

THE RECORDER

IN PRACTICE

IP, trade secrets and employee mobility

Judges and attorneys discuss top-of-mind issues for Silicon Valley tech employers



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Intellectual Property

Increasingly today, the value of a company is measured not by its physical assets, but by the talents of its employees and the utility of its intellectual property. Because of their knowledge and experience, talented employees are constantly wooed by competitors. Many believe that innovation is the product of employee mobility. However, as employees leave, many of them carry with, mentally and sometimes physically, intellectual property belonging to their employer.

Recently a roundtable discussion—jointly sponsored by The Recorder and JAMS—addressed the topic “Trade Se-

crets and Intellectual Property in the Age of Employee Mobility.” Panelists included judge James Kleinberg, Santa Clara Superior Court; Bradford Newman, Paul Hastings; Dan Feldstein, Zynga Inc.; and yours truly. The discussion was moderated by U.S. District Court Magistrate Judge Laurel Beeler. Some practical points can be derived from the discussion.

DEFINING “TRADE SECRETS”

The general term “intellectual property” is used to describe multiple types of information: copyrights, patents, trademarks, trade secrets, other confidential business information. Unlike other forms of IP, there is no formal system in which trade secrets are defined or registered. Thus, when employees leave, the protection of trade secrets presents special challenges.

The panel agreed that in order to protect trade secrets after employment ends important steps must be taken at the beginning of employment.

Although misappropriation of a trade secret is actionable in the absence of a contract, many employers require employees who will be exposed to trade secrets and other confidential information to sign a contract prohibiting improper disclosure or use. Care should be taken to distinguish between contractual language in which the employee agrees not to compete and a promise not to use or disclose trade secrets or confidential information. A non-competition covenant might be regarded by a court as void. See California Bus. & Prof. Code

§16600. On the other hand, a thoughtfully drafted employment contract can protect both the employee’s interest in mobility and the employer’s interest in its intellectual property.

Many businesses regard all business information as “trade secrets.” Under the laws of many states, including California, the only information that is protectable as a trade secret is that which meets the statutory definition. Most states have adopted a version of the Uniform Trade Secrets Act. In California a ‘trade secret’ is defined as information such as a formula, method, or compilation that is known by others and actually or potentially could be economically valuable to others if it were disclosed or used by them. In other words, the information has value because it is a secret. In addition, the information must be the subject of efforts that are “reasonable under the circumstances to maintain its secrecy.” Civil Code §3426.1.

In many trade secrets disputes, considerable time and resources are expended over the identification of the alleged trade secret. Cases have been dismissed or summarily adjudicated against the owner of the alleged trade secret because the owner could not identify the alleged trade secret with sufficient precision. *See e.g., All Business Solutions, Inc. v. NationsLine, Inc.*, 629 F. Supp. 2d 553 (W.D. Va. 2009). Therefore, the more precisely a company identifies its trade secrets during the course of employment, the more likely the company will be able to successfully protect its trade secrets when a dispute arises.

Judge James Ware (Ret.) joined JAMS after spending 16 years as a civil litigator, and 24 years as a judge. He served as a United States District Judge on the Northern District of California, including a year and a half as the Chief Judge of the Northern District.

CONTRACTUAL PROTECTIONS AND ARBITRATION

As a prophylactic measure, the employment contract can also be used to emphasize the acquiring company's policy that a new employee should not use proprietary information of a former employer.

During the course of employment, just as employee's performance is periodically reviewed, the changing contours of the company's trade secrets should also be periodically reviewed and reinforced with employees.

Increasingly, employment contracts provide for arbitration of any dispute "arising during" or "related" to employment. A dispute over a former employee's use or disclosure of a trade secret is likely to be regarded as subject to such an arbitration agreement. *See e.g., Simula, Inc. v. Autoliv, Inc.*, 175 F.3d 716 (1999).

Feldstein and Newman attribute the frequency with which employment contracts now provide for arbitration of disputes to a number of factors, such as the number of arbitrators with judicial experience. An increasing number of retired judges are available to serve as arbitrators. Arbitrating before a former judge can be assured by including that requirement in the arbitration agreement.

Injunctive relief is an important remedy in trade secrets disputes. When including an arbitration clause, consideration should be given to whether to empower the arbitrator to grant such relief or to require such motions to be brought in court.

Another factor causing parties to favor arbitration when they anticipate a trade secrets dispute is the confidential nature of arbitration proceedings. Courts are public institutions. Judges are reluctant to conduct closed sessions or order the sealing of papers filed in court proceedings. Moreover, even when papers are filed under seal, circumstances might develop that lead to the opening of sealed records. By its nature, arbitration is a private proceeding. It offers a forum in which trade secret issues can be fully litigated outside of the public eye.

A perceived advantage of civil litigation over arbitration is the right to ap-

peal an adverse civil judgment. In fact, in an arbitration agreement, parties are free to agree to an appellate process. Many years ago, JAMS adopted rules that allow parties the option of selecting arbitration with the right to appeal. The rules provide that a three-neutral panel (or a single neutral if the parties elect) will apply the same standard of review that the first-level appellate court would apply in an appeal from a trial judge decision. The JAMS rules include an additional procedure that is unavailable in a civil appeal. If the appellate panel determines that evidence was improperly excluded, instead of remanding the matter to the original arbitrator, the panel may re-open the record for de novo review. The taking of additional evidence is also available if the panel concludes that the evidence is necessary under its interpretation of substantive law.

Trade secrets cases can arise out of information shared by employees with vendors, or non-employees proposing business joint ventures. The careful language used to bind employees to nondisclosure and nonuse of trade secrets should also be used in nondisclosure agreements.

In response to development deadlines, many employees work remotely, from home or as they travel. To provide easy access to information, they might store it on home computers or in the "cloud." Indeed, many companies use cloud storage. Based on the "shared" nature of cloud computing, terms-of-service agreements with cloud storage companies should be carefully examined to ensure that information stored in the cloud does not lose its "secret" status.

TORT CLAIMS

In addition to contractual protections, the panel discussed tort claims that might be brought for misappropriation of confidential information. It is not uncommon that in a trade secrets dispute the plaintiff will also desire to protect from improper use or disclosure business information that does not meet the rigorous statutory requirements to qualify as a trade secret.

In seeking a tort remedy for non-trade secret confidential information, practi-

tioners have included claims for conversion or unfair competition. However the availability of these alternative tort claims has recently been called into question in a case entitled *Silvaco Data Syst. v. Intel Corp.*, 184 Cal.App.4th 210 (2010). In *Silvaco*, the Sixth District of the California Court of Appeal rejected the plaintiff's attempt to combine claims for conversion, conspiracy, and unfair competition with a claim for misappropriation of a trade secret. The *Silvaco* court reasoned that the alternative tort claims were superseded by the express language of the California Uniform Trade Secrets Act. Civ. Code §3426.7(b). CUTSA contains an express preemption clause that states that, with three exceptions, it provides the exclusive tort claim and remedial scheme for misappropriation of a trade secret. The three exceptions are: contractual claims, criminal law claims or other civil remedies not based upon misappropriation of a trade secret. Civ. Code §3426.7(b).

The *Silvaco* court stated that any tort claim for misappropriating information that has value because it is secret must be brought under CUTSA. Subsequently Judge Lucy Koh in the Northern District Court of California followed *Silvaco* and held that CUTSA supersedes claims for misappropriation and conversion of proprietary information even where the information at issue is not identified in the complaint as constituting a trade secret. *See SunPower Corp. v. SolarCity Corp.*, No. 12-CV-00694-LHK, 2012 WL 6160472 (N.D. Cal. Dec. 11, 2012).

The California Supreme Court has not yet addressed the issue and the panelist advised practitioners to stay abreast of developments in this area.

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