

## IP Issues in Employment Law

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### I. Introduction

Intellectual property (IP) issues arise often in employment law matters, including disputes with departing employees over trade secrets and customer lists, questions regarding ownership of intellectual property developed or discovered by an employee, and rights of an employer to develop new products and lines of business by hiring executives away from other companies excelling in the manufacture of such products. While not all IP disputes can be avoided with advance planning, many can. Business lawyers aware of these issues can provide a great service to their clients.

As noted at the end of Chapter 1, there are three basic IP-related concerns that arise in the employment context. First, a business must

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ensure that any IP rights created by its employees in the course and scope of employment belong to the business. Second, businesses must take care to ensure that employees do not misappropriate their intellectual property assets. Finally, businesses must educate employees about the IP rights of others to ensure that such rights are not infringed. Each of these concerns is discussed in detail in the sections that follow.

### *Traps for the Unwary*

1. Employers must plan in advance to obtain and protect ownership of intellectual property; calling their lawyers only after employees leave to set up competing businesses or to join competitors is too late.
2. The copyright principle known as the “work for hire doctrine” is very limited in its application: it applies only to employees and some independent contractors. Pursuant to the doctrine, an employer will own the copyrights in works of authorship created by employees in the course and scope of their employment but will not own the copyrights in works created by independent contractors unless the appropriate written agreement has been obtained.<sup>1</sup>
3. In order to protect trade secrets it is essential for companies to engage in reasonable efforts to maintain the secrecy of such information, but claiming that everything used in a business is a trade secret is not the way to do it. Instead, companies should identify their key trade secrets and institute a trade secret protection policy focused on them.
4. Noncompetition agreements may prevent employees from leaving with knowledge and information and competing with the employer, but they must be carefully drafted to ensure that they are “reasonable” (and therefore enforceable) under applicable law.

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1. See 17 U.S.C. § 101, definition of “work made for hire.” See also *Community for Creative Non-Violence v. Reid*, 490 U.S. 730 (1989).

5. Employers who want to obtain instant expertise in a particular area by hiring top talent from their competitors should think twice. Employers who hire from competitors must be aware of the risk of lawsuits for theft of trade secrets and other proprietary information.

## II. Ensuring Ownership of IP Created by Employees

Much of the IP-related litigation that arises between employers and employees concerns the ownership of intellectual property rights that were created by an employee (or former employee) during her employment. Typically, such claims arise when an allegedly employee-generated idea, work of authorship, or invention is successfully utilized by a company to generate income. The more successful and profitable the idea, work, or invention, the more likely there will be employees who believe that they “deserve” a piece of the profits. This is particularly true in the case of companies that do not have clear policies regarding the ownership of employee-generated IP.

High-tech and biotech companies, record labels, and movie studios are not the only businesses that thrive or fail based upon their intellectual capital and, thus, they are not the only companies that should worry about potential IP ownership claims by current and former employees. Manufacturing, service, oil field, food service, distribution, and many other types of businesses create and rely upon intellectual property. In order for a company to make sure that it is securing ownership of all IP created by its employees, it must first identify the IP rights that it owns and is creating and, next, take whatever steps are necessary to secure ownership of such rights.

### A. *Identifying IP Rights*

Chapters 1 and 10 of this book contain detailed descriptions of the various types of IP rights and detailed information about how to identify IP that may be lurking in your business. The following is a brief discussion of those rights.

### 1. Copyrights

Copyright protection is granted by federal law to “original works of authorship fixed in tangible form.”<sup>2</sup> Because the requirement of “originality” means only a modicum of originality,<sup>3</sup> and copyright protection automatically attaches to a work once it is “fixed,” every company is likely to create copyrightable works. The nature and extent of these works will depend on the nature of a company’s business, but chances are there are at least some copyrighted works in every company.

To determine whether and to what extent a company owns copyrightable materials, it is important to first consider the list of works of authorship that is set forth in the Copyright Act. U.S. law defines “works of authorship” to include:

- a. literary works;
- b. musical works, including any accompanying words;
- c. dramatic works, including any accompanying words;
- d. pantomimes and choreographic works;
- e. motion pictures and other audiovisual works;
- f. sound recordings; and
- g. architectural works.<sup>4</sup>

Looking at the foregoing list, one might be tempted to conclude that only companies that are engaged in the creative arts are likely to create copyrightable works, but don’t be misled. The terms listed above have been defined by statute and court decisions to include a wide variety of business information, including manuals, charts, diagrams, technical drawings, plans, computer software, and training videos. Thus, the question for most companies is not whether they own copyrightable works, but whether such works are worth protecting.

### 2. Patents

Patents are easy to identify because, unlike copyrights, they do not come into existence automatically but must be granted by the patent office of the United States or a foreign country. If granted, these rights

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2. 17 U.S.C. § 101, *et seq.* (the “Copyright Act”).

3. *See Feist Publications v. Rural Telephone Service*, 499 U.S. 340 (1991).

4. 17 U.S.C. § 102(a).

are documented in written “letters patent” and are recorded with the applicable patent authorities. They may also exist in the form of pending patent applications that may or may not be granted.

Obviously, companies that have gone to the time, trouble, and expense of obtaining patent rights know that such rights exist. There may, however, be companies that don’t know that they are creating potentially patentable inventions. More importantly from an employment law perspective, some companies may not be fully cognizant of the activities being undertaken by their employees and may not realize that although an employee is not formally engaged in research and development activities, he has created a new invention.

To plan ahead, companies must understand that the scope of potentially patentable inventions is very broad. It includes not only physical items such as tools, machinery, and devices, but processes, chemicals, software, and business methods.<sup>5</sup>

### **3. Trade Secrets**

If a company has potentially patentable inventions, they are likely to be trade secrets until such time as a patent application is filed and disclosed. However, the scope of trade secret protection is not limited to information that falls within the scope of patentable subject matter. Trade secrets, which are governed by common law<sup>6</sup> or by state statute (usually based upon the Uniform Trade Secrets Act) rather than by federal law, provide protection against misappropriation of a formula, pattern, device, compilation of information, program, method, technique, or process that has value to a business, that is not generally known in the industry, and that is subject to reasonable efforts to protect its secrecy.<sup>7</sup>

### **4. Trademarks and Service Marks**

Like patents, trademarks and service marks are relatively easy to identify, but not necessarily because they are registered. Rather, trademarks and service marks are usually easy to identify because they are the name of a company’s products and services. However,

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5. 35 U.S.C. §§ 101, 161, & 171.

6. Restatement of Torts § 757.

7. MICHAEL A. EPSTEIN, EPSTEIN ON INTELLECTUAL PROPERTY, Ch. 1 (Aspen Publishers, 2006) (hereinafter, “EPSTEIN”); BRIAN M. MALSBERGER, TRADE SECRETS: A STATE-BY-STATE SURVEY (BNA Books, 3d ed. 2006) (hereinafter “MALSBERGER, TRADE SECRETS”).

because the scope of trademark and service mark protection is not well known or understood by a lot of companies, there is a possibility that a company will create trademarks and service marks without even knowing that they are doing so. Thus, as with copyrights, patents, and trade secrets, it is important for a company to understand all the things that may constitute trademark and service mark rights and to take the necessary steps to protect what it believes are the most important and valuable of such rights.

Trademarks and service marks are protected to some extent by both federal<sup>8</sup> and state law (either common law or statutory filing schemes). Generally, trademark law protects any word, phrase, logo, or other device that serves to identify the source of goods or services. The definition of protectable trademarks and service marks has been held to include trade dress, including the appearance of product packaging and the interior and exterior designs of businesses, the shape and configuration of products, the color and scent of a product, and sound marks.

### **5. Ideas**

Not everything that is useful or valuable to an employer fits neatly into one of the categories listed above. Plain old “ideas,” whether novel and therefore potentially patentable, reduced to a form that is entitled to copyright protection, or not generally known in the industry, are often critical to increase productivity, line up new markets, and otherwise distinguish a successful company. In limited circumstances, ideas that are not eligible for protection as one of the types of intellectual property described above may be protectable based upon principles of contract law.<sup>9</sup> Given their ill-defined nature, the biggest risk posed to employers from ideas is usually not the failure to secure ownership in them but rather the claims that can arise when an employer uses an employee’s ideas under circumstances that may lead the employee to believe she is owed additional compensation. (See discussion of avoiding misappropriation and litigation claims below.)

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8. 15 U.S.C. § 1051, *et seq.* (the “Lanham Act”).

9. EPSTEIN, Ch. 6 (Aspen Publishers, 2006); ALCES & SEE, THE COMMERCIAL LAW OF INTELLECTUAL PROPERTY (Little, Brown & Company, 1994, 2007 Supp. Aspen Publishers) (hereinafter, “ALCES & SEE”), § 7.3.

## ***B. The Rules of IP Ownership***

Employers often assume that because they pay their employees a salary, all intellectual property developed by their employees belongs to them. Unfortunately, as discussed below, this is not necessarily true. Each type of intellectual property discussed above has its own particular issues in determining ownership and rights of use, and if a company wants to be certain that it owns the IP created by its employees, the best practice is to document its ownership in writing.

### ***1. Copyrights***

The presumptive rule is that the author (creator) of a work of authorship is the owner of the copyrights therein.<sup>10</sup> However, U.S. copyright law recognizes a number of limited exceptions to this rule. First, works that are jointly prepared by two or more authors “with the intention that their contribution be merged into inseparable or interdependent parts” are owned jointly by their authors.<sup>11</sup> Second, individuals and companies can acquire copyrights in a work (in whole or in part) through a purchase, inheritance, or by other means of conveyance.<sup>12</sup> Third, and most importantly for employers, copyrights in a work of authorship will be deemed owned by the employer if an employee creates such work in the course and scope of his employment.<sup>13</sup>

The last rule is NOT the case when the work is developed by a consultant or third-party contractor rather than by an employee. In such case the employer will own the copyrighted work ONLY if: (1) the work of authorship falls within one of nine statutorily specified types of works and there is a written “Work for Hire Agreement” between the creator of the work and the person or company who commissioned its creation; or (2) the copyrights are assigned in writing by the consultant or contractor. The nine types of works that may qualify as works for hire under the first listed circumstance are: a

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10. 17 U.S.C. § 201.

11. 17 U.S.C. § 201(a). If a work consists of a number of separate contributions, then the work is considered a collective work, and the copyrights in each separate contribution will be owned by their respective authors with the copyrights in the collective work being owned by whoever created such work. 17 U.S.C. § 201(c).

12. 17 U.S.C. § 201(d).

13. 17 U.S.C. § 101, definition of “work made for hire.”

contribution to a collective work, part of a motion picture or other audiovisual work, a translation, a supplementary work, a compilation, an instructional test, a test, answer material for a test, and an atlas.

## **2. Patents**

The presumptive rule in patent law is that the individual inventor(s), not his or her employer, owns the patent rights in the invention.<sup>14</sup> This rule is reflected most clearly in Section 111 of the U.S. Patent Act, which states that all patent applications “shall be made, or authorized to be made, by the inventor.” Keep in mind, however, that because patent rights exist only once a patent is granted, state law will likely govern the ownership of ideas, inventions, and trade secrets for which no patent has been issued. (See discussion of ownership of trade secrets and ideas that follows.)

Because all patent applications must be filed in the name of the inventor(s) and the inventor’s(s’) cooperation is likely to be needed to successfully prosecute a patent application,<sup>15</sup> the best practice is for employers to secure ownership of potential patent rights through what is known as an “Invention Assignment Agreement.” In the event that such an agreement is not secured, however, there are some judicially created doctrines that may allow an employer to claim, if not the patent rights, at least the right to use the patented invention. First, an employer may be able to prove that it owns the patent and trade secret rights in an employee’s invention because the employee was “hired to invent.” Second, even if the employee was not hired to invent, if the invention was developed on the employer’s time and in the scope of the employer’s business, the employer may have “shop rights” (meaning the right to use the patent in its business). As discussed below, documentation of the conditions to entitle an employer to claim that an employee was hired to invent, to shop rights, or for assignment of the patent to the employer is important.<sup>16</sup>

## **3. Trade Secrets and Ideas**

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14. 3235 U.S.C. §§ 111, 115–18.

15. ROBERT C. DORR & CHRISTOPHER H. MUNCH, *PROTECTING TRADE SECRETS, PATENTS, COPYRIGHTS, AND TRADEMARKS* (Aspen Law & Business, Supp. 2003) (hereafter, “Dorr & Munch”), §§ 4.14, 5.15.

16. DORR & MUNCH, Ch. 4.

Unlike patent and copyright law, there is no federal law that specifies the presumptive ownership rights of trade secrets or other “good ideas” developed on the job. Because such rights are a creature of state law, the laws of each state where a company is located must be evaluated to determine the applicable ownership rules. In some states, these rules may only be found in case decisions. In other states, like California, they may be spelled out in detail in statutes.<sup>17</sup> Generally, however, the applicable rules of ownership can be modified by contract. For that reason, documentation of the terms and conditions of employment and ownership of these rights is very important.

#### **4. Trademarks and Service Marks**

The rights in trademarks and service marks are generally owned by the company that uses such marks. The principal exceptions to this rule are when marks are used pursuant to a license or by related companies. Thus, unless an employee might claim that a particular trademark or service mark was his “idea,” disputes concerning the ownership of trademarks and service marks are unlikely to arise between an employer and employee.

### ***C. Obtaining Ownership of IP for the Employer***

As indicated in the foregoing sections, an employer is not automatically the owner of all intellectual property created or developed by its employees. The employer must consult with its counsel to institute the necessary policies to ensure it obtains ownership of this valuable property. This may include drafting employment manuals and workplace rules and policies that address this issue. But employment policies alone are usually not enough. Particularly concerning employees who are engaged in research and development or who routinely create copyrighted works, it is important for employers to obtain clear, timely, and written agreements that spell out the ownership of all copyrights, inventions, trade secrets, and ideas that the employee conceives of or develops during her employment. Depending upon the type of IP involved, the written agreement may take the form of an “Invention Assignment Agreement,” a “Work for Hire

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17. See CALIFORNIA CIVIL CODE §§ 980–89.

Agreement,” a “Copyright Assignment,” a “Noncompete Agreement,” or some combination of all four.

For a number of reasons, if an employer has a choice between obtaining a Copyright Assignment agreement or a Work for Hire Agreement from an independent contractor (see discussion of difference above), it should opt for a Work for Hire Agreement. The principal reason for this decision is that, unlike Copyright Assignments, a Work for Hire Agreement is not subject to termination in the future. Pursuant to Section 203 of the Copyright Act, the exclusive or non-exclusive grant of a transfer or license of copyright is subject to termination during a five-year period beginning at the end of 35 years from the date of execution of the grant. Another reason for this preference is that the moral rights of attribution and integrity that are applicable to works of visual art do not attach to works made for hire.<sup>18</sup>

As noted above, not all works of authorship created by independent contractors qualify for treatment as works made for hire. Thus, in addition to opting for a Work for Hire Agreement if it applies, many employers are well-advised to opt for employees rather than independent contractors if their business is highly dependent on the creation of copyrighted works. This is because the works of employees are considered works made for hire even in the absence of a written agreement and, therefore, are automatically entitled to the benefits noted in the preceding paragraph.

The laws of the various states differ on the issue of what constitutes an enforceable invention assignment agreement. California law, for example, states that such agreements are *unenforceable* concerning:

[A]n **invention** that the employee developed entirely on his or her own time without using the employer’s equipment, supplies, facilities, or trade secret information except for those inventions that either:

- (1) Relate at the time of conception or reduction to practice of the **invention** to the employer’s business, or actual or demonstrably anticipated research or development of the employer; or
- (2) Result from any work performed by the employee for the employer.<sup>19</sup>

<sup>18</sup> 17 U.S.C. § 101, definition of “work of visual art.”

<sup>19</sup> CALIFORNIA LABOR CODE § 2870.

Without such a statutory restriction, employers might be tempted to claim ownership of all inventions or ideas that an employee conceives of during his employment whether or not it is related to his work for the employer. However, as with all contracts, a judge may be unwilling to enforce an agreement if it overreaches and is unreasonable. Thus, it is generally recommended that at a minimum, the scope of invention assignment agreements be limited to processes, inventions, works, and ideas that are related to the course and scope of employment. The applicable laws of the state where the employee is located should be researched to determine if any special rules exist.

#### ***D. Protecting IP Rights Once They Are Secured***

Once an employer is certain it has identified existing IP rights and secured the ownership therein, it should decide whether and to what extent it wants to expend money and effort to protect such rights through available registration, business, contractual, and litigation strategies. In Chapter 1, the various statutory methods of protecting copyrights, patents, trademarks, and trade secrets are described in detail. In the section that follows, business, contractual, and litigation strategies are discussed.

### **III. Preventing Employees from Misappropriating and Infringing the Employer's IP**

Once an employer has obtained ownership of the intellectual property it must take steps to protect it. This may include protection against third parties, but all too often, also includes protection against one's own employees.

#### ***A. General Business Strategies***

##### ***1. Education and Counseling***

As the foregoing discussion reveals, there are a lot of misunderstandings and misconceptions about the scope and ownership of IP rights. If these misunderstandings and misconceptions can exist among educated business lawyers and corporate executives, it is easy to understand how they may also exist among employees and plaintiff's lawyers. Thus, one of the simplest ways for an employer to prevent employees from misappropriating and infringing its IP rights is to engage in appropriate educational programs. At a minimum, employees should be informed of the nature and identity of the IP rights the employer claims. The agreements discussed in the preceding and following sections will, obviously, perform an educational function, but other strategies might also be employed, such as workshops on IP law.

If an employee is hired with the expectation that he or she will develop patentable products or procedures, or will develop software or customer lists or special formulae for restaurants, it is imperative that the employee be instructed in the proper method of dealing with the production and protection of that information. Such efforts are within the realm of the pure intellectual property lawyer, rather than the business lawyer or the employment lawyer, but even the business and employment lawyers should be familiar with the general outlines of the issues so that IP specialists can be involved when necessary.

## **2. *Written Agreements***

One way to educate employees about their duties concerning an employer's IP rights is to obtain a written agreement in which employees: (1) acknowledge the existence of the employer's IP rights; (2) agree that the employer owns any IP rights created during the course and scope of their employment (see discussion above); and (3) promise not to infringe or misappropriate the IP rights of the employer. These agreements can take many forms, from an all-encompassing "Employment Agreement" to a series of agreements that are IP-specific (e.g., an invention assignment agreement, a work-for-hire agreement, and a copyright-assignment agreement).

Two other forms of agreements employers often use in an effort to educate employees and protect IP (particularly trade secrets) are the "Noncompete Agreement" and the "Confidentiality Agreement."

State laws vary greatly regarding the limitations on and enforceability of noncompetition agreements.<sup>20</sup> However, even in instances in which a noncompetition agreement with an employee is unenforceable, a confidentiality or nondisclosure agreement is normally upheld.

### ***3. The Employment Manual and Policies***

One way to educate employees about their duties concerning an employer's IP rights is to include a discussion of such rights and duties in a company's employment policies and manuals. However, while such policies or manual will help to reduce disputes, it is generally recommended that employers utilize employee-specific written agreements for all employees who are directly engaged in inventive and creative activities.

### ***4. The Exit Interview***

The use of exit interviews with employees can be very helpful in ensuring that an employer's IP rights are not infringed or misappropriated. These interviews afford the employer the opportunity to obtain copies of any confidential information and the reaffirmation by the employee that he or she will not disclose any confidential information. Such termination procedures are also cited by courts as evidence of proper trade secret protection procedures. As a practical matter, if the employee refuses to acknowledge the confidential nature of the information, the client will be aware of the possible breach of confidence and may take other defensive measures. Alternatively, if the employee does acknowledge the existence of a trade secret but later breaches the agreement, the client's burden of proof in litigation may be met more easily.

## ***B. Strategies That Are IP-Specific***

### ***1. Copyrights***

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20. BRIAN M. MALSBERGER, COVENANTS NOT TO COMPETE: A STATE-BY-STATE SURVEY (BNA Books, 5th ed. 2006); MARK A. ROTHSTEIN, CHARLES B. CRAVER, ELINOR P. SCHROEDER, & ELAINE W. SHOEN, EMPLOYMENT LAW Ch. 8 (Thomson West, 3d ed. 1999).

A copyright gives the owner several affirmative and exclusive rights. These include the exclusive rights to reproduce the work, prepare derivative works, distribute copies of the work, such as by sale; to perform the work; and to display the work.<sup>21</sup> In addition, the owner of the copyright may license others to utilize these rights.<sup>22</sup>

As noted in Chapter 1, it is generally recommended that copyright owners register their copyrights with the U.S. Copyright Office. Although this is not necessary to secure copyright protection, it is needed to preserve certain remedies for infringement and is a prerequisite to bringing a copyright infringement claim.

Employees who create works of authorship may not be aware that because the copyrights in those works are automatically owned by their employer pursuant to the work-for-hire doctrine, they are restricted by copyright law from utilizing those works in the future without the consent of their employer. Thus, particularly upon the departure of an employee, it is good practice for employers who generate copyrightable works to educate their employees about copyright law and to clearly identify those works that are off limits for the employee's future use.

## **2. Patents**

Unlike copyright registration, which, absent an unusual situation, is routinely granted, a patent is issued only after examination and scrutiny by an examiner of the U.S. Patent Office or a foreign patent office. Utility and plant patents are generally valid for 20 years from the date the patent application was filed.<sup>23</sup> A design patent is valid for 14 years from the date the patent is issued.

The effect of the grant of a patent is that the owner has the right to exclude others from making, using, offering for sale, or selling the invention, or importing the invention into the United States.<sup>24</sup> Thus, as with copyrights, if an employer owns patent rights, it has the right to prevent current and former employees from utilizing its patented inventions. By definition, however, patent rights do not extend to general knowledge and scientific principles, including the general know-how that employees gain through experience. Generally, if an

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21. 17 U.S.C. § 106.

22. *See generally*, EPSTEIN, Ch. 4.

23. 35 U.S.C. § 154.

24. 35 U.S.C. § 154; *See generally*, EPSTEIN, Ch. 5.

employer wants to prevent an employee from utilizing such information, its only option is to attempt to successfully assert a trade secret infringement claim.

### 3. Trade Secrets

Protection of trade secrets is one of the most important considerations in the employment context. Unlike copyrights that are protected as a matter of federal law upon creation (and that receive greater protection by federal registration), or patents that are protected upon the issuance of a patent by the U.S. Patent and Trademark Office, trade secrets are creatures of state law and are not protected by any federal filing or registration procedure. They are protected only if their secrecy is maintained.<sup>25</sup>

Means for protection of trade secrets will vary greatly with the type of information involved and the nature of the employer's use of the information. Unfortunately, it is not until a lawsuit for trade secret misappropriation is filed that an employer's subjective beliefs regarding the existence of a valid trade secret, the performance of reasonable steps to keep it secret, and the imposition of a confidential relationship between the client and third parties will be tested. If the client has failed to take the necessary protective steps, it may be too late to protect its interest in the information or materials.

Concerning employees, it is recommended that the employer limit the accessibility of its trade secrets to those employees who need to know or use them. Those employees must agree, expressly or by implication, that they have a duty to preserve the trade secrets. The employer should utilize good security procedures, including such simple measures as locking confidential material when not in use, limiting access to computer data by passwords, and prohibiting employees from removing trade secret documentation from the office or area in which it is used. Sensitive materials should be shredded rather than discarded. The enormous amount of information stored on computers makes it essential that the client consider how it uses e-mail, electronic transmission, and other communication systems, and to determine who can access the information stored on its computers and in digital form.

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25. EPSTEIN, Ch. 2; DORR & MUNCH, Ch. 2; ALCES & SEE, Ch. 3.

The employer must educate its employees and others given access to confidential information regarding the need to preserve it in secrecy. Simple inattention is a common problem that can be reduced by simply sensitizing employees to the need for confidentiality. This education can be accomplished through training meetings, the circulation of written policies regarding trade secrets protection, and signs and posters in the workplace. Counsel to the employer can assist in drafting policies and procedures and in auditing the employer's compliance with those procedures. The failure to enforce written policies for the protection of trade secrets can be as damaging as the failure to adopt any policies.

It is also important to recognize that trade secrets are protected only against misappropriation, such as by theft, bribery, misrepresentation, breach of a confidential relationship, or industrial espionage. Although cases of true espionage exist, the vast majority of trade secrets cases arise in the context of breach of a confidential relationship. Although a court can find the existence of a confidential relationship without a written contract or confidentiality agreement, the existence of a written agreement eases the burden of proof. At a minimum, there must be evidence that the plaintiff notified the defendant that the information was considered confidential and instructed the defendant to hold it in confidence.

Although general policies or employment agreements may protect many of a company's trade secrets, employers should be urged to utilize specific confidentiality or nondisclosure agreements with employees having access to trade secrets.<sup>26</sup> (See discussion of these agreements above.) The contents of a confidentiality agreement will obviously vary greatly based upon the relative bargaining position of and the relationship between the parties. Often a confidentiality agreement will acknowledge the existence of a confidential relationship or of an obligation to maintain secrecy; identify the existence of trade secrets; restrict the right to further use, disclose, or communicate the confidential material; agree to return all evidence of the material upon termination of the relationship, and acknowledge that damages or injuries would result from disclosures and stipulation of the necessity of injunctive relief.

While a confidentiality agreement will not prevent an employee from leaving and utilizing the general knowledge and understand-

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26. BRIAN M. MALSBERGER, *EMPLOYEE DUTY OF LOYALTY: A STATE-BY-STATE SURVEY* (BNA Books, 3d ed. 2005).

ing gained in the course of employment, it can prevent use of actual trade secrets. Will such an agreement preserve an employer's list of customers? This depends a great deal on the local jurisdiction, but many cases find that a customer list is not a trade secret, as it is (or could be) known to anyone in the industry, based upon simple use of telephone books, etc. While some jurisdictions hold otherwise, a noncompete agreement may preserve the competitive advantage of that list of customers.

If an exit interview indicates that an employee is leaving to begin work with a competitor, or if a client otherwise believes that its trade secrets may have been disclosed, it should immediately notify any third person it believes may obtain this information. Under the state laws governing trade secrets, third parties who have notice that materials they receive constitute trade secrets can also be liable for misappropriation. If the client can give actual notice to a third party that it suspects trade secrets are being disclosed, the client will be relieved of the burden of having to prove that the circumstances were such that the third parties should have known of the improper disclosure.

### ***C. Litigation***

Litigation against employees or competitors misappropriating trade secrets or infringing other IP rights may be necessary. Often the first step in the litigation process will be to seek a temporary restraining order or a preliminary injunction pending the conclusion of a trial on the merits. Although the exact test for such preliminary relief will depend upon applicable law and procedure and the jurisprudence of the court where the case is filed, the plaintiff can expect to be required to show that there is no adequate remedy at law, that it will suffer irreparable injury if the injunction is not issued, and either that there is a strong likelihood of success on the merits or at least a strong balance of competing equities in its favor. Further, concerning a trade secret claim, the plaintiff typically must demonstrate that there is a real threat of disclosure of trade secrets.<sup>27</sup>

Assuming that the plaintiff is successful in proving its case at trial, the court may order several permanent remedies. Often the most desirable is a permanent injunction against use of the employer's IP rights. Depending upon the jurisdiction and the facts, the injunction may last indefinitely or for a limited time. For instance, the laws of

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27. See generally, MALSBERGER, TRADE SECRETS.

most states permit an injunction to be later terminated if the trade secret has ceased to exist, as would occur if the information became public knowledge, either through disclosure by the plaintiff, or by independent development and disclosure. Additionally, all of the IP regimes discussed above allow an injured party to recover monetary damages, although the four regimes differ somewhat on what type of evidence is required to prove entitlement to a monetary award.

## **IV. Avoiding Liability to Third Parties**

While earlier sections of this chapter have focused on the problems faced by the employer in protecting its intellectual property from loss, the employer must be aware that actions of its employees can subject it to liability to third parties. There are several risks of which the employer should be aware, and several procedures and safeguards that it must take in order to reduce the risks of liability.

### ***A. Counseling an Employer Hiring from a Competitor***

An employer may wish to move into another area or product line. There are a number of ways to accomplish this. The first thing that may come to mind may be to hire someone knowledgeable in the area from another company. Why not? Are there any risks in such a procedure?

Definitely! Just as your client may wish to protect its intellectual property, the competitor will want to protect its intellectual property as well. By hiring employees who are privy to the trade secrets and other intellectual property of a competitor, your client may be unknowingly (or knowingly) involved in misappropriating those trade secrets and other intellectual property and may be the defendant in an injunction action brought by the prior employer.

Assuming the employer innocently proceeds with hiring an employee from a competitor, it should be advised to check for the existence of any noncompetition agreements or confidentiality agreements with the prior employer and should document that it does not condone misappropriation of the competitor's trade secrets and

other intellectual property. To the extent possible, it should assign the employee to areas of the business other than those in direct competition with the prior employer. Finally, it should be aware of the possibility of a lawsuit.<sup>28</sup>

### ***B. Avoiding Infringement or Theft of IP***

To the extent an employee “borrows” ideas, inventions, or content from a third party and uses it in the course of her work, her employer may be liable to such third parties for infringement of their IP rights. This could arise from use of another’s patented or copyrighted material without a proper license or from copying of commercial newsletters and downloading music and software without authority. Employees in marketing departments must be educated to the rights of competitors in their trademarks and service marks. An employee who designs packaging, brochures, logos, or other designs should avoid any designs that are confusingly similar to those of competitors or the employer may find itself in a trademark infringement suit. Employees must be educated to understand that the employer respects the properties of others, and that they may not use another’s property without authority. Equally important is education to avoid claims of theft or misappropriation of others’ ideas or trade secrets. While trade secrets are not protected against independent development or reverse engineering, obtaining copies of another’s internal documents and manuals in order to learn the details of trade secrets is clear misappropriation. While ideas have only limited and spotty protection, they are sometimes given protection. The employer must insure that its employees do not solicit ideas from third parties and then use them as their own. In fact, most companies institute procedures to refuse ideas from outside sources, in order to reduce the risk of claims of theft.<sup>29</sup>

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28. EPSTEIN, Chapter 3; DORR & MUNCH, § 2.10.

29. EPSTEIN, § 6.03.

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