

Strong Policies and Vigilance Are Key to Protecting the Confidential Information of Businesses

Consistent National Policies become More Readily Enforceable as Texas Adopts Uniform Trade Secrets Act

Unless companies are involved in technology or related products, most do not consider how they are going to protect their confidential information until there is a problem. Problems can arise in very common scenarios, for example when multiple employees leave to work for a competitor with the intent to use the prior employer's business information for the new company or where inadvertent or even malicious disclosure of confidential information is disseminated via social media. Having in place an effective trade secret/goodwill protection plan, including restrictive covenants governing trade secret disclosure, covenants not to compete and covenants not to disclose, can be effective protection for business assets such as intellectual property, goodwill, proprietary business information, employees and clients. Enforcement of restrictive covenants is generally governed by state law such as the Uniform Trade Secrets Act, which has been adopted in by 47 states, most recently Texas. *Continued*

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STATE LAWS GENERALLY GOVERN ENFORCEABILITY OF RESTRICTIVE COVENANTS AND THE SCOPE OF COMMON LAW PROTECTIONS OF PROPRIETARY INFORMATION

Despite the fact that many businesses operate nationally or even globally, the ability of an employer to enforce a restrictive covenant to protect its customer relationship or trade secret information is governed by the laws of individual states. If an employee or group of employees leaves to work for a competitor, the prior employer might lose more than personnel if steps are not taken to protect confidential and trade secret business information.

One of the biggest challenges that an employer faces when an employee leaves and goes to work for a competitor is deciding how to prevent the former employee from using the employer's trade secrets, goodwill or other business information to unfairly compete against it. Some of the best ways to protect employer trade secrets and goodwill are through the use of *employment agreements that contain covenants not to compete and nondisclosure agreements – including trade secret agreements*.

TRADE SECRET AGREEMENTS

Protection of trade secrets is a matter of state law, and the majority of the states have adopted the Uniform Trade Secrets Act (UTSA). Effective September 1, 2013, Texas is the 47th state to adopt trade secret protections based on the UTSA. Before the enactment of the Texas Uniform Trade Secrets Act (Texas UTSA or the Act), Texas followed common law principles governing trade secret protection, defined in Restatement of Torts section 757 as "any formula, pattern, device or compilation of information which is used in one's business, and which gives him an opportunity to obtain an advantage over competitors."²

The Texas Uniform Trade Secrets Act was enacted with the goal of bringing Texas trade secret law in line with the majority of states. However, the Texas law does contain some differences from the UTSA. Primary among these is

the way in which the term "trade secret" is defined. Under the Texas UTSA, the term "trade secret" means:

- Information, including a formula, pattern, compilation, program, device, method, technique, process, financial data, or list of actual or potential customers or suppliers, that:
 - Derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by other persons who can obtain economic value from its disclosure or use; and
 - Is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

The Texas UTSA thus updates the UTSA definition of "trade secret" to provide potentially broad protection to trade secret owners as exemplified by the inclusion of financial data and lists of customers or suppliers, neither of which appears in the UTSA.³

As it does with "trade secret," the Texas UTSA also expands the definition of what constitutes "misappropriation." Under the Texas UTSA, any of the following conduct will suffice to constitute the misappropriation of a trade secret:

- The acquisition of another's trade secret by a person who knows or has reason to know that the trade secret was acquired by improper means; or
- The disclosure or use of a trade secret of another without express or implied consent by a person who:
 - Used improper means to acquire knowledge of the trade secret;
 - At the time of disclosure or use, knew or had reason to know that his knowledge of the trade secret was:
 - Derived from or through a person who had utilized improper means to acquire it;
 - Acquired under circumstances giving rise to a duty to maintain its secrecy or limit its use; or
 - Derived from or through a person who owed a duty to the person seeking relief to maintain its secrecy or limit its use; or *Continued*

¹ New York has not adopted the UTSA. Legislation is pending in Massachusetts to adopt a version of the UTSA. North Carolina's trade secret statute is similar to, but does not mirror, the UTSA.

² *Hyde Corp. v. Huffines*, 314 S.W.2d 763, 776 (Tex. 1958).

³ UTSA § 1(4) (1985).

- Before a material change in his position, knew or had reason to know that it was a trade secret and that knowledge of it had been acquired by accident or mistake.

While the “proper means” of acquiring or discovering another’s trade secret are not materially altered by the adoption of the Texas UTSA, the legislature has with the Act broadened the enumerated scope of “improper means.” These improper means of acquisition now include (1) theft; (2) bribery; (3) misrepresentation; (4) breach or inducement of a breach of a duty to maintain secrecy, to limit use, or to prohibit the discovery of a trade secret; or (5) espionage through electronic or other means.⁴ Once again the expansive protection for trade secret owners provided by the Texas UTSA is reflected in the fact that the term “improper means” in the UTSA does not include language concerning the breach of a duty to limit use or prohibit discovery of a trade secret.

When drafting trade secret protection and nondisclosure agreements, employers should be aware of the applicable state law and the information that it is truly seeking to protect.

EXPRESS COVENANTS NOT TO COMPETE

Covenant not to compete provisions in employment agreements should be considered as part of a company’s trade secret/goodwill protection plan. Restrictive covenants are also governed by state law. A few states, such as California, greatly limit an employer’s ability to enact a true noncompete agreement, but the majority of the states recognize the legitimate business interests in enforcing reasonable noncompete agreements. Noncompete provisions can range from a pure noncompete, which prohibits the former employee from working for a competitor for a limited time in a specific business in a defined geographic scope, to more narrowly drawn customer-specific nonsolicitation provisions.

Well-drafted noncompete agreements provide a company with a timely and flexible remedy that in most cases will adequately protect its business interests that otherwise might not be protected by the common law. An enforceable covenant not to compete provides protection for business

goodwill and other interests that are generally left unprotected by the law. Restrictive covenants can be very effective in extending the protection of the company’s trade secrets, not only by its use as a security measure but also by more readily extending the scope of injunctive relief beyond a “use” injunction. A “use” injunction is one that merely prevents the defendant from “using” the plaintiff’s trade secrets. Although this type of injunction is technically adequate to protect one’s trade secrets, it is in reality very hard to monitor and enforce if the former employee is in a key position working for a competitor.

Finally, covenants can be used to help fortify an employer’s argument for an injunction under “the inevitable disclosure doctrine,” which is a common law doctrine that courts have used to enjoin employees from being able to work for a competitor in any job position in which there is a strong likelihood that the former employee, even in good faith, could not help but disclose his former employer’s trade secrets, even though there is no direct evidence of misappropriation.

NONDISCLOSURE AGREEMENTS

There are several reasons why a company should have all of their employees sign nondisclosure agreements as an alternative to or in addition to covenant not to compete agreements:

- First, unlike covenants not to compete, nondisclosure agreements are not a restraint on trade and, thus, are more readily enforced.⁵
- Second, it allows a business to add other provisions to the agreement – such as employee non-recruitment, idea assignment, agreements to certain types of injunction paragraphs – and have them enforced under general contract principles, not the higher standards applied to a noncompete agreement.
- Third, requiring employees to sign nondisclosure agreements should prevent them from raising the “I didn’t know the information I stole was a trade secret” defense. *Continued*

⁴ Texas UTSA § 1(1) (1985).

⁵ See, *CRC-Evans Pipeline Int'l v. Meyers*, 927 S.W.2d 259, 265 (Tex. App.-Houston [1st Dist.] 1996, no writ) (nondisclosure agreements are not considered restraints of trade and do not need to meet the statutory requirements for covenants not to compete).

- Fourth, a properly drafted agreement can clarify and identify the company's trade secrets.
- Finally, once an employee signs such an agreement and then breaches it forcing the company to sue, under certain state laws if the company is successful, it may be able to recover its attorney's fees for bringing suit.

SOCIAL MEDIA POLICIES

An employer's social media policies should be coordinated with its policies that protect confidential information. For example, social media is easily used by employees and former employees to disclose information that may be confidential to the business; therefore, an employer's social media policy should expressly prohibit posting or disclosing confidential information. Former employees may use social media to directly or indirectly solicit business and recruit their former co-workers; again, an employer's non-solicitation and non-acceptance of customers' post-termination offer of employment provisions should be broad enough to address the situation where a former employee posts information on Facebook or LinkedIn® that leads to a customer calling that employee.⁶

DRAFTING POINTERS FOR COVENANTS NOT TO COMPETE AND NONDISCLOSURE AGREEMENTS

The following is a list of the types of provisions that employers should consider for inclusion in employment agreements to protect confidential information, subject to specific requirements of the applicable state laws:

1. A provision in which the employer agrees to provide confidential information and/or trade secrets in return for the employee's promise not to disclose the confidential information and/or trade secrets
2. A provision that sets forth what the employer believes are its trade secrets and confidential information
3. A provision that cites what business interests (e.g., trade secrets, goodwill) the employer is trying to protect
4. A provision containing reasonable restraints as to time, geographic area and scope of activity curtailed, which also should include a provision where the employee acknowledges such reasonableness
5. An employee non-solicitation provision and a customer non-solicitation provision
6. A provision that requires the employee to inform his or her prospective employer, prior to accepting employment, of the existence of the covenant not to compete agreement
7. An assignment of intellectual property provision
8. A provision that the employee will return and/or not keep originals or copies of any of the company's documents, materials, equipment, etc. upon termination of employment
9. A provision wherein the employee acknowledges that, even using his or her best faith efforts, it is inevitable that he or she would disclose the former employer's confidential information while working for a competitor in the same capacity as employed by the former employer
10. A provision wherein the employee (1) acknowledges the irreparable harm that he or she will cause if he or she breaches the agreement and (2) agrees to a temporary injunction preventing further breach of the agreement by the employee
11. If appropriate, include a provision that the employee, based on the employee's own experience and capabilities, agrees that the restrictions in the noncompetition provisions will not prevent employment or earning a living doing something else, and that if the employment is terminated, that the employee is ready, willing and able to seek employment with an employer who is not a competitor. *Continued*

⁶ See, e.g., *Enhanced Network Solutions Group, Inc. v. Hypersonic Techs. Corp.*, 951 N.E.2d 265 (Ind. Ct. App. 2011) (holding that "solicit" was not defined by the employer broadly enough to prohibit indirect solicitation on LinkedIn).

THE DECISION TO SUE FOR TRADE SECRET
MISAPPROPRIATION OR BREACH OF NONCOMPETE
AGREEMENT

A lawsuit for breach of a noncompete agreement or an action for misappropriation of trade secrets is normally initiated with a request for injunctive relief. If successful in litigation, the company will have protected its intellectual property by stopping further use and or dissemination of its trade secrets. It may also send a message to other employees and its competitors that the company is serious about protecting its trade secrets. This will often cause competitors to be more reluctant to hire an employee whose employment would be in violation of a noncompete. Failure to file suit to enforce a noncompete or to protect trade secrets could be used to raise a question of waiver of these rights by subsequent employees who violate these obligations.



CONCLUSION

The summer months are a good time for employers to work with legal counsel to review policies and procedures designed to protect confidential information and business goodwill under the applicable – and evolving – state laws. Effective policies regularly enforced arm the business with the necessary tools to stop the loss of valuable company property.

Members of Wilson Elser’s Employment & Labor practice, located throughout the country, provide one convenient point of contact for our clients. Please contact any of the following partners to access the experience and capabilities of this formidable team.

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