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# 1983 TRADE SECRETS LAW HANDBOOK

by Melvin F. Jager

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# About the Author

**Melvin F. Jager** is a partner of the Chicago firm of Lee, Smith & Jager. He is a member of the Illinois and District of Columbia Bars, and has been engaged in the private practice of intellectual property law continually since 1962. He holds a Bachelor of Science degree and a Juris Doctor from the University of Illinois. His experience encompasses litigation, prosecution and consultation in patent, trademark, copyright, trade secret, licensing, and antitrust matters. He also has lectured in patent law as Adjunct Professor of Law at the Northern Illinois University School of Law. Mr. Jager is currently Chairman of the Council of the Patent, Trademark and Copyright Section of the Illinois Bar Association, and former Vice-Chairman and Editor of the Section Newsletter.

# Preface

The 1983 TRADE SECRETS LAW HANDBOOK provides the bench and the bar with an up-to-date source of the law in the expanding field of trade secret protection. The 1983 revisions also include topics which expand the coverage of previous editions.

Chapter 9 has been added to the HANDBOOK to apprise the practitioner of the current developments in the law governing the trade secret protection of computer software. As everyone knows, the computer industry in America has blossomed into a multi-billion dollar business. This growth has created a shortage in highly skilled personnel, such as programmers. High employee mobility has created a strong upsurge in employment-related trade secret cases in the computer field. The high stakes in the market also induce computer companies to enforce their valuable trade secrets by litigation, if necessary. Chapter 9 sheds light on the state of law in this expanding area.

Chapter 10 has been added to discuss the interesting and multifacted interfaces between trade secrets and the patent and copyright laws. The federal preemption arguments are explored, and the cases dealing with seemingly inconsistent efforts to copyright material while maintaining its secrecy are analyzed and explained. The problems and policy considerations relating to the rights of trade secret owners versus patent owners on the same idea are also explored.

Finally, Chapter 11 has been added to introduce the very important topic of the relationship between trade secrets and the antitrust laws. The history of trade secrets as an alleged restraint of trade is traced. The types of restrictions which can be imposed in trade secret licenses, as ancillary to the transfer of the secret, are further identified and ex-

plored. A line of authority is also discussed which holds that trade secret misappropriation and other unfair competitive acts can constitute a *per se* violation of Section 1 of the Sherman Act. Another line of cases is analyzed which considers the misuse of trade secrets as part of an attempt to monopolize a market under Section 2 of the Sherman Act.

The existing Chapters 1 through 8 and the appendices have been expanded by this revision to include current cases and laws, such as the state laws recently enacted to govern the ownership of inventions between employers and employees.

M.F.J.

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CHAPTER 1

# The Public Policies Underlying Trade Secret Law

## §1.01. The Maintenance of Commercial Morality

Imagine for a moment a commercial society that has never heard the term "fiduciary obligation," and where no one owes any duty of fair play to anyone else. In that society the protection of intellectual property would not exist. Business might not grind to a halt, but severe problems would arise. The pirating of commercially valuable ideas would be commonplace. Fear and suspicion would invade every transaction. Any idea of value could be bought or sold from even the most trusted employees. Why invest time and money in developing a new product or process, if all you have to do is hire someone else's employee to obtain the most current commercial information? Why invest great sums of money in research, when the investment can be wiped out by an employee selling his knowledge, and yours, to the highest bidder?

A moment's reflection about such an abominable business climate leads to the recognition of practical reasons for the development of the law of trade secrets. The legal protection of trade secrets stabilizes the relationship of people in commercial transactions by providing rules of fair play which govern even in the absence of an express contract. Trade secret law further increases efficiency and productivity by providing a framework which encourages the free flow of information among all parties to a commercial transaction.

A historical review of the law[1] shows that many societies

[1] *See* Schiller, *Trade Secrets and the Roman Law; The Actio Servi Corrupti,* 30 Colum. L. Rev. 837 (1930); Barton, *A Study in the Law of Trade*

were concerned with the maintenance of commercial morality and with protecting trade secrets in a variety of different situations and relationships. During the Roman empire, for example, the employee-employer problems were complicated by the fact that slaves formed the largest group of employees. It was evidently a common practice in ancient Rome to entice (or force) another's slave to divulge business secrets. Since it did little good to sue a slave, Roman civil law developed a cause of action which could be used against the third party who enticed the trade secret violation.

The cause was the *actio servi corrupti*—the action for corrupting a slave.[2] The measure of recovery was double the actual damages caused by the disclosure or use of the secret. Damages also included reimbursement of the owner for the resulting diminution in the value of a once-loyal slave.[3]

Rome continues to grant protection for industrial and commercial secrets (*segreto industriale* and *segreto commerciale*), but on quite different terms than provided by the *actio servi corrupti.*[4] As the industrial revolution replaced rural and agrarian societies with technology and increasing employee mobility, other European societies became interested in preserving commercial morality. Since the middle of the nineteenth century, France and Belgium have had articles in their penal codes punishing unauthorized disclosure of "secrets of the factory" (*secret de fabrique*).[5] Similar protection for trade secrets, as well as civil remedies for trade secret misappropriation, were provided by the Ger-

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*Secrets*, 13 U. Of Cinn. L. Rev. 507 (1939); Klien, *The Technical Trade Secret Quadrangle: A Survey*, 55 N.W.U.L. Rev. 437 (1960); and Comment, *Nature of Trade Secrets and Their Protection*, 42 Harv. L. Rev. 254 (1929).

[2] Schiller, *supra* note 1.

[3] *Id.* at 841.

[4] *See* 4 A. Wise, Trade Secrets and Know-How Throughout the World, Par. 5.01 (1974).

[5] *See Id.*, Vol. 3, Par. 3.01 (1974). (Now French Penal Code, Article 418); *Id.*, Vol. 1, Par. 107 (2) (Belgium Penal Code of 1860).

man Unfair Competition Law of 1909.[6]

The Anglo-American common law also began to develop protection for business secrets to enhance commercial morality and good-faith dealings in business. England had no statutory law which applied to secrets, but the common law began to consider protection for trade secrets in the early 1800's.[7] In 1820, an English Court of Chancery granted an injunction against use or disclosure of a trade secret because the discovery was obtained by a "breach of trust and confidence." *Yovatt v. Winyard,* 1 Jac. & W. 393, 37 Eng. Rep. 425, 426 (Ch. 1820); see also *Green v. Folgham,* 1 Sim & St. 398, 57 Eng. Rep. 159 (Ch. 1823).

The public policy of enhancing commercial morality by granting protection for trade secrets was exported to the United States from England. The introduction of trade secret law into the U.S. began in 1837, with the case of *Vickey v. Welch,* 36 Mass. 523 (1837), and was nearly completed by the 1868 decision of *Peabody v. Norfolk,* 98 Mass. 452 (1868). Since the beginning, the focus of U.S. trade secret cases has been on penalizing a breach of confidence and trust by the trade secret misappropriator. *Peabody v. Norfolk,* 98 Mass. 452 (1868). The underlying public policy was articulated by Judge Adams in the early case of *Eastman Co. v. Reichenbach,* 47 N.Y. 435, 20 N.Y.S. 110 (1892), where the court was faced with former key employees of Eastman who started a competing business with Eastman's trade secrets. Judge Adams enjoined the defendants, and reasoned:

> This is not legitimate competition, which it is always the policy of the law to foster and encourage, but it is *contra bonos mores,* and constitutes a breach of trust which a court of law, and much less a court of equity, should not tolerate.[8]

The concern for business morality has been a constant theme as the common law of trade secrets developed in the United States over the last century. This policy touchstone

[6] *Id.* Vol. 1 at Par. 4.04(2).
[7] *See* §1.02, *infra.*
[8] 20 N.Y.S. at 116.

was recently emphasized by the U.S. Supreme Court in its landmark case of *Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470 (1973). After thoroughly reviewing the public policies underlying the U.S. patent laws and the state laws governing trade secrets, the Court held that trade secret law was *not* preempted by the federal patent law. In support of trade secret law, the Court noted:

> *The maintenance of standards of commercial ethics* and the encouragement of invention are the broadly stated policies behind trade secret law. The necessity of good faith and honest fair dealing is the very life and spirit of the commercial world.[9]

A main policy goal of U.S. trade secret law is thus to foster and preserve a wholesome and fairminded commercial ethic. Encouragement of honest and good faith business dealings is even more important in modern society, where extremely valuable ideas are often embodied in compact and easily transportable form, and espionage techniques are highly sophisticated.[10]

## §1.02. The Encouragement of Research and Innovation

A second policy touchstone for trade secret law is the encouragement of research and innovation. This policy area has been very troublesome for the courts, because of the continuing conflict between trade secret law and the related laws governing patents and restraints of trade. On the one hand, the policy against restraints of trade is designed to promote free competition by allowing unfettered use of ideas in the public domain. On the other hand, the policy

[9] 416 U.S. at 481-82 (emphasis has been added throughout unless otherwise indicated).

[10] For example, one estimate states that about $4. billion worth of trade secrets are misappropriated annually in the U.S. *See* Hutter, *Trade Secret Misappropriation: A Lawyer's Practical Approach to the Case Law*, 1 W. New England L. Rev. 1, 3 (1978).