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A Guide to Trade Secret Protection without a Non-Compete

In a world where employees routinely jump ship to competing companies, courts struggle over whether a presumption of inevitable disclosure of trade secrets protects core intellectual property or instead acts as a backdoor to a missing or illegal noncompetition clause.

By Joseph Casino, Thomas Landman, and Rikesh Patel – September 15, 2020

Companies can effectively use trade secret protection to respond to an environment in which their competitors seek to hire their best and brightest stars. Trade secret law protects confidential formulas, patterns, compilations, databases, programs, devices, methods, techniques, and processes. The ability to protect such secrets may help a company preserve its economic and strategic advantages over competitors while hindering competitors' efforts to make and market viable competing products. Trade secret law protects against unauthorized disclosure and may be used instead of, or as a complement to, patent and copyright protections, which inherently involve public disclosure. As companies focus on protecting trade secrets, trade secret protection is growing: Most state legislatures have adopted the Uniform Trade Secrets Act (UTSA), Congress has enacted the Defend Trade Secrets Act of 2016, Pub. L. No. 114-153, 130 Stat. 376 (DTSA), and courts have expanded common-law protections.

Employers whose former employees have been lured away by competitors often suspect theft. Indeed, allegations that an ex-employee stole a company's valuable trade secrets are commonplace—motivated, for example, by the ex-employee having been intimately involved with a company's technology. However, proving such trade secret theft can be challenging because confidential information can be easily transferred or remembered. Where an ex-employee likely will use the former employer's trade secrets at a new job but where it would be difficult to prove intentional or inadvertent theft of those secrets, courts have relied on the inevitable disclosure doctrine to fill the gap.

The Inevitable Disclosure Doctrine

The inevitable disclosure doctrine permits a former employer to prove a claim of trade secret misappropriation by proving that the ex-employee's new employment in a closely related field will inevitably lead to the use of the trade secrets. The proof required by the inevitable disclosure doctrine, that there is no credible way that the employee will not use the trade secret at the new employer, is generally easier to establish than actual misappropriation of the trade secret.

The principle underlying the inevitable disclosure doctrine is based in equity and was first applied in *PepsiCo, Inc. v. Redmond*, 54 F.3d 1262, 1269 (7th Cir. 1995). In *PepsiCo*, the defendant was a high-level manager at PepsiCo who quit to join a competitor. The defendant had signed a confidentiality agreement with PepsiCo but had not signed any noncompete agreement.

Nevertheless, the Seventh Circuit affirmed a preliminary injunction restraining the new employment, explaining that "a plaintiff may prove a claim of trade secret misappropriation by demonstrating that defendant's new employment will inevitably lead him to rely on the plaintiff's trade secrets." *Id.*

The *PepsiCo* decision effectually creates noncompete protection even when the parties never agreed to do so.

Trade Secret Law in the United States

Trade secret law in the United States exists both at the state and federal levels, and federal trade secret protection does not preempt or supplant the state protection. Every state except New York and North Carolina has substantially adopted the UTSA. At the federal level, the DTSA created a federal cause of action for misappropriating trade secrets. 18 U.S.C. § 1836(b). It provides private parties a right to seek damages and injunctive relief. The DTSA provides injunctive relief to prevent actual or threatened misappropriation, as long as the injunctive relief does not "prevent a person from entering into an employment relationship" and any conditions placed on employment are based on "evidence of threatened misappropriation and not merely on the information the person knows." *Id.* § 1836(b)(3)(A)(i)(I). Thus, a party seeking injunctive relief under the DTSA would need to meet a heightened evidentiary standard by providing proof of an imminent threat of misappropriation that is based on more than what the employee knows. Commentators have viewed this standard as requiring increased proof for inevitable disclosure rather than eliminating the doctrine. *E.g.*, Symposium, "Understanding the Defend Trade Secrets Act (DTSA): The Federalization of Trade Secrecy," 50 *Loy. L.A. L. Rev.* 331, 339 (2017).

California Courts' Rejection of the Inevitable Disclosure Doctrine

Inevitable disclosure was at the center of a May 2020 California appellate court decision in a case between Apple Inc. and start-up Hooked Media Group. *Hooked Media Grp., Inc. v. Apple Inc.*, No. H044395, 2020 WL 2765770 (Cal. Ct. App. May 28, 2020). The court rejected injunctive relief under the inevitable disclosure doctrine, holding that Apple did not misappropriate Hooked's trade secrets when Apple hired away Hooked's key employees.

Hooked had developed a recommendation app for mobile devices. The app provided users with suggestions for other apps they might enjoy based on usage patterns. In 2013, Apple expressed interest in acquiring the start-up through an "acqui-hire," a Silicon Valley term for effectively buying another company's employees, but ultimately did not do so. *Id.* at *1. Hooked's chief executive officer (CEO) settled on a plan to "sell" three of its engineers to Apple, including Hooked's chief technology officer (CTO). Apple initially responded that it might pay Hooked a "finder's fee" for the engineers, but it never paid a fee. *Id.* Instead, it contacted two of the engineers directly and hired them. Meanwhile, the third (Hooked's CTO) was also in private negotiations to join Apple. Upon learning of these negotiations, Hooked's CEO fired the CTO and sent an email demanding that the former CTO return all Hooked company property, including "copies of confidential technical information kept on his personal computer." *Id.*

Hooked's CEO also emailed Apple's general counsel expressing concern about the three former Hooked employees retaining Hooked's confidential information. Apple responded that it had no desire to use Hooked's trade secrets and would facilitate the return of all confidential information the former employees had. *Id.*

Several months later, Hooked sued its former CTO and Apple for, inter alia, trade secret misappropriation. In the complaint, Hooked alleged that Apple had misappropriated Hooked's "technical information, such as algorithms and app recommendation strategies," in violation of the California UTSA (CUTSA). *Id.* at *3. The court found no evidence that Apple's actions met the CUTSA standard for improper use or acquisition. Hooked's claim relied on circumstantial evidence: "[I]ts former employees were assigned to tasks at Apple similar to the work they did at Hooked and within weeks one of them produced a detailed plan for a recommendations system much like Hooked's version." *Id.* The court noted that, although "an expert opined that the source code for Apple's recommendation system was similar to the source code for Hooked's," "suggest[ing] the engineers drew on knowledge and skills they gained from Hooked to develop a product for their new employer," "California's policy favoring free mobility for employees specifically allows that." *Id.*

The court derived California's policy from *Whyte v. Schlage Lock Co.*, 125 Cal. Rptr. 2d 277, 294 (Cal. Ct. App. 2002), which rejected the "inevitable disclosure" doctrine. It held that "[a]llowing an action for trade secret misappropriation against a former employee for using his or her own knowledge to benefit a new employer is impermissible because it would be equivalent to *retroactively* imposing on the employee a covenant not to compete." *Hooked*, 2020 WL 2765770, at *3. The court explained that "[t]he chief ill in the covenant not to compete imposed by the inevitable disclosure doctrine is its after-the-fact nature: The covenant is imposed *after* the employment contract is made and therefore alters the employment relationship without the employee's consent." *Id.* (quoting *Whyte*, 125 Cal. Rptr. 2d at 293).

The Inevitable Disclosure Doctrine in Other States

Adoption of the doctrine of inevitable disclosure varies by jurisdiction. Arkansas, Connecticut, Delaware, Illinois, New York, and Ohio have cautiously adopted the doctrine; California, Kentucky, Louisiana, Maryland, and Massachusetts have rejected it; and other states allow the doctrine to be applied only in limited circumstances, such as where evidence of actual misappropriation exists. Many state courts have yet to rule directly on the doctrine.

Courts in jurisdictions that recognize inevitable disclosure have used the doctrine as the basis for enforcing covenants not to compete, establishing irreparable harm in granting preliminary injunctions, finding threatened misappropriation of trade secrets, and enjoining a former employee from working for a competitor even in the absence of a covenant not to compete. *See, e.g.*, *Orthovita, Inc. v. Erbe*, C.A. No. 07-2395, 2008 WL 423446, at *6 (E.D. Pa. Feb. 14, 2008). The success of an allegation of inevitable disclosure is highly dependent on the particular facts. When deciding whether the disclosure of a trade secret would be inevitable, courts have considered

- the similarity between the employee's former and current positions;
- the competition between the former and current employers;
- the current employer's efforts to avoid the former employer's trade secrets;
- the value of the trade secrets to both employers;
- the technical nature of the trade secrets;
- whether the employee is a high-level employee or provides unique services; and
- the balance between the competing policy interests of robust trade secret protection to promote innovation and protect corporate investments, on the one hand, and of employee mobility to protect employees' freedom to work in a field of their choosing and to facilitate the efficient allocation of labor, on the other.

See, e.g., *Molon Motor & Coil Corp. v. Nidec Motor Corp.*, No. 1:16cv03545, 2017 WL 1954531, at *5 (N.D. Ill. 2017); *Int'l Paper Co. v. Suwyn*, 966 F. Supp. 246, 258-59 (S.D.N.Y. 1997); *Marietta Corp. v. Fairhurst*, 754 N.Y.S.2d 62, 65–66 (N.Y. App. Div. 2003).

As a counterpart to inevitable disclosure, courts often simultaneously weigh "the threat of misappropriation." Section 2(a) of the UTSA provides that "[a]ctual or threatened misappropriation may be enjoined." The recently enacted Massachusetts version of the UTSA, for example, provides that "[a]ctual or threatened misappropriation may be enjoined upon principles of equity, including but not limited to consideration of prior party conduct and circumstances of potential use. . . ." Mass. Gen. Laws ch. 93, § 42A(a).

The DTSA, as explained above, similarly allows an injunction to be granted for the threatened misappropriation of a trade secret, but it expressly prohibits injunctive relief that would prevent a person from entering into an employment relationship, and it requires that conditions placed on employment be based on evidence of threatened misappropriation, not merely on the information the person knows. *See* 18 U.S.C. § 1836(b)(3)(A)(i)(I). While allowing injunctions for "threatened misappropriation," the DTSA requires evidence of that threat and does not allow employee knowledge to be the sole basis of an injunction. Therefore, state UTSA law may be stronger for some claims of inevitable disclosure.

Courts are grappling with how to differentiate between inevitable disclosure and threatened misappropriation. In *Barilla America, Inc. v. Wright*, No. 4-02-CV-90267, 2002 WL 31165069 (S.D. Iowa July 5, 2002), for example, the court explained that the two concepts are aimed in different directions. "The inevitable disclosure doctrine appears to be aimed at preventing disclosures despite the employee's best intentions, and the threatened disclosure doctrine appears to be aimed at preventing disclosures based on the employee's intentions." *Id.* at *9. Meanwhile, the California Court of Appeal for the Fourth Appellate District has held that the inevitable

disclosure doctrine is "based upon an inference (based in turn upon circumstantial evidence)," distinguishing it from actual or threatened misappropriation of a trade secret, which requires proof. *See Whyte*, 125 Cal. Rptr. 2d at 292.

Recent DTSA Cases Relying on the Inevitable Disclosure Doctrine

In *General Electric Co. v. Uptake Technologies, Inc.*, 394 F. Supp. 3d 815 (N.D. Ill. 2019), GE sought injunctive relief and damages from Uptake and six high-ranking former GE employees who had left for Uptake, a technology competitor. GE alleged "both actual and threatened misappropriation" and that "the individual defendants cannot perform their jobs at Uptake without inevitably disclosing GE's trade secrets and confidential information." *Id.* at 832. Uptake moved to dismiss, and the court considered the claims under the inevitable disclosure doctrine separately for the Illinois UTSA and the DTSA. Citing *PepsiCo*, the court noted that Illinois recognizes the doctrine of inevitable disclosure to prove a claim of trade secret misappropriation by demonstrating that a defendant's new employment will inevitably misappropriate the trade secrets. *Id.* at 832–33. Moreover, rejecting the defendants' argument that the DTSA does not recognize the inevitable disclosure doctrine, the court asserted it acted consistently with other courts in the same district in finding that a DTSA claim based on inevitable disclosure may survive a motion to dismiss.

In *Jazz Pharmaceuticals, Inc. v. Synchrony Group, LLC*, 343 F. Supp. 3d 434 (E.D. Pa. 2018), Jazz sued Synchrony for alleged violations of the DTSA and Pennsylvania Uniform Trade Secrets Act (PUTSA). Jazz and Synchrony had entered into an agreement that included provisions to protect Jazz's confidential information, which Synchrony subsequently had access to for several years. Before the end of the agreement, Synchrony informed Jazz of its intent to work for a competing pharmaceutical firm. Jazz asserted claims against Synchrony for violations of the DTSA and PUTSA, moving for a temporary restraining order and a preliminary injunction. In ruling on the adequacy of a stipulated preliminary injunction, the court observed that the Third Circuit has held that where there is substantial overlap with work for a former employer, "a district court may conclude that those employees would likely use confidential information to the former employer's detriment." *Id.* at 446 (citing *Fres-co Sys. USA, Inc. v. Hawkins*, 690 F. App'x 72, 76 (3d Cir. 2017)). The court explained in a footnote that its "inevitable disclosure" finding applies to both the DTSA and the PUTSA. *Id.* at 446 n.52.

Conclusions

There will be more litigation relying on inevitable disclosure theories, particularly in states that have not rejected this doctrine. Employers should consider the extent to which noncompetition agreements are allowed in their state when hiring employees. If permitted to rely on inevitable disclosure, an employer should still consider evidence to show why the trade secret at issue would be relied on at a competitor and why it would be unlikely that the ex-employee and competitor could avoid using that trade secret. Employers also should consider how the competitor may have changed its products or strategies after hiring the new employees.

Ultimately, each case will turn on its individual facts, but parties and their counsel should be well versed in the inevitable disclosure doctrine and its potential to help employers protect their trade secrets from misappropriation.

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