The Protection of Confidential Information

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This article describes some ways of protecting confidential information and some of the associated problems that may arise. In particular, the areas of trade secrets, confidential information, confidentiality agreements and non analysis agreements are considered. The protection of confidential information is dealt with under two main categories: Protection in the employment situation and protection when dealing with third parties.

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Intellectual property can be differentiated into two main categories: That which is published, such as patents, trademarks and copyright, and intellectual property which is confidential. The protection of such confidential information is of vital importance to most organizations, and is of particular importance, given the frequency of changes in employers and the emergence of joint ventures, which are common in modern life.

Protection of Information in the Employment Situation

The courts have found it remarkably difficult to define trade secrets and usually prefer to give examples rather than attempt to formulate a definition. The Faccenda case¹ gave as examples ‘secret processes of manufacture such as chemical formulae’, ‘design and special methods of construction’ and ‘other information which is of a sufficiently high degree of confidentiality to amount to a trade secret’. The last example is rather circular and one might state that like an elephant a trade secret is easier to recognize than to define.

It is, however, very important to be able to decide whether or not a particular piece of information constitutes a trade secret, since, if it is not a trade secret then it is not capable of being protected either by a express clause in the employment agreement ‘not to make use of the confidential information’ or by a quia timet injunction.

It may be worth considering here the duties that an employee owes to an employer both during the employment and post-employment. During employment, the employee owes the employer a duty of confidence which may be stated in the employment contract, but if not it will be implied by law that the employee will serve the employer with ‘good faith and fidelity’.²,³

When employment ceases any obligation that the ex-employee owes will be defined by any restraint of trade clause that was in the contract or by the general law of confidence. A restraint of trade clause would typically prevent an ex-employee from disclosing confidential information. However, under the Indian Contract Act (Section 27) any agreement of ‘restraint of trade’ is void. An express clause in the employment agreement ‘not to make use of the confidential information’ however, serves the same purpose. If no restraint of trade clause were present in the contract of employment, an employer may also rely on the law of confidence as in the Coco case⁴ where the elements needed to establish an action for breach of confidence were described as:

(i) the information must have the necessary quality of confidence
(ii) the information must have been imparted in circumstances importing an obligation of confidence
(iii) there must be an unauthorized disclosure.

Thus even in the absence of a restraint of trade clause the employer has some protection regarding unauthorized disclosure or use of confidential information. However, this protection must be assessed in the light of Ocular Sciences case⁵ where it was held that for public policy reasons an employee was entitled to use and put at the disposal of new

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employers all acquired skill and knowledge whether or not it was secret at the time the employee acquired it. Where there is a conflict between an employers’ right to protect confidential information and public policy, the latter prevails. Similarly in *Faccenda*, the Court of Appeal held that the obligation of confidence existing post-employment was more restricted than that which operated during the currency of the employment contract. In *Faccenda*, the UK Court of Appeal identified four aspects which are relevant to differentiating between trade secrets and other information which could not be protected post-employment, and the most relevant are:

1. Has the information been given to only a limited number of employees
2. Has the employer impressed on the employee the confidentiality of the information
3. Can the confidential information be easily separated from other information acquired by the employee during the course of employment.

Thus identification of trade secrets or confidential information is very important. It is also important to differentiate between confidential information and know-how, which is the general skill and knowledge that an employee acquires during the course of employment that can be transferred to a future employer.7

In considering cases regarding employees and trade secret/confidential information, care should be taken when relying on UK cases. The UK courts take a very strict approach to restraint of trade clauses, especially where their effect is to prevent an employee from working, and if such a clause is found to be too wide then it is void. In New Zealand, however, if a restraint of trade clause is too wide then by Section 8 of the Illegal Contracts Act 1970, the court may modify the clause and apply the clause as modified. Thus a New Zealand court, being able to separate out (say) trade secrets and know-how might excise the know-how and apply the modified clause involving only trade secrets, whereas a UK court would find the whole clause void and of no effect, which is also the case in India.

**Protection of Confidential information and Third Parties**

The protection of confidential information that is to be disclosed to third parties needs careful consideration. The first matter to be decided is the drafting of a suitable confidentiality agreement. This is not a routine matter and thought must be given to such aspects as the duration of the confidentiality period, to whom disclosure may be made, any exceptions and the destruction of samples or copies of the information when the agreement ends, amongst other matters.

The area of confidential information and disclosure to third parties was recently considered by the New Zealand Court of Appeal and the Privy Council in the *Norbrook Laboratories* case.8

The Court of Appeal held that in order to succeed in a claim for breach of confidence, the plaintiff had to establish that the information was of a confidential nature, that it had been communicated in circumstances importing an obligation of confidence and that the defendant had made or was about to make an unauthorized disclosure of the information. The Court of Appeal also held that the onus was on the plaintiff to prove misuse and that in a commercial situation there was no presumption against a party in possession of confidential information. The Privy Council agreed that the burden of proof lay on the plaintiff, but stated that if the plaintiff adduces evidence from which, in the absence of any adequate explanation, an inference of breach may properly be drawn, an evidential burden or provisional burden fell on the defendant.9 Thus, if A entrusts B in confidence with confidential information, and B is precluded by contract from using that information for its own purposes, and the relationship between them ends, and B markets a product which could not ordinarily be made without using A’s confidential information, a claim by A for breach of contract is likely to succeed unless B shows that it obtained the information from another legitimate source, or as a result of independent research, or in some other manner not involving misuse of A’s information. In this context, it is interesting to note that the Court of Appeal stated that the purpose of the law of confidence was to prevent disclosure and misuse and not to stifle competition. Thus possession of confidential information did not of itself preclude a person from developing an equivalent product, provided that the confidential information was not misused.

On the facts of the case, the Court of Appeal agreed with the High Court that the defendant had not misused the confidential information but had merely taken some comfort from that information. The Privy
Council came to the opposite conclusion and allowed the appeal. It is a noteworthy aspect of the litigation that the High Court made two important findings of fact that the Court of Appeal held were wrong. The Privy Council also disagreed with the Court of Appeal and found that the defendant disclosed the confidential information ‘exactly and unambiguously’ whereas the Court of Appeal found no misuse of information by the defendant.

However, a confidentiality agreement may be insufficient to protect fully the interests of the disclosing party, and a non disclosure or non-analysis agreement (NAA) may also be necessary.

The use of NAAs to prevent the analysis of samples or reverse engineering is becoming increasingly common, either as agreements in their own right or as part of confidentiality agreements.

The importance of NAAs has been highlighted by a recent case in the English High Court. The case has since been heard in the Court of Appeal where it was upheld without disturbing and of the legal principles stated in the High Court.

This case involved chemicals and the plaintiff supplied the defendant with product under a confidentiality agreement but without an NAA. The High Court held that if a product was supplied in confidence and was copied completely there was a breach of confidence. However, if the formula was in the public domain, the formula could not be confidential. The same was true for the constituents. In the absence of an NAA, the defendant could not be prevented from analysing the plaintiff’s product and from using information that was in the public domain but which had been acquired by that analysis.

In particular, the defendants submitted that this defence was available to them whether or not they had used public sources. The High Court held:

(i) It did not follow that just because the products had been supplied in confidence that the products and their properties were confidential information. It was necessary to look at the product and its constituents to decide whether the product had a confidential nature due to the work that had been done on it. The existence of the products and the fact that they worked meant that their purpose was not confidential. Confidentiality, if there was any, lay in how the products were made up.

(ii) If a product was supplied in confidence and was then copied completely, there would be a breach of confidence because the defendant would have used the product of the plaintiffs’ brains, time and energy.

(iii) It followed from point (ii) above that if there had been something confidential which the defendants had copied that would have been actionable. However, a thing did not become confidential merely because it was supplied confidentially. If a supposedly secret formula was in the public domain then the formula could not be confidential. The same was true as regards the constituents. The plaintiffs had publicly stated what type the constituents of its products were, and if there was material in the public domain which pointed to specific constituents, that could not be said to be confidential. In the absence of an NAA, the defendants could not be prevented from examining and analysing the plaintiff’s products and from using information which was in the public domain but which had been acquired by that analysis.

(iv) The plaintiff’s formulation of its case was not sustainable, i.e. that the specific products and their make-up prevented a party from analysing that product (in the absence of NAA) and using those parts of the constituent products and method of making up which were in the public domain. This would lead to the result that by signing a confidentiality agreement the defendant would be the only person in the world that could not carry out such activities.

Thus, when a product is supplied to a third party an NAA should always be drafted to prevent either analysis or reverse engineering. Should the product consist entirely of known materials the necessity of an NAA is obvious.
Conclusion

It can be seen that the protection of confidential information, while essential, is not straightforward. It is clearly important for all organizations to have in place a system to identify confidential information and to take steps to protect it. Such steps would include ensuring that appropriate terms are present in the contracts of employment, impressing the confidentiality of such information upon employees and restricting the availability of confidential information to a ‘need to know’ basis. If any confidential information is to be disclosed outside of the organization, appropriate confidentiality and non-disclosure agreements need to be entered into.

References
1 Faccenda Chicken v Fowler [1985] 1 All ER 724.
2 Robb v Green [1895] 2QB 315.
6 Printers & Finishers Ltd v Holloway 1085 RPC 239.