforts would be an onerous task. While the Maryland Act is clear that information that is generally known or readily ascertainable can not be a trade secret, combinations of generally known information, combinations of readily ascertainable information and combinations of both, can be trade secrets.

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protect a trade secret.<sup>53</sup> The Court held that the whole manual was a trade secret.

<sup>54</sup> 3 F.3d 730 (4<sup>th</sup> Cir. 1993); see also, *Avtec Sys. Inc. v. Peiffer*, 805 F.Supp. 1312 (E.D. Va.), aff’d in part and vacated in part, 21 F.3d 568 (4<sup>th</sup> Cir. 1994).

<sup>55</sup> 50 F. Supp. 2d. 460 (D.Md. 1999)

In the Federal Circuit in *BBA Nonwovens Simpsonville, Inc. v. Superior Nonwovens, LLC*<sup>56</sup>, BBA Nonwovens, and other manufacturers brought an action against a competitor, Superior Nonwovens, alleging trade secret misappropriation and patent infringement as a result of Superior's manufacture of certain spunbond nonwoven fabric. After a jury trial in favor of the Plaintiffs, the Defendants appealed arguing that because most, if not all of the elements of the Plaintiffs' process were in the public domain, they could not be considered a trade secret. The Federal Circuit rejected that argument instead following the widely held rule that "a trade secret can exist in a combination of characteristics and components, each of which, by itself, is in the public domain, but the unified process, design and operation of which, in unique combination, affords a competitive advantage and is a protectable trade secret." Thus, by combining or compiling information, the amount of information that can be protected as a trade secret can be maximized.

Alternatively, there are legal arguments to challenge such a broad interpretation of the amount of information that may be considered a trade secret. It is a well recognized public policy in Virginia<sup>57</sup> and other local jurisdictions<sup>58</sup> to permit the free mobility of employees. Nearly forty years ago one court said:

[a]n employer who discloses valuable information to his employee in confidence is entitled to protection against the use of these secrets in competition with him. But the employee who possesses the employer's most valuable confidences is apt to be highly skilled. The public is interested in the reasonable mobility of such skilled persons from job to job in our fluid society, which is characterized by and requires mobility of technically expert persons from place to place, from job to job and upward within the industrial structure. And the employee himself must be afforded a reasonable opportunity to change jobs without abandoning the ability to

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<sup>56</sup> 303 F.3d 1332 (Fed. Cir. 2002) (Applying SC law).

<sup>57</sup> *County of Giles v. Wines*, 262 Va. 68 (2001); *Town of Vinton v. City of Roanoke*, 195 Va. 881 (1954).

<sup>58</sup> *Szaller v. Am. Nat'l Red Cross*, 293 F.3d 148; *Parker v. Penske Truck Leasing Corp.*, 18 Fed. Appx. 148.

practice his skills.<sup>59</sup>

A broad interpretation of the scope of trade secret protection can effectively interfere with this public policy of free mobility of employees. If the volume of information alleged to be a protectable trade secret is large, it may mean that an employee can not leave his job to continue to work in the same industry since the employee will necessarily use or disclose trade secret information of his previous employer. It is also a well recognized public policy to allow an employee to depart employment with general knowledge and skills. A broad interpretation of the scope of trade secret protection can effectively interfere with this public policy as well.

Significantly, such a broad interpretation can also arguably result in a constructive and an unlawful prohibition on competition. As noted above, the Virginia Act does not have any geographic or temporal limit on the protection of a trade secret. In order for a non-compete agreement to be enforceable in Virginia, it must have reasonable limitations as to the breath of the activity being restricted, time and geography.<sup>60</sup> In practice, the protection of a large volume of information could function as the equivalent of an unlawful non-compete agreement without reasonable restraints on time or geography. In the case of the protection of a large volume of information, an employee can not reenter his business, trade or profession since virtually everything that the departing employee would do would disclose or utilize the information in the voluminous alleged trade secrets of the employer.

## **B. Definition of Misappropriation**

Section 59.1-336 of the Code of Virginia defines misappropriation as follows:

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

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<sup>59</sup> *Standard Brands Inc. v. Zumpe*, 264 F.Supp. 254, 259 (E.D. La. 1967)

<sup>60</sup> *Simmons v. Miller*, 261 Va. 561, 544 S.E.2d 666 (2001).

- a. Used improper means to acquire knowledge of the trade secret; or
- b. At the time of disclosure or use, knew or had reason to know that his knowledge of the trade secret was
  - (1) Derived from or through a person who had utilized improper means to acquire it;
  - (2) Acquired under circumstances giving rise to a duty to maintain its secrecy or limit its use;
  - (3) Derived from or through a person who owed a duty to the person seeking relief to maintain its secrecy or limit its use; or
  - (4) Acquired by accident or mistake.

The United States District Court for the Eastern District of Virginia, Alexandria Division, has addressed the issue of whether the mere acquisition of a trade secret of another by improper means is a misappropriation under the Virginia Act. In the case of *Smithfield Ham and Products Company, Inc. v. Portion Pac, Inc.*,<sup>61</sup> the Court held that mere acquisition is sufficient, explaining its holding by applying property theory to justify the protection of the trade secrets:

[T]he VUTSA [Virginia Uniform Trade Secrets Act] prohibits the improper acquisition of a trade secret, whether or not the trade secret is used in direct competition with the rightful owner. Va. Code Ann. Section 59.1-336; *see Trandes Corp. v. Guy F. Atkinson Co.*, 996 F.2d 655, 665 (4th Cir.) (interpreting the Maryland UTSA, and citing cases) cert. denied, 114 S.Ct. 443, 126 L.Ed.2d 377 (1993). This is so because the value of the trade secret as an asset of the company is diminished by its disclosure, whether or not the person acquiring it uses it competitively.

“Improper means” is a critical term used in this definition of misappropriation. It is defined in Section 59.1-336 of the Virginia Act as “theft<sup>62</sup>, bribery, misrepresentation, breach of a duty or

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61 905 F.Supp. 346 (E.D.Va. 1995).

<sup>62</sup> *E.I. DuPont de Nemours & Co. v. Christopher*, 431 F.2d 1012 (5<sup>th</sup> Cir. 1970), holding that aerial photography of plant construction to determine competitor’s process for producing methanol constituted “Improper means.”

inducement of a breach of a duty to maintain secrecy, or espionage through electronic or other means.” There is no actionable misappropriation if the trade secret is acquired by proper means.<sup>63</sup> In *Scheduled Airlines Traffic v. Objective*<sup>64</sup>, a provider of travel management services (SATO), contracted with Objective, to produce a software system to assist SATO in providing travel management services to its prospective customers. In the contract, Objective granted SATO “the right and license to use, reproduce, sublicense, prepare derivative works, distribute copies, publicly perform and display such Proprietary Components for use in connection with the [software] System. SATO paid Objective in full for the software. Objective did not, however, complete the work in full. As a result of uncorrected defects in Objective’s software, SATO never used the Objective programmed software, but instead constructed its own system using a different programming tool. Objective claimed that this was a misappropriation of its trade secrets by SATO. The court, however, concluded that Objective contractually granted SATO unrestricted permission to use its software system via the following provision: “Developer hereby assigns and conveys to Customer all of Developer’s proprietary rights in and to the System and all “System Updates” and “System Enhancements.”” In addition, Objective agreed in the contract to execute any documents required to evidence SATO’s ownership of trade secrets in the System. Under the terms of the contract, therefore, there was no misappropriation by SATO since there was no acquisition by improper means.

Also, the Virginia case of *Peace v. Conway* is frequently cited for the proposition that it is not an “improper means” to memorize something.<sup>65</sup> This probably should be taken with a grain of salt.

In the absence of an agreement to the contrary, after the termination of employment, an employee may use general information concerning the method of business of the employer and the names of the employer’s customers retained in his or her memory, if not acquired in violation of any duty to the employer.

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<sup>63</sup> For a discussion of proper means, see Section III.E of this Outline.

<sup>64</sup> 180 F.3d 583 (4<sup>th</sup> Cir. 1999).

<sup>65</sup> 246 Va. 278, 435 S.E.2d 133 (1993).

In the case of an employee who has misappropriated a trade secret from his former employer, such an employee's new employer may be vicariously liable for the employee's misappropriation of a trade secret of the former employer under the doctrine of respondeat superior.<sup>66</sup>

### **C. Requirement of Independent Economic Value**

The definition of a trade secret in the First Restatement requires that the trade secret gives the user an opportunity to obtain an advantage over nonusers. The Virginia Act's definition of a trade secret requires that the secret information derive "independent economic value, actual or potential." This quoted phrase as used in the Virginia Act and the Uniform Act, while seemingly unfathomable, has been interpreted by courts to simply mean that the trade secret information must give the owner of the secret some actual or potential competitive advantage.<sup>67</sup> The Virginia and Uniform Acts do not state that the independent economic value has to be substantial or significant, but the economic value has to be more than *de minimis*.

Usually, proving this element is not an issue. However, it was an issue in the recent Maryland case of *Padco Advisors, Inc. v. Omdahl*<sup>68</sup>. The plaintiff mutual fund company fired Defendant, a regional sales manager, who went to a competing company. Plaintiff sued Defendant for violation of the Maryland Uniform Trade Secrets Act alleging he memorized a list of registered investment advisors compiled by his former employer. He did not physically copy the list. Plaintiff obtained a TRO and preliminary injunction, lasting two years until the final court decision. The court found in the case that where the information had been memorized and over two years had past since he had been fired, it was doubtful that the Defendant would remember anything useful. The court found that the information on the list was constantly changing. There was testimony that the two year old list had substantially changed. The court held that the list was not a trade secret because plaintiff had not shown any continued value to competitors.

### **D. Requirement That Trade Secret Not Be Generally Known**

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<sup>66</sup> *Newport News Industrial v. Dynamic Testing, Inc.*, 130 F.Supp.2d 745 (2001).

<sup>67</sup> *ElectroCraft Corp. v. Controlled Motion, Inc.*, 332 N.W.2d 890, 900 (Minn. 1983).

<sup>68</sup> 179 F.Supp.2d 600 (D.Md. 2002).

The Virginia Act's definition of a trade secret further requires that the trade secret not be generally known. The drafters of the Uniform Act and the courts are clear that "not generally known" does not mean not generally known to the public. It means not generally known to those who are in the relevant industry or trade.<sup>69</sup> In trade secrets cases, this requirement that the information not be generally known is often a vigorously contested issue and it can be a close factual issue for a judge or jury to decide. For example, consider whether a particular method of selling a product or service is or is not generally known. A company may argue that it has developed a secret method of selling a product or service on which it has spent much money, time and effort to develop its particular sales method, train its employees to use it and maintain the secrecy of the method. On the other hand, a departing employee of that company who wants to use the method for her own benefit may argue that the method is most certainly generally known since you can simply read a book at your local public library on sales or marketing to find out about almost any sales method. Further, a departing employee may also contend that the sales method is generally known since several of the competitors of the company use the same or similar method. This is not unlikely in a mature competitive industry.

One way to make something generally known is to post it on the Internet. It is surprising how frequently companies post critical information on their website. Courts have held that posting works to the Internet makes them generally known. Once a trade secret is posted on the Internet, it is effectively part of the public domain and impossible to retrieve.<sup>70</sup> The case of *Religious Technology Center v. Lerma*,<sup>71</sup> is a very interesting case factually. In 1991, RTC (Church of Scientology) sued Fishman, a disgruntled former member, who then filed embarrassing Church documents in the open court file. That court refused to seal these documents until August 15, 1995. Before the documents were sealed, Lerma published them on the Internet and mailed them to *The Washington Post*. On August 14, 1995, one day before they were sealed, the *Post* also sent a reporter to the Fishman court and obtained a copy of the documents from the open court file even though the Church had been

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69 Unif. Trade Secrets Act, § 1, 14 U.L.A. at 439 cmt.

<sup>70</sup> *Religious Technology Center v. Lerma*, 908 F.Supp. 1362 (E.D. Va. 1995); 37 U.S.P.Q.2d 1258.

<sup>71</sup> *Id.*

checking the file out and holding it all day, every day, so no one could see it. The file was not sealed at that time. The *Post* published an article about the Church and documents. The Church sued the *Post* for copyright infringement and trade secret misappropriation. The Court found that the documents could not be trade secrets since they were in an open court file for over 28 months and therefore in the public domain. They were also published on the Internet for ten days. The court found that the person originally posting the documents to the Internet may have misappropriated them but the party downloading them from the Internet can not be liable for misappropriation.

You would think that another way to make something generally known is to make it public by putting it in the court record. In the case of *Hoechst Diafoil Co. v. Nan Ya Plastics Corp.*,<sup>72</sup> the U.S. Court of Appeals, Fourth Circuit, took a different position with regard to trade secrets filed in an open court file but not posted on the Internet. In that case, a party had filed documents, which they alleged were trade secrets, in another court proceeding. They had been in the open court file for several months. The U.S. Court of Appeals, Fourth Circuit, reached a result different than the court in the Scientology case, stating:

In holding that the [Church's] works were not trade secrets when the *Post* acquired them, the court specifically relied on both of these factors [documents in an open court file for 28 months and published on the Internet]. First, it noted that the documents' extended presence in the court's public files, from which the *Post* had obtained its own copy, made them no longer a secret. Importantly, though, the court reasoned that the documents' posting on the Internet was "[o]f even more significance" than their extended presence in public records: "posting works to the Internet makes them "generally known" at least to the relevant people interested in the news group." As a result, the court correctly found that the information which had been both disclosed in public court files and made "generally known" by Internet publication had lost its trade secret status. In this case, there is no suggestion that the ... [d]ocument was published [on the Internet], only that it was present in the district court's public files. We hold that, under the Act, this presence in the district court's public files, in and of itself, did not make the information contained in the document "generally known" for purposes of the Act.<sup>73</sup>

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<sup>72</sup> 174 F.3d 411 (4th Cir. 1999).

<sup>73</sup> *Id.*

### **E. Requirement That Trade Secrets Not Be Readily Ascertainable**

The Virginia Act also requires that a trade secret not be readily ascertainable by proper means.

Improper means are defined in the Virginia Act and the Uniform Act and have already been discussed.<sup>74</sup> The Commentary to the Uniform Act lists several proper means<sup>75</sup>, including:

1. Discovery by independent invention;
2. Reverse engineering;<sup>76</sup>
3. Discovery under a license;
4. Observing the product or service on public use or display; and
5. Review of publicly available literature. <sup>77</sup>

Like the Virginia Act's related requirement that a trade secret not be generally known, there is no line in the sand as to when information is readily ascertainable. This is also a factual issue which is often litigated. A common example in trade secret litigation is the case of a departing employee who takes the customer list with him when he departs to work at a competing business, which may even be the employee's own start-up company. The former employer of the departing employee will argue that its customer list was developed only after many years of effort and great expenditures on advertising, client development and salaries. On the other hand, the departing employee, who has appropriated the list, will argue that the list constitutes information which is readily ascertainable through common business sources such as telephone books, trade magazines, published industry information sources, etc.

The nature of this requirement was simply but eloquently described in the 1922 case of *Fulton Grand Laundry Company v. Edward Johnson*.<sup>78</sup> Apparently in 1922 laundry was picked up and delivered by horse drawn carriage. Since this was the case, the location of the laundry was unimportant but the laundry route, the identity and location of the customers, was critical. A laundry

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<sup>74</sup> See, Section III. B; Unif. Trade Secrets Act, § 1, 14 U.L.A. 439.

<sup>75</sup> Uniform Trade Secrets Act, Section 1, 14 U.L.A. 439 (1990) Commissioners' Comment.

<sup>76</sup> *Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470, 475 (1974).

<sup>77</sup> Unif. Trade Secrets Act, § 1, 14 U.L.A. 439 cmt. (1990). *Tao of Sys. Integration, Inc. v. Analytical Servs. & Materials, Inc.*, 299 F.Supp.2d 565, 2004 U.S. Dist. LEXIS 313 (E.D. Va. 2004), where motion to dismiss granted where alleged trade secrets were information contained in published patent.

<sup>78</sup> 140 Md. 359, 117 A. 753, 23 A.L.R. 420 (1922).

carriage driver departed from his employer and started his own laundry business. He solicited the customers of his previous laundry route. The Court found that the identity and location of the laundry customers on the laundry route was not a trade secret since those identities and locations could be readily ascertained by merely observing the driver on his laundry route.

Some trade secret cases dealing with the issue of whether a trade secret is readily ascertainable are reverse engineering cases. The U.S. District Court for the Eastern District of Virginia recently decided the reverse engineering case of *DSC Communications Corporation v. Pulse Communications, Inc.*<sup>79</sup> In this case a manufacturer of plug-in channel cards for use in a telecommunications digital switching system lawfully purchased, through an agent, a competitor's system on the open market with the specific intent to reverse engineer the card. The Court held that since the card was purchased lawfully, the trade secret was not obtained by improper means as defined in the Virginia Act, even though it was purchased with the intent to reverse engineer the card and even though it was purchased indirectly through an agent.

#### **F. Requirement of Reasonable Efforts to Maintain Secrecy**

Section 59.1-336 of the Virginia Act provides that a trade secret is protectable only if it "...is the subject of efforts that are reasonable under the circumstances to maintain its secrecy."<sup>80</sup> There are no qualifications or exceptions to this requirement. However, it is also clear from this provision that complete secrecy is not required. Sensibly, trade secret protection is not lost if the trade secret is disclosed in confidence to those that need to know it, such as employees, agents, suppliers, subcontractors and others.<sup>81</sup> However, courts have also interpreted the Act to require that a trade secret owner demonstrate that he pursued an active course of conduct to keep the information secret.<sup>82</sup> Doing nothing is not enough, even though doing nothing has been good

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<sup>79</sup> 976 F.Supp. 359 (E.D. Va. 1997).

<sup>80</sup> Unif. Trade Secrets Act, §1(4) (ii), 14 U.L.A. 439; *Secure Serv. Tech., Inc. v. Time & Space Processing, Inc.*, 722 F.Supp. 1354 (E.D. Va. 1989).

<sup>81</sup> *Dionne v. Southwest Foam Converting & Pkg.*, 240 Va. 297 (1990), citing *Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470, 475 (1974).

<sup>82</sup> *Jet Spray Cooler, Inc. v. Crampton*, 282 N.E.2d 921, 925 (Mass. 1972)

enough in the past to protect the secret. While the trade secret owner must be able to demonstrate that he has pursued an active course of conduct to protect the secret, the trade secret owner need not take heroic measures.

Generally speaking, if trade secret information is disclosed to outsiders or the public, trade secret protection is lost. In *Advanced Computer Services v. MAI Systems*,<sup>83</sup> the court simply stated the basic concept: “[t]rade secrets rights do not survive when otherwise protectable information is disclosed to others, such as customers or the general public, who are under no obligation to protect [its] confidentiality...”<sup>84</sup>

Sometimes in early trade secret cases courts held that not much is required to protect the information as a trade secret. In *Dionne*,<sup>85</sup> cited above, the Virginia Supreme Court upheld the Circuit Court’s decision that the company had used reasonable efforts to maintain the secrecy of the trade secret, referring only to the fact that the company had required confidential information agreements from all its “employees, suppliers, customers, contractors and other plant visitors...”<sup>86</sup>

However, in many cases, a court will look much more closely at the facts of the case. In a Fourth Circuit case, the Court closely looked at the facts to determine if reasonable efforts were employed to maintain secrecy. In *Trandes Corporation v. Guy F. Atkinson Co.*,<sup>87</sup> the developer and owner of a software program, used to design subway tunnels, sued a licensee and its contractor, the Washington Metropolitan Area Transit Authority, for misappropriation of that trade secret. The defendants argued that the information was not a trade secret since the software was widely disclosed, mass marketed and its existence and its abilities were not secret. The defendants argued that the plaintiff software owner even offered a demonstration version of

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<sup>83</sup> 45 F.Supp. 356 (E.D. Va. 1994).

<sup>84</sup> *Id.*, p. 370, citing *Secure Services Tech., Inc. v. Time and Space Processing, Inc.*, 722 F.Supp. 1354, 1361 (E.D. Va. 1989).

<sup>85</sup> 397 S.E.2d 110.

<sup>86</sup> *Id.* at 300.

<sup>87</sup> 996 F.2d 655, certiorari denied 114 S.Ct. 443, 126 L.Ed.2d 377.

the software for sale for \$100. However, the Court looked closely at the facts, found that only six or seven persons inquired about the demonstration version and none were sold. In deciding the case, the Court found that the owner took measures that were reasonable under the circumstances to protect the secrecy of the software. The Court found that the company licensed only two object code versions of its software and they were licensed under a confidentiality agreement, the company used a password to prevent access to the program in-house and for licensed versions and there was no other unauthorized person who had ever obtained a copy of the software.

Of course, efforts that are reasonable under the circumstances will vary from case to case. Some examples include:

1. Classifying and labeling certain documents as trade secrets;
2. Restricting access to certain materials or areas;
3. Limiting disclosures within the company only to those individuals who need the trade secrets in order to perform their jobs properly;
4. Implementing badge or other electronic monitoring systems;
5. Advising employees of the existence of trade secrets and conditioning employment on signing confidentiality agreements;
6. Requiring consultants, customers, vendors, and ancillary service providers to sign confidentiality agreements;
7. Implementing periodic internal review procedures regarding inventions, periodicals, marketing materials, and government filings;
8. Restricting access to computers, copiers, fax machines, and trash receptacles;
9. Performing security checks of employees, visitors, and others with access to trade secrets; and
10. Using protective orders when disclosing trade secrets in the course of litigation.

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There is much for a lawyer to do here to advise and assist his clients. Today's numerous trade secret law suits are *ad hoc* testimonials to the fact that many companies still do not take measures that are reasonable under the circumstances to protect their trade secrets. A trade secret owner should consider the implementation of a trade secret protection program, designed by counsel, to protect such secrets from disclosure and to increase the owner's probability of

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88 Cohen & Gutterman, *supra* note 11 at 89-90.

success in future litigation involving the misappropriation of the secret.<sup>89</sup>

## **G. Other Provisions of the Act**

### **A. Injunctive Relief**

Because of the nature of trade secrets cases, money damages may be inadequate and injunctive relief may be necessary. In recognition of this, Section 59.1-337 of the Virginia Act specifically provides that a court may order an injunction in the case of actual or threatened misappropriation.<sup>90</sup> The court order imposing the injunction can specify that the injunction shall terminate when the trade secret has ceased to exist. However, the court may continue the injunction for an even longer period in order to eliminate any commercial advantage that otherwise would be derived from the misappropriation. It is notable that even threatened misappropriation is the proper subject of an injunction under both Acts. In Virginia, courts have already upheld the use of the Virginia Act to enjoin threatened misappropriation. In *Dionne*, cited above, the court granted an injunction against the misappropriating son, prohibiting him from the threatened use or disclosure of the secret manufacturing process.

As a significant consequence of the provision of the Act authorizing an injunction, the plaintiff will not have to prove irreparable injury or inadequacy of money damages to obtain an injunction as might otherwise be required for injunctions in Virginia. Virginia case law clearly stands for the proposition that where a statute specifically authorizes an injunction, the moving party does not have to prove irreparable injury or inadequacy of money damages.<sup>91</sup> The moving party will only have to show that there has been actual or threatened misappropriation.

As noted above, in 1985 the Commissioners adopted various amendments to the Uniform Act. One

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<sup>89</sup> See Richard C. McCrea, Jr., *Protecting Trade Secrets & Confidential Business Information (with Forms)*, 44 PRAC. LAW. 71 (1998).

<sup>90</sup> *Zuccari v. Adams*, 42 Va. Cir. 132 (Fairfax 1997); *Motion Control Sys. V. East*, 262 Va. 33, 546 S.E.2d 424, 2001 Va. LEXIS 72 (2001).

<sup>91</sup> *Env'tl. Def. Fund, Inc. v. Lamphier*, 714 F.2d 331 (4th Cir. 1983); *Hart v. Riverside Hosp., Inc.*, 899 F.Supp. 264 (E.D. Va. 1995); and *Virginia Beach S.P.C.A., Inc. v. S. Hampton Rds. Veterinary Ass'n*, 329 S.E.2d 10 (1985).

of those amendments was to add language to Subpart b of Section 2 of the Uniform Act concerning injunctive relief in the case of “exceptional circumstances.”<sup>92</sup> This new language was also added to the Virginia Act. The new language provides that:

(b) In exceptional circumstances, 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. Exceptional circumstances 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.

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## **B. Damages**

### **1. Actual Loss, Unjust Enrichment and Reasonable Royalty**

With regard to damages, the exact language of the Virginia Act and the Uniform Act differ somewhat. Section 3 of the Uniform Act provides that damages can include damages for actual loss and damages for unjust enrichment that is not taken into account in computing damages for actual loss. Damages can also be measured by a reasonable royalty in lieu of any other damages. In the Virginia Act, damages can be measured by actual loss or unjust enrichment as in the Uniform Act, but damages can be measured by a reasonable royalty only “[i]f a complainant is unable to prove a greater amount of damages by other methods of measurement.”<sup>94</sup> Since plaintiffs are always seeking to be awarded the highest damages, the difference in practice between the Uniform Act and the Virginia Act on this point may be small. One commentator has also argued that the Racketeer Influenced and Corruption Organizations Act (RICO) is applicable to causes of action based on the misappropriation of trade secrets.<sup>95</sup> RICO provides for treble damages and legal fees.<sup>96</sup> Virginia’s law before the Virginia Act was that damages

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92 Unif. Trade Secrets Act, Section 2(b), 14 U.L.A. 450, 456 cmt. (1990).

93 Va. Unif. Trade Secrets Act, §§ 59.1-339(B).

94 Va. Unif. Trade Secrets Act, §§ 59.1-338.

95 Thomas P. Heed, *Misappropriation of Trade Secrets: The Last Civil RICO Cause of Action That Works*, 30 J. MARSHALL L. REV. 207 (1996).

96 18 U.S.C. §1964(c).

could be awarded for plaintiff's actual loss or defendant's unjust enrichment but not both.<sup>97</sup>

Measuring damages by a royalty amount instead of actual loss or unjust enrichment may be advantageous for some plaintiffs. Plaintiffs may not be able to easily determine their own actual losses because the defendant has kept his misappropriation secret and the plaintiff may not be aware of or be able to reasonably calculate the effects of the defendant's misappropriation on plaintiff's business. Also, plaintiffs may not be able to calculate defendants' unjust enrichment because the defendant may not fully disclose the amount he has profited by the misappropriation. A royalty amount may be much easier for the plaintiff to prove since he has the information concerning the trade secret and may be already aware of its value. From a defendant's point of view, measuring damages by a royalty amount may be disadvantageous. The defendant may have only had the secret for a short time, may not have been able to use it to its full potential and not have generated much money from it because it was wrongfully obtained. Also, the defendant may not have all of the facts concerning the secret to be able to disprove the alleged value which the plaintiff attributes to the secret.

Virginia may have one of the few reported cases awarding a reasonable royalty as damages. *American Sales Corporation v. Adventure Travel, Inc.*<sup>98</sup> involves a multilevel marketing company, which previously licensed its customer list to one of its suppliers. After the supplier's contract with the multilevel marketing company terminated, the supplier took the customer list and used it to start a competing business. There was no substantial actual loss to the plaintiff since the defendant did not disclose the list to others and there was little unjust enrichment to the defendant since the defendant only had gross sales from the subject list in the amount of \$1,178. However, the Court found that the lack of significant profits did not insulate the defendant from being obligated to pay for what it had wrongfully obtained.<sup>99</sup> The Court decided to award a reasonable royalty. It

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<sup>97</sup> *American Sales Corp. v. Adventure Travel, Inc.*, 862 F.Supp. 1476 (E.D. Va. 1994) at p. 1479, citing *Sperry Rand Corp. v. A-T-O, Inc.*, 447 F.2d 1387 (4<sup>th</sup> Cir. 1971), cert denied, 405 U.S. 1017, 92 S.Ct. 1292, 31 L.Ed.2d 479 (1972).

<sup>98</sup> 862 F. Supp. 1476 (E.D. Va. 1994). See also 867 F. Supp. 378 (E.D. Va. 1994).

<sup>99</sup> 862 F. Supp. at 1479-80 (citing *Univ. Computing Co. v. Lykes-Youngstown Corp.*, 504 F.2d 518 (5<sup>th</sup> Cir. 1974)).

attempted to define a reasonable royalty as an approximation of the actual value of the infringed secret to the defendant, relying on the fiction that a license was granted at the time of the beginning of the infringement and then determining what the value of the license should have been if both parties were reasonably trying to reach an agreement.

## **2. Punitive Damages**

Under Section 59.1-338 B of the Virginia Act, a 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.” Some states do not have any punitive or exemplary damages provision in their state uniform trade secrets act.<sup>100</sup> Of those states providing for punitive or exemplary damages in their uniform trade secrets act, Virginia is the only state which sets a cap on its damage provision. As many Virginia trial lawyers know, Virginia law does not favor punitive damages and reserves them for only the most egregious conduct.<sup>101</sup>

## **3. Attorney Fees**

Section 59.1-338.1 of the Virginia Act provides that if the court determines that (i) a claim of misappropriation is made in bad faith, or (ii) willful and malicious misappropriation exists, the court may award reasonable attorneys' fees to the prevailing party.<sup>102</sup> “Willful and malicious” and “bad faith” are two different standards but the use of different standards may be appropriate since the types of acts and actors are different. However, both “bad faith” and “willful and malicious” are interpreted by the courts to require egregious conduct of a similar degree.<sup>103</sup>

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<sup>100</sup> Arkansas, Michigan, Mississippi and Nebraska do not have any punitive or exemplary damage provision in their state uniform trade secrets acts.

<sup>101</sup> *Am. Sales Corp. v. Adventure Travel, Inc.*, 862 F. Supp. 1476, 1481 (E.D. Va. 1994) (citing *Owens-Corning Fiberglass Corp. v. Watson*, 413 S.E.2d 630, 639 (Va. 1992), the court did not find the requisite willfulness and maliciousness even where the defendant's president said he wanted to “destroy” plaintiff.

<sup>102</sup> *Young Design, Inc. v. Teletronics Int'l, Inc.*, -- F.3d --, 2002 U.S. App. LEXIS 14570 (4<sup>th</sup> Cir. July 19, 2002). The Uniform Act also allows for attorney's fees if a motion to terminate an injunction is made or resisted in bad faith. The Virginia Act has no such provision.

<sup>103</sup> For egregiousness for punitive damages, see *American Sales*, 862 F. Supp. 1476 (E.D. Va. 1994). *See also* 867 F. Supp. 378 (E.D. Va. 1994). For egregiousness in bad faith cases, *see*

The *American Sales* case considered the award of attorney fees under the Virginia Act. After the plaintiff was awarded reasonable royalty damages in *American Sales*, the plaintiff sued for attorney's fees.<sup>104</sup> The Court awarded attorney's fees but refused to do so under the Virginia Act. It awarded them based on an indemnity clause in the contract between the parties. The Court refused to find the requisite willfulness and maliciousness, even though defendant's representative admitted that he wanted to "destroy" plaintiff.

#### **4. Preservation of Secrecy**

During the course of a court proceeding, Section 59.1-339 of the Virginia Act requires that a court preserve the secrecy of any alleged trade secret by reasonable means and sets forth some examples, including (1) protective orders during discovery; (2) in camera hearings; (3) sealing records; and (4) ordering persons not to disclose the information.

Of course, the parties and the court can also protect the secrecy of discoverable information under the Rules of the Supreme Court of Virginia by stipulation<sup>105</sup> and by motion for protective order.<sup>106</sup> Quite frequently in trade secret litigation, the alleged trade secrets of both plaintiff and defendant are discoverable. In such cases, counsel for both parties may negotiate, prepare and submit to the court a stipulated protective order, applicable to all parties, restricting the disclosure of information in discovery, depositions, hearings and at trial. Such protective orders may have provisions allowing: (1) limited disclosure of specified information to counsel and parties; and (2) limited disclosure of other specified information to counsel only or special masters only. In such cases, all parties have a significant interest in reaching such an agreement to protect their information and such an agreement can go a long way in minimizing legal fees and court time.

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Optic Graphics, Inc. v. Agee, 87 Md. App. 770, *cert. denied* 598 A.2d 465 (1991).

<sup>104</sup> 867 F. Supp. 378 (E.D. Va. 1994).

<sup>105</sup> Rules of the Supreme Court of Virginia, Part 4, Rule 4:4.

<sup>106</sup> Rules of the Supreme Court of Virginia, Part 4, Rule 4:1(c).

## 5. Statute of Limitations

Section 59.1-340 of the Virginia Act sets forth a statute of limitations of three years, which begins to run from the date the misappropriation is discovered or should have been discovered by the exercise of reasonable diligence. The District of Columbia and Maryland have a three year statute. Two other states have four and five year statute of limitations provisions in their uniform trade secrets acts.<sup>107</sup>

## 6. Effect on Other Law

Section 59.1-341 of the Virginia Act provides:

- (a) Except as provided in subsection (B) of this section, this chapter displaces conflicting tort, restitutionary, and other law of this Commonwealth providing civil remedies for misappropriation of a trade secret.
- (b) This chapter does not affect:
  - (1) Contractual remedies whether or not based upon misappropriation of a trade secret; or
  - (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.

The Commentary to the Uniform Act specifically states that the Uniform Act is not intended to affect the law concerning contractual provisions not to disclose trade secrets and covenants by employees not to compete against their employers.<sup>108</sup>

The scope of this “Effects on Other Law” provision has been the subject of litigation. In trade secret litigation, it is unusual that the complaint only allege a misappropriation of a trade secret. Frequently, the alleged facts support a number of causes of action, including but not limited to:

- a. Duty of loyalty;
- b. Unfair competition;

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<sup>107</sup> Illinois and Maine have a 5 and 4 year statute of limitations, respectively. Unif. Trade Secrets Act, § 6, 14 U.L.A. 462 cmt. (1990).

<sup>108</sup> Uniform Trade Secrets Act, § 7, 14 U.L.A. 463 cmt. (1990); *see also* Smithfield Ham & Prod. Co., Inc. v. Portion Pac, Inc., 905 F. Supp. 346 (E.D. Va. 1995).

- c. Lanham Act;
- d. Fraud;
- e. Constructive fraud;
- f. Waste of corporate assets;
- g. Breach of director's duty;
- h. Breach of fiduciary duty;
- i. Business conspiracy<sup>109</sup>;
- j. Tortious interference;
- k. Trade or service mark infringement;
- l. Violation of copyright;
- m. Patent infringement;
- n. Breach of contract;
- o. Unjust enrichment;
- p. Promissory estoppel; and
- q. Breach of confidentiality agreement.

Since pleading in the alternative is specifically permitted by court rule,<sup>110</sup> pleading numerous counts in trade secrets law suit has been standard practice. This practice was brought into issue in *Stone Castle Financial, Inc. v. Friedman, Billings, Ramsey & Co.*<sup>111</sup> and other recent cases.<sup>112</sup> In *Stone Castle*, the plaintiff, a California financial investment company, hired the defendant which was an investment banking firm in Alexandria, Virginia to assist the plaintiff in the purchase of a loan processing software design company to integrate loan processing software into the plaintiff 's system.. The plaintiff disclosed to the defendant information concerning the acquisition and the plaintiff's business plan to "revolutionize" the Internet mortgage industry. The defendant signed the plaintiff's confidentiality agreement. The plaintiff alleged that the defendant gave the confidential information to a competitor of the plaintiff. The competitor purchased the software design company itself. The plaintiff plead six counts in its complaint: (1) intentional interference with prospective

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<sup>109</sup> There is a very interesting and useful Virginia article on this cause of action recently published at: J. Scott Sexton, *What's In A Word? The Tortured Life of the Virginia Conspiracy Statute, VA Code Sections 18.2-499 and -500*, *Litigation News*, VSB, Vol. XI, Number 1, Spring 2004.

<sup>110</sup> VA Rule 1:4(k); MD Rule 2-303(c); and DC Rule 8(e) (2).

<sup>111</sup> 191 F.Supp.2d 652 (2002). *See also*, *Smithfield Ham and Products Co., Inc. v. Portion Pac, Inc.*, 905 F.Supp. 346 (1995); and *H.E.R.C. v. Turlington*, 62 Va. Cir. 489 (2003); *see also* *H.E.R.C. Prods. V. Turlington*, 62 Va. Cir. 489, 2003 Va. Cir. LEXIS 305 (Norfolk 2003).

<sup>112</sup> *Lucini Italia Co. v. Grappolini*, 231 F.Supp.2d 764 (N.D. Ill. 2002); *Swedish Civil Aviation v. Project Mgmt. Enter.*, 190 F.Supp.2d 785 (D.Md. 2002). *See also*, *First Union Nat'l Bank v. Steele Software Sys. Corp.*, 838 A.2d 404 (Md. Ct. Spec. App. 2003); *Brodeur & Co., CPAs, P.C. v. Charlton*, No. X04CV0101245195, 2003 WL 21214140 (Conn. Super. Ct. May 09, 2003); *H.E.R.C. Prods. V. Turlington*, 62 Va. Cir. 489, 2003 Va. Cir. LEXIS 305 (Norfolk 2003); *Callaway Golf Co. v. Dunlop Slazenger Group Am.*, 295 F.Supp.2d 430 (D.Del. 2003).

business advantage; (2) misappropriation of trade secret; (3) breach of fiduciary duty; (4) fraud; (5) breach of confidentiality agreement; and (6) conspiracy to injure business. The defendant moved to dismiss, contending that counts 1, 3, 4 and 6 were preempted by the Virginia Act because they are all predicated on the general allegation that the defendant misappropriated the plaintiff's trade secrets. The plaintiff argued that because it can not be certain that its confidential information will be found to be a trade secret, it should be able to assert alternative theories of recovery; also, it alleged some of the tort claims involved additional elements beyond those necessary to prove a misappropriation claim. The Court held that there was a "common thread" in prior case law: where courts have found preemption on a motion to dismiss, they have repeatedly established that the information at issue – as alleged - constitutes a trade secret before reaching the preemption question. "Indeed, we do not agree that the UTSA provides blanket preemption to all claims that arise from a factual circumstance possibly involving a trade secret." "...unless it can be clearly discerned that the information in question constitutes a trade secret, the Court can not dismiss alternative theories of relief as preempted by the VUTSA."

#### **IV. Conclusion**

The Virginia Uniform Trade Secrets Act was enacted just when many high tech businesses were starting up in or moving to Virginia. Twenty years after the Virginia Act's enactment, Virginia courts have decided numerous cases under the Act which have interpreted the provisions of the Act. A critical review of the Act and much of the reported Virginia trade secrets case law suggests that the Virginia Act currently meets the needs of both the high tech and non-high tech trade secret litigants for a unified and comprehensive body of law governing this subject matter area without the apparent need for substantial amendment or supplementation by the General Assembly. The increasing volume of case law under the Act reflects the continuing need for this unified and comprehensive body of law governing the protection of trade secrets. This case law also suggests that many Virginia businesses are not making efforts that are reasonable under the circumstances to maintain the secrecy of their trade secrets. Accordingly, Virginia lawyers should advise their clients as to the need for a comprehensive and demonstrable program to identify and protect trade secrets.