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Enforceable Nondisclosure Agreements: Protecting Trade Secrets and Other Confidential Business Information

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Today's faculty features:

Jeff Neurman, Founding Partner, **Farkas & Neurman**, New York

Daniel R. Saeedi, Partner, **Taft Stettinius & Hollister**, Chicago

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Non-Disclosure Agreements: A Litigator's Perspective

Daniel R. Saeedi

Partner - Taft Stettinius & Hollister LLP

Why are Non-Disclosure Agreements Important?

- The Three Goals of NDAs:
 - NDAs provide *notice and guidance* to the recipient party and the courts
 - NDAs provide a *contractual remedy* for the sharing party
 - NDAs bolster the sharing party's *trade secret claims*

Interplay between Trade Secrets and NDAs

- Why are we even talking about trade secret statutes?
 - Statutory attorney's fees
 - Punitive damages of up to twice the actual damages amount
 - A well-defined body of law familiar to the courts
 - Overlap between NDAs and trade secret statutes: a wrongful disclosure often violates both the contract and statutory law.

What is a Trade Secret?

- The Defend Trade Secrets Act – 18 U.S.C. 1839
- “Trade Secrets” can be several types of business and financial information, provided:
 - (A) the owner thereof has taken reasonable measures to keep such information secret; and
 - (B) the information derives independent economic value from not being generally known.

What is Misappropriation?

- “Acquisition, disclosure or use of a trade secret without express or implied consent by someone who:
 - Used improper means to acquire it; or
 - Knew it was improperly acquired; or
 - Derived the trade secret from a person who owed a duty to maintain secrecy
- Improper Means – Theft, bribery, misrepresentation, ***breach or inducement of a breach of a duty to maintain secrecy.***

The Interplay Between Trade Secrets and NDAs

- NDAs *broaden* protection against disclosure: an enforceable NDA may protect material not properly characterized as a trade secret.
- NDAs help *define elements* for a trade secret tort claim.
- NDAs put parties on *notice of compliance* and thus establish wrongful intent when violated.

NDA: Defining the Scope

- Attorneys make the mistake of drafting scope clauses with undefined general terms.
- A good NDA provides the parties and the Court with guidance as to what falls under it.
- Customize the agreement to fit your client's needs: reference certain specific client proprietary categories.

NDA: Defining the Scope

- Example 1 – “Information concerning the Company's business operations, such as marketing techniques; business development plans and procedures; pricing; profits; costs; sales; losses; financial information; accounting and unpublished accounting information”
- This clause leaves the courts guessing as to whether a specific document falls under any of these general categories.

NDA: Defining the Scope

- (ii) Example 2 – “Information concerning the Company's business operations. . . . ***and information stored on the Company's “Customer Relationship Manager” database; “Client Pricing” database; and any other proprietary company database for which the employee was given password-protected access.***”
- This clause leaves no doubt for both the recipient party and the courts.

NDA: Trade Secret Buzzwords

- Use the relevant trade secret statutory buzzwords!
- Make sure that your NDA:
 - **Labels** categories of information as “trade secrets”
 - Acknowledges that these categories of information are **valuable**
 - Specifies that these categories of information are the subject of **significant efforts to maintain secrecy**

NDA: Trade Secret Buzzwords

- Example 3 – Acknowledgement of value and efforts to ensure secrecy
- ***“Vendor agrees that Confidential Information defined herein are trade secrets of the Company. Vendor agrees that the Company derives considerable economic value from this information being kept secret, and that the Company has expended significant time, effort and funds to ensure that this information is kept secret.”***

Beware of Overly-Broad NDAs

- Warning signs
 - Scope clauses that broadly define confidential information (i.e. “all information relating to the Company”)
 - Scope clauses that violate statutory laws
 - Scope clauses that do not contain exceptions (i.e. information which is public knowledge, publicly disclosed by the Company or lawfully known prior to work commencement)
 - In some jurisdictions, scope clauses that do not contain durational or geographic limitations

Defining the NDA Violation

- NDAs should impose significant duties:
 - Duty to **preserve** confidentiality
 - Duty to **return** confidential information upon project completion
- NDAs should define grounds for violation:
 - **Disclosing or using** confidential information without written permission
 - **Permitting anyone** to use confidential information without written permission
 - **Copying, duplicating or removing** confidential information without written permission

Remind Parties of NDA Obligations

- Companies should remind parties of NDA obligations, especially at the conclusion of a project or employment relationship.
- The “Exit Interview.” This further helps establish wrongful intent if a subsequent disclosure occurs. Also an opportunity to receive confidential information in the possession of the other party.

Other Helpful Clauses to Potentially Include in an NDA

- Work product clause
- Return of Company property clause
- Non-Competition / Non-Solicitation clauses

Crafting the Remedy

- Choice of Law
- Choice of Forum – make it exclusive!
- Attorney's Fees Clause
- Irreparable Harm Clause

Any Questions?

Contact Information:

Daniel Saeedi

Taft Stettinius & Hollister LLP

111 E. Wacker Drive Suite 2800

Chicago, IL 60601

dsaeedi@taftlaw.com

(312) 840-4308



Elements of an NDA

Key provisions and considerations

I. Parties Involved

- Bilateral or one-way: Will both parties be sharing information or just one?
- Less is more: From disclosing party's perspective, the more narrow the permissible recipients the better
- "Representatives": Often receiving party will wish to include other parties – e.g., employees, officers, directors, equityholders, counsel and accountants, sometimes defined as the receiving party's "Representatives"
 - Limit to those who have a legitimate need to know and, ideally, sign an NDA too
- Parties should agree on whom may receive confidential information (CI)
 - Additional signatories?: Often disclosing party will require any party that receives the information to either sign the NDA or get a representation from the main recipient that those with whom it shares the information are aware of the NDA and its terms or are otherwise bound by an NDA in favor of receiving party

II. Scope of Relationship

- Generally, it is in disclosing party's interest to describe the relationship as broadly as possible
 - Broader description makes it less likely that receiving party will be able to claim that certain information was provided to it in the course of a separate arrangement between the parties and thus outside the NDA
- Nonetheless, too broad a definition could permit receiving party to use CI more widely than disclosing party intends.
 - This is a particular concern if the parties are pursuing a relationship other than an investment by receiving party (e.g., the parties are competitors discussing a possible joint venture)
- Important to pick up any information disclosed before NDA was signed
- CI should only be allowed to be used in the context of the relationship

III. Standard of Care

- General standard: Receiving party treats and safeguards, as confidential and secret all CI received by it and shall not (nor permit its Representatives to), without prior written consent, disclose or reveal any CI or the fact that it has received CI
 - Existence of discussions: The mere fact that the parties are in discussions at all should often, if not generally, be kept confidential as well
- Alternative approach: Receiving party may suggest to treat CI "with the same degree of care that it maintains its own sensitive information."
 - Hard to verify: Disclosing party may should generally resist this formulation as there is often no simple way to verify appropriateness of receiving party's confidentiality protection processes.
- Compromise: Agree to how receiving party handles its own sensitive information but add a qualifier that the degree of care the receiving party uses "shall be no less than a commercially reasonable degree of care."

IV. What is Confidential Information

- Confidential Information: Any information not generally known to the public or recognized as standard industry practice. Examples include know-how; strategies; strategic partnerships and the existence of the discussions between the parties; employee information; financial records and inventory records of disclosing party; intellectual property; trade secrets; ideas; concepts; inventions; methods or processes; clients and agreements with clients, suppliers and any third party; customer lists; supplier lists; marketing arrangements; channels of distribution; pricing policies and records
 - Also any other information (i) normally understood to be confidential or (ii) designated as such in writing by disclosing party
 - Includes information derived from any of the above or that comes into receiving party's possession as a result of the NDA or relationship.

V. What is not Confidential Information

- General categories excluded from definition of CI:
 1. Prior possession: Information in receiving party's possession prior to disclosure to it by disclosing party, provided that such information was not furnished to it by a source known by receiving party to be bound by a confidentiality agreement or otherwise prohibited from disclosing the information
 2. Public: Information generally available to the public other than as a result of a disclosure by receiving party or its Representatives
 3. 3rd Party Source: Information that becomes available to receiving party on a non-confidential basis from a source other than disclosing party or any of its Representatives, provided that such source is not known by receiving party to be bound by a confidentiality agreement with receiving party or otherwise prohibited from disclosing the information
 4. Independently Developed: Information which was or is independently developed without violating NDA's obligations

VI. Other Exception to Confidentiality

Receiving party may request provision permitting disclosure of CI if required to do so by law, regulation, or court order.

- This provision should typically be acceptable to disclosing party if receiving party:
 1. Agrees to notify disclosing party, before disclosing CI (if legally permitted to do so), so as to allow disclosing party to (i) prepare for disclosure and (ii) use its resources to contest the disclosure obligation or court order
 2. Agrees to cooperate with disclosing party to limit the disclosure
 - Note: Often in this instance receiving party will require that it be compensated for any costs incurred with such cooperation

VII. The End

- NDA should specify what receiving party must do with CI at end of the applicable period.
 - It is most favorable to disclosing party if receiving party must return CI.
 - Disclosing party should resist including language that would require it to request return of the information (in other words, the obligation should arise automatically at the end of the period).
- Receiving parties often ask for the option to destroy materials instead of returning them.
 - Receiving party might be particularly concerned about not agreeing to "return" CI contained in receiving party's own derivative documents containing CI.
 - If this is agreed to, receiving party should certify in writing to disclosing party of such destruction.
- Receiving party may seek to add provision to retain copy of some or all of CI in accordance with its record-keeping policy or similar policies, laws, or regulations.
 - This may be acceptable so long as the provision requires receiving party to maintain the strictest standards of confidentiality for the retained information.
- Should specify period in which return or destruction of CI must occur -- "immediately" probably not practical but "promptly" should be. Alternatively, parties can agree to a fixed time period for compliance, such as five business days.

VIII. Breach

- In the case of a breach of the NDA, Receiving Party shall:
 1. immediately notify the disclosing party, in writing, of the breach;
 2. fully cooperate to mitigate the effect of such breach; and
 3. be responsible for any breach caused by any of its Representatives or any third party to whom or to which it has provided or given access to CI.

IX. Data Protection

In light of concerns about identity protection, the receiving party, and any third party to whom or to which it provides CI, will comply with all applicable laws with respect to the use and maintenance of CI, including any applicable data protection laws.

X. Term and Termination

- Several options for term of an NDA including (i) an indefinite term (unlikely to be accepted by receiving party), (ii) a fixed term beginning on the date of the NDA – often a year (although longer is better for disclosing party) and (iii) a fixed term beginning after conclusion of the relationship.
- If the parties want to continue the term of the NDA beyond the point that they enter into the principal agreement for the investment in the company or other transaction, that new agreement can include a confidentiality provision that references or incorporates this NDA.
- The NDA should include a survival clause with a definite survival period. A term of two years is common.

XI. Additional Provisions

- No representation about the information: The purpose of the NDA is to share information, not to make assertions about its accuracy, etc. (which would typically be covered in the definitive documentation for the transaction).
- Retention of IP Rights: This is intended to clarify that receiving party is not granted any rights or license to use CI for any purpose other than in connection with the relationship
- No Obligation: This clarifies that the NDA should not in any manner bind the parties to additional obligations – i.e., sharing information is not tantamount to agreeing to a deal.
- Injunctive Relief: Because the sharing of CI could result in hard to calculate damages, injunctive relief is generally sought.

Questions? Need Assistance?

- Feel free to contact Jeff Neurman at jneurman@farkasneurman.com or 347-470-4596.

