

Are You Carrying Trade Secrets?

In its broadest sense, a trade secret is any confidential information used by a business that gives it an advantage over competitors who do not know or use the information. Trade secrets can be technical in nature, such as a formula, plans, or a device—which are often thought of as industrial trade secrets. They can also be related to the business operations of a company, such as confidential customer lists or marketing plans.

Trade secrets are legally protected in every state in the United States by either statute or common-law principles of unfair competition. The most prevalent law is the Uniform Trade Secrets Act, which has been adopted in some form in 42 states and the District of Columbia. In addition, many states have enacted criminal statutes making it a crime to knowingly participate in the theft of a trade secret.

The United States has also enacted the Economic Espionage Act of 1996, which creates two federal crimes involving trade secrets. The first crime is economic espionage, which makes it a felony to knowingly steal a trade secret intending to benefit a foreign government or foreign agent. The second crime is the general theft of trade secrets relating to a product that is produced for or enters interstate commerce. These offenses are punishable by jail terms of up to 15 years and 10 years, respectively, and substantial fines.

Trade secret elements

The essential elements of any trade secret are that the information:

- is neither generally known in the trade nor publicly available,
- has some independent economic value,

such as giving a competitive advantage to its owner, and

- must not have been publicly disclosed by its owner.

In addition, the owner must have made reasonable efforts to maintain its secrecy.

A trade secret can include many different types of information, such as formulas for chemical compounds, processes for

manufacturing or testing of materials, patterns for machines or other devices, and lists of customers, vendors, and marketing plans, as long as the owner has held the information secret.

Unlike inventions covered by patents (see *The Industrial Physicist*, August 2000, pp. 26–27), a trade secret does not require novelty to be protected because the law does not protect against independent invention or discovery of the secret. Nor is there a requirement of absolute secrecy. Even information that is known only to a few competitors—and is held secret by them—may be protected from exploitation by a third party. A trade secret also is protected even if the owner has disclosed it to employees or to others pledged to secrecy.

Nevertheless, there must be a substantial element of secrecy so that, except by use of improper means, it would be difficult to obtain the information. Conversely, it is not proper for someone to appropriate information that is publicly known or generally known in an industry as his or her trade secret. Similarly, no trade secret protection exists for matters that are completely disclosed by products sold to the public—those, for example, that can be reverse-engineered without infringing any patent rights.

Because the definition of a trade secret is

broad and indefinite, the courts have struggled with what is, or is not, a trade secret. In some cases, expert testimony has persuaded the courts that a process or method is not a trade secret because of its widespread use by others. The courts also have frequently declined to protect customer or vendor lists or cost and pricing information if that information can be readily obtained from public sources.

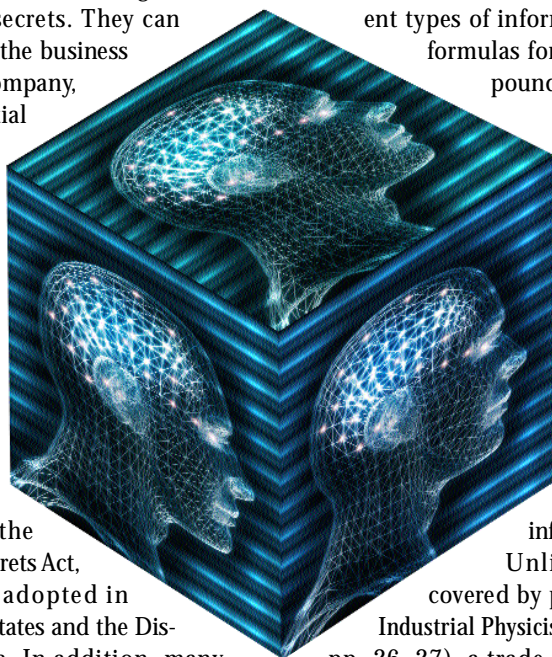
Often, the deciding factor for the court is whether the trade secret owner expended considerable time and money developing it. Inherent in every trade secret case is the notion of unfair competition or improper conduct, and courts are reluctant to deprive an owner of a competitive advantage or value because of a stolen trade secret.

The other major issue in any trade-secret dispute is whether the owner of the information has taken reasonable steps to protect its secrecy. Companies seeking to protect their trade secrets often fail to do so because of lax secrecy procedures. The easiest way to lose a trade secret is to disclose it outside of an expressed or implied obligation of secrecy. For this reason, any business should take care to include confidentiality provisions in all contracts with its vendors, potential business partners, and others who may gain access to the company's confidential information.

Employer vs employee

Most trade-secret disputes arise in the context of the employer–employee relationship. Employers view every piece of valuable knowledge or information that their employees acquire as company property. An employee, however, may understandably think that his or her skills, knowledge, and experience are personal assets that can be sold to the next employer. On occasion, this issue is the subject of explicit confidentiality or noncompetitive agreements that a person signs as a condition of employment.

Employees who have had access to confidential technology or business information and leave their jobs to work for a competitor—or to enter into business in competition with their former employer—must



consider several critical issues. First, they should examine the employment agreements they have signed to determine any expressed confidentiality or noncompetitive obligations. The existence of such agreements, unless they are unreasonable in scope or duration, may prevent a worker from accepting employment in competition with a former employer.

In the case of expressed, noncompetitive clauses, many jurisdictions will not enforce the agreements except to the extent necessary to protect identifiable trade secrets. If there is no possibility of disclosure of trade secrets, or if the duration of the noncompetitive agreement is excessive, the courts may not enforce the restrictions at all. On the other hand, there is in existence a doctrine of inevitable disclosure of trade secrets by which some courts impose noncompetition restrictions on certain high-level employees even in the absence of a confidentiality agreement.

Where no written confidentiality agree-

ment exists, the law still implies an obligation not to use or disclose an employer's confidential information if the employee knew or should have known that his employer wanted such information to remain secret. This implied obligation, however, may not apply to general information learned as the result of employment, and it does not expressly prohibit an employee from soliciting former customers or clients unless the knowledge of such customers is itself a trade secret.

A more difficult issue arises when an employee did not simply learn the trade secret or confidential information from his employer but actually developed it at his or her initiative. Some courts have found that under these circumstances, the employee may have an equal right or privilege to use this information in other employment. The issue often turns on whether the employee was "hired to invent." For this reason, written confidentiality agreements frequently provide that any inventions belong to the

employer. A few states, including California and Illinois, have enacted statutes that restrict such agreements only to inventions made by employees during their employment at the direction of their employer.

From the employer's perspective, there should always be clearly defined and communicated policies restricting employees' use of confidential information. Employers should also consider the use of written confidentiality agreements with key employees, including agreements about intellectual-property ownership and restrictive employment covenants where appropriate. They should also take special care to designate sensitive materials as confidential and to restrict access to their trade secrets on a need-to-know basis. Even the posting of signs on company premises restricting access to areas where confidential technology is used may provide critical evidence of efforts to maintain trade secrets.

The successful plaintiff in a trade-secrets lawsuit may be entitled to an award of

damages as well as injunctive relief. The courts have allowed the calculation of damages in different ways, including recovery of lost profits sustained by the trade-secret owner, recovery of the economic gains earned from the trade secret by the defendant, or a reasonable royalty for its use.

A court injunction remains, however, the most important remedy. The right to exclude others from using a trade secret is inherent to the property right in any trade secret. The principal issue in many cases is the duration of the injunction. Some jurisdictions follow a rule that favors a permanent injunction—even though the trade secret may later become public information—on the theory that the defendant should never be able to benefit from information obtained by a breach of a confidential relationship.

In other jurisdictions, the courts cannot impose injunctive relief after public disclosure of the trade secret, as, for example,

where the trade secrets are subsequently disclosed in a patent. This assumes that the defendant did not disclose the trade secret. In cases where a defendant did, the courts have enjoined the defendant from using the trade secret, notwithstanding its subsequent public disclosure. In cases involving former employees, injunctions are frequently limited in duration to balance the individual's right to seek employment in his or her field with the former employer's right to protect its confidences.

The law of trade secrets, although simple in concept, is difficult to apply in practice. Every situation has to be judged on its own facts and involves balancing the interests of the trade-secret owner with the public interest in making nonconfidential, useful information freely available. Cases are usually decided on the degree of secrecy maintained by the owner, the economic value of the secrets, and the bad faith of the defendant. In any industry involving industrial secrets, the employer and employee should


be aware of the law and should take great care in the dissemination or use of competitive secrets. The loss of a trade secret by an owner, or a court injunction and damages levied against a defendant, can be a disaster awaiting the unwary.

Further reading

Milgrim, R. M. *Milgrim on Trade Secrets*; Matthew Bender: New York, 2001.

Pooley, J. *Trade Secrets*; Law Journal Press: New York, 2001.

Jensen, J. C., and King, J. *Torts of Competition*. In *Commercial Litigation in New York State Courts*, Chapter 63, West Publishing: St. Paul, MN, 1995.

General questions about trade-secrets law are addressed at <http://www.law.freeadvice.com>; click on Intellectual Property. 

B I O G R A P H Y

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