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TRADEMARK ATTORNEYS

Employer Precautions When Sharing Trade Secrets

Generally, a "trade secret" is any valuable business information that is kept confidential in order to give the business a commercial advantage in the marketplace. Trade secrets are valuable forms of property and thus, the owner of the secret is entitled to certain rights of exclusion and protections from disclosure. Most states have adopted the Uniform Trade Secrets Act in some form, which protects trade secrets from misappropriation, theft or disclosure without authorized consent. An individual, including a former employee, who knowingly infringes on a trade secret, may be held civilly and/or criminally liable to the owner.

Disclosing Trade Secrets to Employees

In order to qualify as a trade secret, the confidential business information must not be generally known and it must give that business an advantage over competitors. In addition, the owner of a trade secret must affirmatively act to ensure that the information remains confidential. Trade secrets can include formulas for a soft drink, recipes, customer lists and preferences of a product, patterns, processes, etc. Often, it is necessary for employers to disclose trade secrets to employees to enable them to perform their jobs. However, if the employee leaves the company to work for a competitor or to start a competing business of their own, they also leave equipped with that valuable information.

Protection Against Disclosure by Former Employees

In order to ensure that certain information qualifies and is protected as a trade secret, the owner of the secret must have initially acted in a manner which demonstrated their desire to keep the information confidential. Employers often solicit their employees to sign nondisclosure agreements (confidentiality agreements or NDAs) and/or covenants not to compete. These agreements create an express contractual duty of confidentiality by contract. However, employees generally have an implied duty not to disclose trade secrets regardless of such express agreements.

Employee Nondisclosure Agreements

NDAs are contracts between the employer and employee (or any two parties) whereby each agrees to maintain the subject matter of the contract in secrecy. A typical nondisclosure agreement includes the following:

1. General definition of exactly what information is to be kept confidential;
2. Exclusions from confidential information;
3. Obligations of the party receiving the confidential information;
4. Time periods for which the information must remain confidential; and
5. Miscellaneous provisions.

Such agreements are not always necessary in the employment relationship, since their duty not to disclose confidential information is implied. However, in a case where an employee discloses a trade secret, the existence of an NDA is useful as evidence that the information was in fact meant to be kept confidential. Employers may require all new employees to sign nondisclosure agreements when they are hired.

Employee Noncompete Covenants

Under a covenant not to compete, an employee agrees not to work for a direct competitor or start a competitive business for a certain period of time after their employment terminates with the current company. These agreements effectively prevent former employees from disclosing trade secrets to competitors, or from using the information in their own competing business. To be enforceable, noncompete covenants must be reasonable. Generally, a non-compete covenants must not:

- Be too long in duration;
- Cover too wide of a geographic scope or area; and/or
- Prohibit employees from engaging in too many types of businesses.

Although effective, noncompete covenants are not legal in every state. For example, California invalidates such agreements (except in limited circumstances) on the grounds of public policy since they restrain an individual's right to earn a living.

Inevitable Disclosure Doctrine

In a 1995 decision, the Seventh Circuit Court of Appeals effectuated the judicial doctrine of "inevitable disclosure" as an interpretation of Section 2 of the Uniform Trade Secrets Act (threatened misappropriation). The inevitable disclosure doctrine enables a court to prevent a former employee of one company from working for a competitor in a comparable position, if the nature of the performance of the position would inevitably require the use or disclosure of trade secrets of the former employer.

This doctrine can apply where the employee signed an NDA, yet a noncompete covenant does not exist or is invalid. Also, where the court is hesitant to completely prevent the former employee from working for a competitor, the risk of inevitable disclosure might justify the court to prevent them from working on particular tasks. However, inevitable disclosure is only recognized in some, not all, jurisdictions.

Remedies

In the event that there is an unauthorized disclosure of trade secrets by an employee, courts are authorized to order an injunction which prevents the information from further misappropriation. In addition, the infringing former employee may be liable for any damages resulting from actual losses suffered by the former employer and/or for the unjust enrichment of the new employer. Finally, in cases of willful misappropriation, punitive damages and attorneys' fees may be awarded to the injured party.

The intentional theft of trade secrets is a crime under both federal law and the law of many states. Under the Economic Espionage Act of 1996 (EEA), the U.S. Attorney General has the power to criminally prosecute those involved in the intentional theft, copying or receiving of trade secrets. Fines of up to $500,000 for individuals or $5 million for corporations may be imposed, and all property used and proceeds received from the theft may be seized and sold by the government. Violators also face prison terms of up to ten years.