MANAGEMENT OF NONDISCLOSURE AGREEMENTS

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Trade secrets can be shared safely only in a confidential relationship. Sometimes the confidence can be implied, such as with an employee or a long-standing, trusted supplier. But even in those classic circumstances, a written contract is always useful, to prove and reinforce the relationship, to clarify obligations, and to demonstrate that you as the trade secret holder have satisfied your legal obligation to exercise "reasonable efforts" to protect your assets. But these contracts, often called "NDAs," can also represent a risk, because you may have taken on obligations to protect someone else's information, and that can sometimes interfere with your freedom to operate your business.

So whether your concern is making sure that your own data are adequately protected, or avoiding complications from the promises you've made to someone else, this is a critical issue. But in my experience, far too many companies pay too little attention to nondisclosure agreements and get themselves involved in litigation that could have been easily avoided. Like any other high-value, high-risk activity, this one needs to be carefully managed.

Keep in mind that not all NDA's appear as a separate document titled "Nondisclosure Agreement" or "Confidentiality Agreement." Very often the obligation of secrecy is embedded in some other contract. For example, a company that works with you to supply or design a device that you will incorporate in your own product may include in their contract a provision requiring you to treat their design suggestions and tolerance data as confidential. This may appear only as a brief paragraph in a long document that deals with many other issues and doesn't highlight the confidentiality clause. But in the end it can be just as consequential as a contract with "nondisclosure" in bold capitals on the first page.

NDAs can be simple and still be fit for purpose. For example, a single sentence or short paragraph can establish the subject of a confidential exchange. But often there will be important issues to consider and negotiate. In fact, when the other side proposes what appears to be a complicated proposal, this can be an opportunity to address and resolve issues that might otherwise have caused a problem later in the relationship. However, be sure that you keep the confidentiality issues separate at the beginning stages, and don't try to use the NDA as a platform for negotiating the substantive transaction; that comes later. In this paper I will describe what in my experience have been the more typically contested issues in confidentiality contracts, or at least the ones that raised questions at the outset.

The first of the challenging issues is how you define the information that is supposed to be protected as a secret. In the simple deal, this is glossed over with a promise to treat as confidential whatever is disclosed. In a high-stakes transaction that is usually not enough. To get more precision, the NDA will specify a particular subject matter at the beginning, but will go on to require that all "confidential information" be identified as such, in writing on documents, and for oral disclosures, in a written notice provided within a certain number of days. In theory, this should result in a specific written record of exactly what was shared. But be careful; the disclosing side needs to exercise real discipline in following up to be sure that the required notice is comprehensive and is given within the required time. And the receiver has to take the time to look at the notice when it comes in, compare it to the recollections of those who were at the meeting, and communicate a (usually written) objection if it is vague, overreaching or incomplete. In my experience it is easy for people to forget these "details," and for misunderstandings to ripen into lawsuits.

The typical NDA includes an "exceptions" clause, pointing out that, no matter what is revealed, no obligations apply to information that is generally known or otherwise can't qualify as a trade secret, or to information that comes to the other side independently of the relationship. These provisions are as reasonable as they are common. But be careful about the so-called "residuals" clause, which with some variation provides that "confidential information" will not include information "retained in the unaided memories" of the people who received the disclosure in confidence. You may think that an exception like that could swallow the rule, and you would be right. However, some very large companies are so concerned about possible interference with their other ongoing projects, and are so powerful in relation to those who want to deal with them, that they can insist on this broad reservation. So if you are one of those that can demand it, this will certainly help mitigate your exposure. But if you are confronted with a residuals clause, ask what the proponent is concerned about, and see if you can come up with narrower language to address that concern. If they press on this issue, you will need to decide if you are willing to have the risks of their "unaided memories" shifted to your side.

Some NDAs include a termination provision: the obligations apply only for a specified period, such as three or five years. The advantage of that kind of agreement is pretty obvious: for information that you have received, there comes a time when you don't have to worry about it any more; your obligations have ceased. For many companies that receive a lot of third party information, that can be a very valuable limitation. The flip side, however, is that any rights you might have in the information you have shared will expire at the same time. So before agreeing to a finite term for an NDA, be sure that you are comfortable with losing rights to your own information after a set period of time.

One issue too often neglected by companies signing NDA's is what it means to be respecting the confidentiality of the other's trade secrets. Sure, you won't

consciously misuse or disclose them; but what is the “duty of care” for someone else’s data? Frequently that question is passed over in favor of a clause saying only that the recipient will use the same level of care that it applies to its own secrets in handling the ones it receives. But as information security expert Naomi Fine points out, that solution begs some very important questions. How does the recipient determine which of its employees has a “need to know”? If the recipient treats its own information with different levels of control, which of those should it apply to the entrusted data? What sort of digital and physical security should be used? Are passwords and a locked cabinet enough? More to the point, does the trade secret owner know exactly what will be done with its crown jewels? The message here is that both sides should address those issues at the front of the transaction, rather than waiting to see if there is a loss with recriminations about what could have been done to prevent it.

Then there is the international dimension to worry about. Although the basic concept of confidentiality is understood globally, standards and expectations vary enormously from one country to the next. Some countries, for example, limit the enforcement of secrecy obligations after the primary relationship ends; others require assignment of certain technology rights to local partners. So although you might prefer to have one form of NDA that works around the world, that’s probably unrealistic, especially for high-impact transactions. In general, you need to be sure that your foreign transactions and operations are covered by contracts reviewed by local lawyers. Close management includes making sure that all disclosures are documented and that employees and subcontractors with access -- not just their foreign employer -- sign NDAs with your company as the named beneficiary, acknowledging their access to specific confidential information (and preferably agreeing to jurisdiction in the U.S. to resolve disputes).

Finally, keep in mind that with the signing of an appropriate NDA, your job as manager is not over, it’s just beginning. In fact, in my experience many more problems stem from poor management of the NDA obligations, than from what is in, or missing from, the contract. I’ve already noted one way that this happens, because people forget to send a written confirmation of an oral disclosure, or forget to examine a confirmation they have received. Many more mistakes can happen during the course of the relationship, when information is handled in a sloppy way, or at the end, when documents are not destroyed or returned as the agreement requires. The lesson is clear: in any transaction where secrets are exchanged and entrusted, someone needs to be responsible and accountable for ensuring that everything is handled and documented properly.