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Will the Revised Uniform Partnership Act (1994) Ever Be Uniformly Adopted?

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CONFLICTING INTERESTS IN TRADE SECRETS

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Patent lawyers are familiar with a phenomenon commonly referred to as "blocking patents," under which a patentable improvement over an existing patented invention may go unused, unless both the improver and the owner of the earlier patented invention agree to cooperate. To illustrate, suppose that I invent and patent a novel and nonobvious composition of matter that can be used to reduce or prevent the adverse physiological effects of physical exercise or environmental exposure; and that this invention comprises four elements or "limitations"—water, sugar, electrolytes, and glycerol in a concentration from about 0.5% to 5.0%—which I shall refer to as A, B, C, and D.[1] You then conceive of an improvement comprising limitations A, B, C, D, and E, where E stands for some additional element to be added to my patented composition of matter. If the addition of element E results in a new composition that is both a useful and nonobvious improvement over my invention, you can obtain a patent on the improvement, thereby obtaining the right to exclude me from making, using, or selling a composition comprising A, B, C, D, and E. (I could, of course, continue to make, use, and sell the composition comprising A, B, C, and D only). Obtaining a patent only allows one to exclude others from making, using, or selling one's patented invention, however, and does not create an affirmative right to make, use, or sell the invention oneself.[2] Thus,

* Associate Professor of Law, University of Florida College of Law. I wish to thank Margreth Barrett, Robert C. Denicola, and Christopher Slobogin for their comments and criticism; Jon Anderson & Associates Printers for assistance with graphics; and Donald Kirk, Jason Lazarus, and Jennifer Perry for their research assistance. Any errors that remain are mine.

1. The example is drawn from U.S. Patent No. 4,981,687, issued Jan. 1, 1991 (Compositions and Methods for Achieving Improved Physiological Response to Exercise). Subject to certain conditions, any person who "invents or discovers any new and useful process, machine, manufacture, composition of matter, or any new and useful improvement thereof, may obtain a patent therefor." 35 U.S.C. § 101 (1994); *see also* 35 U.S.C. § 102 (defining novelty). In addition, the Patent Act requires that the differences between the subject matter sought to be patented and the prior art be "such that the subject matter as a whole would [not] have been obvious at the time the invention was made to a person having ordinary skill in the art to which [the] subject matter pertains." 35 U.S.C. § 103(a). Once a patent is granted, it entitles the patentee to exclude others from, among other things, making, using, or selling the patented invention within the United States for a term beginning on the date on which the patent issues and ending twenty years from the date on which the patent application was filed. 35 U.S.C. §§ 154(a), 271(a).

2. *See* 35 U.S.C. § 154(a)(1) (granting the patent holder "the right to exclude others from making, using, offering for sale, or selling the invention throughout the United States").

my patent on the composition of A, B, C, and D would entitle me to exclude you from making, using, or selling your improvement thereon, because for you to do so would infringe my patent.[3] Under these circumstances, then, neither you nor I may practice the improvement without first receiving permission from the other; each of us can "block" the other from making, using, or selling the improvement, which will thereafter stand idle unless each of us agrees to license the other. This "blocking patents" phenomenon has received considerable scholarly attention concerning whether the present system, which relies upon voluntary agreement among the parties to free up the improvement for public exploitation, should be changed to an alternative system under which the parties would be required to license one another at some statutorily or judicially fixed rate.[4]

A case that I teach in my intellectual property class, *Structural Dynamics Research Corp. v. Engineering Mechanics Research Corp.*,[5] has led me to consider whether an analogous phenomenon can arise in the context of trade secret law.[6] To illustrate the "conflicting interests" phenomenon I have in mind requires first a brief explanation of some fundamental principles of this body of law. Under the Uniform Trade Secret Act (UTSA), which a majority of states (including Florida) have adopted,[7] a trade secret is defined as:

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3. *See, e.g.*, Texas Instruments Inc. v. Cypress Semiconductor Corp., 90 F.3d 1558, 1563 (Fed. Cir. 1996) ("To literally infringe, the accused device or process must contain every limitation of the asserted claim.") (citing Laitram Corp. v. Rexnord, Inc., 939 F.2d 1533, 1535 (Fed. Cir. 1991)).

4. *See, e.g.*, JOHN W. SCHLICHER, PATENT LAW: LEGAL AND ECONOMIC PRINCIPLES § 2.13[6][d] (Release #4, 1996); Ian Ayres & Eric Talley, *Solomonic Bargaining: Dividing a Legal Entitlement to Facilitate Coasean Trade*, 104 YALE L.J. 1027, 1092-94 (1995); Gianna Julian-Arnold, *International Compulsory Licensing: The Rationales and the Reality*, 33 IDEA 349, 353 & n.15 (1993); Robert Merges, *Intellectual Property Rights and Bargaining Breakdown: The Case of Blocking Patents*, 62 TENN. L. REV. 75, 77-78 (1994); A. Samuel Oddi, *TRIPs—Natural Rights and a "Polite Form of Economic Imperialism,"* 29 VAND. J. TRANSNAT'L L. 415, 466 (1996); Michael A. Sanzo, *Antitrust Law and Patent Misconduct in the Proprietary Drug Industry*, 39 VILL. L. REV. 1209, 1259-61 (1994).

5. 401 F. Supp. 1102 (E.D. Mich. 1975).

6. Technically, the phenomenon I am about to describe can arise if the information at issue is confidential information that does not qualify for protection as a trade secret—though under the modern definition of "trade secret" set forth above, most confidential information of value to business organizations probably does qualify for such protection. This phenomenon may arise regardless of whether the information is patentable.

7. FLA. STAT. ch. 688 (1995). Other sources of trade secret law upon which courts rely as persuasive authority include the restatements. *See* RESTATEMENT (THIRD) OF UNFAIR COMPETITION §§ 39-45 (1995); RESTATEMENT OF TORTS §§ 757-759 (1939). In addition, Congress recently enacted the Economic Espionage Act of 1996, which makes trade secret misappropriation a federal crime under certain circumstances. *See* Pub. L. No. 104-294, 110 Stat.

> information, including a formula, pattern, compilation, program, device, method, technique, or process, that . . . derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use, and . . . is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.[8]

Trade secret protection therefore extends not only to information that is sufficiently novel, useful, and nonobvious that it could qualify for patent protection, but more generally to any information that provides one with a competitive advantage as long as it remains secret.[9] The owner of a trade secret may exclude another from, among other things, acquiring the secret by "improper means" such as theft or espionage;[10] or from using or disclosing the secret if the other knew (or had reason to know) at the time of his disclosure or use that the secret was derived from a person who (1) had used improper means to acquire it, or (2) had acquired it under circumstances giving rise to a duty to maintain its secrecy, or (3) owed a duty of secrecy to the owner.[11] Unlike a patentee, however, the owner of a trade secret cannot exclude one who independently invents or discovers the subject matter of the secret from making use of this information; nor can she prevent one from attempting to discover, and subsequently exploiting, the secret through reverse engineering.[12]

When one who is employed by another discovers or invents a trade secret, ownership of the secret may vest either in the employee or employer, depending on the circumstances. One commentator, after surveying the relevant case law, has suggested that, for purposes of both trade secret and patent law, courts in effect classify employee-inventors as falling into one of three categories which he refers to as "specific inventive," "general inventive," and "non-inventive."[13] A specific inventive employee is one "who is either (1) hired to invent a specific

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3488, 3489 (1996).

8. Unif. Trade Secrets Act § 1(4) (1985).

9. *See, e.g.*, RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 39. By contrast, in order to obtain a patent, an inventor must publicly disclose how to practice her invention, as well as the "best mode" contemplated by her of carrying out the invention as of the time of application. 35 U.S.C. § 112 (1994).

10. Unif. Trade Secrets Act § 1(2)(i) (1985).

11. Unif. Trade Secrets Act § 1(2)(ii).

12. *See, e.g.*, RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 43.

13. Robert L. Gullette, *State Legislation Governing Ownership Rights in Inventions Under Employee Invention Agreements*, 62 J. PAT. OFF. SOC'Y 732, 732-33 (1980).

invention or (2) is assigned the task of making a specific invention or improvement to existing technology."[14] At common law, a specific inventive employee is deemed implicitly to assign ownership of her work to her employer.[15] Ownership of an invention created by a non-inventive employee (one who is not expected to engage in any inventive activity), by contrast, vests in the employee.[16] The third category of general inventive employees consists of those who are hired to invent, such as research scientists and design engineers, but from whom "no specific invention or end result is contemplated."[17] Ownership of the work of a general inventive employee initially vests in the employee, but may be expressly or implicitly assigned to the employer.[18] Among the factors a court will consider in determining whether or not a general inventive employee has implicitly assigned her invention to her employer are:

> the nature and scope of the employment relationship, the amount of money or other resources the employer devoted to the inventive activity, how closely the employee's invention is related to the employer's business, whether the employee has assigned inventions to the employer in the past, and any other evidence of an implicit understanding between the parties about ownership of inventions.[19]

In the case of non-inventive employees and general inventive employees who are deemed to own their own inventions, however, the employer may be deemed to have a "shop right"—"an irrevocable, nonexclusive, non-assignable right to use the trade secret, without an obligation to pay royalties"[20]—if the secret "is related to the employer's business and the employee, in developing it, used her employer's time, facilities, personnel, materials, money or other resources."[21]

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14. *Id.* at 733.

15. MARGRETH BARRETT, INTELLECTUAL PROPERTY LAW: CASES AND MATERIALS 82 (1995); Gullette, *supra* note 13, at 734.

16. Gullette, *supra* note 13, at 733-34.

17. *Id.* at 733.

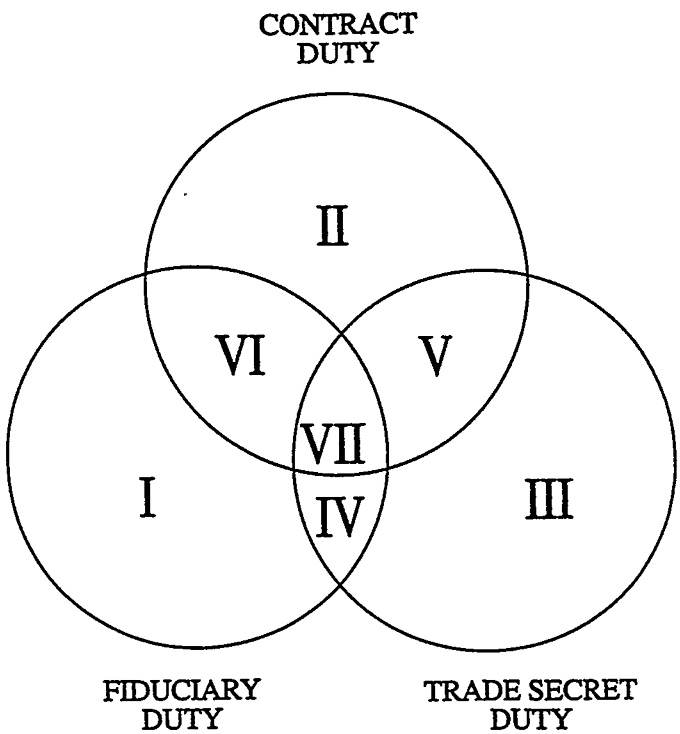
18. BARRETT, *supra* note 15, at 82; 1 ROGER M. MILGRIM, MILGRIM ON TRADE SECRETS § 5.02[4][c], at 5-74 to 75 (1996). Some states, however, have enacted statutes modifying, in various respects, the rules relating to assignment. *See generally* Gullette, *supra* note 13, at 740-60 (discussing state legislation from Minnesota, Washington, and California).

19. BARRETT, *supra* note 15, at 82; *see also* 1 MILGRIM, *supra* note 18, § 5.02[4][c], at 5-74 to 76 (discussing in what situation an employer would be entitled to a "shop right"—an irrevocable nonexclusive license).

20. BARRETT, *supra* note 15, at 83.

21. *Id.*; *see also* 1 MILGRIM, *supra* note 18, § 5.02[4][c], at 5-75 to 76 (stating that even

Because the law of trade secrets penalizes only the disclosure or use of the trade secret *of another*,[22] an employee who owns a trade secret created during her employment does not violate any duty created by trade secret law if she uses or discloses this information to the detriment of the entity that employed her at the time of its creation. In theory, however, she may violate duties owed to this entity under the law of contract or fiduciary obligations, and it is this possibility of conflicting interests between employer and employee that gives rise to the phenomenon under consideration. To illustrate, let us assume that *D* discloses or uses information which qualifies as a trade secret, and that *P* claims that this disclosure or use constitutes a breach of a duty of secrecy which *D* owes to *P*. Depending on the facts, it is possible that *D* owes *P* a fiduciary duty of secrecy, a contractual duty of secrecy, a trade secret duty of secrecy, or any combination thereof (or none of them). The diagram below illustrates the various possible combinations of duties, with the top circle representing the contractual duty of secrecy: the left bottom circle representing the fiduciary duty of secrecy; and the right bottom circle representing the trade secret duty of secrecy.



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if the "matter involved was not within [the] scope of employment," the employer may still be entitled to a shop right).

22. Unif. Trade Secrets Act § 1(2)(ii) (1985).

Regions I, II, and III illustrate how *D*'s disclosure or use may violate only a single duty of secrecy. Thus, in Region I, *D*'s disclosure or use violates a fiduciary duty of secrecy, but not a contractual or trade secret duty of secrecy. An example would be where *D* is a non-inventive current employee of *P*, who has not executed an enforceable nondisclosure agreement with her employer. Because a current employee owes her employer a fiduciary duty not to disclose or use information during the term of her employment in competition with the employer, *D*'s disclosure or use would constitute a breach of fiduciary duty even though *D* owns the secret.[23] Region II represents the situation in which *D*'s disclosure or use violates a contractual duty of secrecy only. For example, this would be the case where *D* is a non-inventive former employee of *P* who has executed an enforceable nondisclosure agreement (but who has not assigned the secret to *P*).[24] The fact that the employment relationship has terminated frees *D* of any fiduciary obligation to abstain from disclosing or using her own secret, but *D* would remain bound by an enforceable contractual obligation. Region III represents the situation in which *D*'s disclosure or use violates only a trade secret duty of secrecy. An example would be the famous case of *E.I. duPont de Nemours & Co. v. Christopher*,[25] in which the defendants obtained trade secretive information concerning a plant duPont

23. RESTATEMENT (SECOND) OF AGENCY §§ 387, 393, 395 (1958); *see also* RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 42 cmts. b, c, & e (1995) (discussing the employer/employee relationship).

24. Because of their potentially anticompetitive nature, nondisclosure agreements and covenants not to compete are not uniformly enforceable.

> [S]ince such agreements can reduce or eliminate potential competition, they are subject to the traditional rules governing contracts in restraint of trade and are accordingly enforceable only when ancillary to a valid transaction and otherwise reasonable. See Restatement, Second, Contracts §§ 186-188. As a general matter, a restraint is unreasonable if it is greater than necessary to protect the legitimate interests of the promisee or if the promisee's interest in protection is outweighed by the likely harm to the promisor or to the public. *Id.* § 188, Comment *a.*
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> . . . A promise by an employee not to compete with the employer after the termination of the employment or by a seller of a business not to compete with the buyer after the sale may be justified as a reasonable attempt to protect confidential information, provided that the duration and geographic scope of the covenant are appropriately related to the promisee's legitimate interests. . . .

RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 41 cmt. d; *see also* 1 MILGRIM, *supra* note 18, § 4.02[1][d], [2][a].

25. 431 F.2d 1012 (5th Cir. 1970).

was building in Texas, by taking aerial photographs of the site.[26] Because the use of aerial surveillance was deemed to be an improper means of acquiring the information, the defendants' subsequent disclosure or use of that information would violate a duty owed to duPont under the law of trade secrets,[27] but (absent a contractual or fiduciary relationship between plaintiff and defendants) neither a contractual nor a fiduciary duty.

Regions IV through VII illustrate how *D*'s disclosure or use may violate multiple duties of secrecy owed to *P*. In Region IV, *D* violates fiduciary and trade secret duties of secrecy. For example, if *D* is a current or former specific inventive employee, her disclosure or use of her employer's secret would violate the UTSA (because the secret belongs to *P*) and also the fiduciary duty owed by former employees to refrain from disclosing information belonging to their former employers, in competition with those employers.[28] It would not, however, violate a contractual duty in the absence of an enforceable nondisclosure agreement. In Region V, *D* violates a contractual and trade secret duty of secrecy but not a fiduciary duty. A common setting in which this situation would arise would be where *D* is an independent entity that licenses *P*'s trade secret. *D*'s disclosure or use of the secret beyond what is permitted by the license would violate not only the terms of the license but also the trade secret duty by disclosure or use of information acquired under circumstances giving rise to a duty of secrecy.[29] It would not, however, violate any fiduciary obligation, inasmuch as a licensee usually is not considered to be a fiduciary of the licensor. An example of a situation illustrating Region VI, where *D* violates a fiduciary and contractual duty of secrecy but not a trade secret duty of secrecy, would be where *D*, a non-inventive employee who has executed an enforceable nondisclosure agreement, while employed by *P* discloses or uses a trade secret, which she developed during her employment and which belongs to her, in competition with P. Finally, in Region VII, *D* violates all three duties. This situation would occur where *P* owns the secret and *D* owes *P* both a fiduciary and contractual duty of secrecy—as, for example, when *D* is a current or former specific inventive employee and has signed an enforceable nondisclosure agreement.

In theory, the conflicting interests phenomenon can arise whenever the employee owns the secret but is obligated under the law of contracts

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26. *Id.* at 1013.

27. *Id.* at 1015-16; *see* Unif. Trade Secrets Act § 1(2)(ii)(A) (1985).

28. RESTATEMENT (SECOND) OF AGENCY § 396 (1958); RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 42 & cmts. b, c, & e (1995).

29. Unif. Trade Secrets Act § 1(2)(ii)(B)(II).

or fiduciary obligations not to use or disclose it in competition with her present or former employer—that is, in certain cases inhabiting Regions I, II or VI. This phenomenon would not be precisely analogous to the blocking patent phenomenon because, as noted above, the employer in the situations under discussion herein may have a shop right to use the secret in its own business. Courts seem to agree, however, that a shop right does not entitle an employer to sell or license the secret to others, even though selling or licensing it, as opposed to merely using it in the employer's own business, may be the information's most highly valued use.[30] As in the blocking patent situation, then, the optimal use of the information depends upon the two parties' being able to agree to some form of licensing, or else upon judicial or legislative action to force an agreement when one otherwise might not be forthcoming.

The crucial issue, of course, is whether there are any real-world cases inhabiting Regions I, II, or VI, in which the employee owns the subject information but is precluded from using or disclosing it under the law of contracts or fiduciary obligations. I suspect there are few such cases falling within Regions I and VI, because an employee who uses information (even if it is his own) in competition with or to the detriment of his current employer is probably unlikely to remain in the latter's employ for very long. Once the Region I or VI employee/trade secret owner ceases his employment, he is free to use the information as he pleases unless he is a Region VI employee subject to an enforceable post-termination nondisclosure agreement (in which event his case moves from Region VI to Region II upon cessation of employment). The more important question, then, is whether there are any relevant real-world cases inhabiting Region II.

30. *See, e.g.*, Melin v. United States, 478 F.2d 1210, 1215 (Ct. Cl. 1973) (stating that shop rights are not assignable); Tripp v. United States, 406 F.2d 1066, 1070 (Ct. Cl. 1969) (holding that owner of shop right in invention is not entitled to license others to use invention) (citing Ushakoff v. United States, 327 F.2d 669, 673 (Ct. Cl. 1964)). These results seem to square with the historical development of the shop right doctrine, as stated by the United States Supreme Court:

> Since the servant uses his master's time, facilities and materials to attain a concrete result, the latter is in equity entitled to use that which embodies his own property and to duplicate it as often as he may find occasion to employ similar appliances in his business. But the employer in such a case has no equity to demand a conveyance of the invention. . . . This remains the property of him who conceived it, together with the right conferred by the patent, to exclude all others than the employer from the accruing benefits.

United States v. Dubilier Condenser Corp., 289 U.S. 178, 188-89 (1933).

On reflection, I would guess that there are few such Region II cases either, because both employers and the courts can take steps to avoid having cases of this nature arise. Employers generally can avoid Region II cases by requiring their employees to agree to the advance assignment of any employee innovations created during the term of employment;[31] and even if the parties fail to agree to such an express assignment, a court would have several options for avoiding a conflicting interests problem. One such option would be to construe the nondisclosure agreement as including an *implicit* assignment of any innovations to the employer. *Structural Dynamics* arguably presents an example of a court employing this option.[32] In the early 1970s, Surana and Kothawala, computer engineers employed by Structural Dynamics Research Corporation (SDRC), worked on developing a computer program for use in isoparametric modeling.[33] These two individuals, along with a third engineer-employee, Hildebrand, each executed a nondisclosure agreement forbidding him from divulging or using, during or after his employment with SDRC, "any privileged or confidential information, trade secret or other proprietary information . . . imparted or divulged to, gained or developed by . . . Employee during his employment with the Company."[34] The three engineers subsequently terminated their employment and established a competing business, Engineering Mechanics Research Corporation (EMRC), where they completed and began marketing a version of the program.[35] SDRC in the meantime completed its own version of the program, and then filed suit against the engineers and EMRC for misappropriation of trade secrets and breach of contract.[36] The court appears to have concluded that Surana, who did most of the work on the project, was a general inventive employee—that

31. *See* RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 42 cmt. g (1995) ("[A]bsent an applicable statutory prohibition, agreements relating to the ownership of inventions and discoveries made by employees during the term of the employment are generally enforceable according to their terms."); *see also* BARRETT, *supra* note 15, at 83 (discussing enforceability of advance assignments); 1 MILGRIM, *supra* note 18, § 4.02[1][a], at 4-12 to 14 (discussing how to create an advance assignment).

32. Structural Dynamics Research Corp. v. Engineering Mechanics Research Corp., 401 F. Supp. 1102 (E.D. Mich. 1975).

33. *Id.* at 1107.

34. *Id.* at 1112. Kothawala also executed an employment contract which forbade him, during the period of his employment or thereafter, from disclosing to anyone "any confidential information or trade secrets concerning the business affairs of SDRC . . . imparted or divulged to, gained or developed by or otherwise discovered by Kothawala during his employment with SDRC." *Id.* at 1113. Each defendant also agreed not to compete with SDRC for a discrete period of time following termination. *Id.* at 1112-13.

35. *Id.* at 1106-08.

36. *Id.* at 1105, 1109.

is, one who (absent an assignment of rights) owed SDRC neither a fiduciary nor a trade secret duty of nondisclosure or nonuse.[37] Construing the defendants' nondisclosure agreements as obligating them to refrain from disclosing or using the subject information in competition with SDRC, the court found the defendants in breach of these agreements.[38] Although this outcome on its face would appear to give rise to the conflicting interests phenomenon, by assigning an ownership interest to Surana while at the same time precluding him from using the secret, other portions of the opinion suggest that the court understood the agreement as containing an implicit assignment of the secret to SDRC.[39] If this is the correct interpretation of the opinion, then, the court avoided the conflicting interests phenomenon by ultimately assigning both property and contract rights to one party, the employer.

One problem with the *Structural Dynamics* approach, however, is that reading an implicit assignment clause into the agreements at issue in that case seems somewhat arbitrary. Granted, one might surmise that the parties did not intend, by virtue of the nondisclosure agreements, to create a conflicting interests situation. Very likely they intended either that all innovations created during the term of employment would belong to SDRC, as the court arguably ultimately concluded—or that the agreement obligated the defendants only to refrain from using or disclosing secrets belonging to SDRC, but not secrets in which ownership originally vested in the defendants. Under this latter interpretation, the conflicting interests problem would have been avoided by the assignment of an ownership interest to Surana coupled with the elimination of any contractual obligation to refrain from exploiting that interest. The ambiguity in the agreement, however, makes it difficult to

37. *Id.* at 1112; *but see id.* at 1116 (stating that the information "was acquired in the course of [Surana and Kothawala's] employment and *a fulfillment* [sic] *of their specific assigned responsibilities*") (emphasis added); *see also supra* text accompanying notes 13-21 (discussing the types of inventive employees).

38. *Structural Dynamics*, 401 F. Supp. at 1118.

39. The opinion lacks clarity on this issue. In various portions of the opinion, the court appears to refer to the information as belonging to SDRC. *See id.* at 1117 (referring to the program as "confidential and proprietary to SDRC"); *id.* at 1118 (referring to "plaintiff's confidential information"); *id.* at 1119 (referring to "SDRC's confidential information"); *id.* at 1120 (stating that "SDRC also seeks a license fee . . . for use of its program," and that defendants are liable for unauthorized use of "SDRC's confidential information"). Moreover, the last portion of the opinion seems premised on the assumption that SDRC was free to continue using the information as it wished, well beyond the limited scope of a traditional shop right. *See id.* at 1117-20. On the other hand, if the court had meant to find an implied assignment it should have found Surana liable for breach of fiduciary duty and (assuming the subject information qualified as a trade secret, an issue on which the court ultimately declined to pass judgment) misappropriation of trade secrets, as well as for breach of contract—something it did not do.

determine which of these two interpretations better squares with the parties' intent at the time of contracting. To avoid Region II in other similar cases therefore might require the court arbitrarily to choose one plausible interpretation over the other, an outcome that may be difficult to square with the rule of law. Perhaps, though, a rule interpreting such agreements in favor of the defendant employee—contrary to the outcome of *Structural Dynamics*—could be justified as more consistent with general notions of fairness or (because the employer is usually in a better position to avoid or insure against the risk of ambiguity) economic efficiency.

Yet another strategy would be to construe a nondisclosure agreement of the type at issue in *Structural Dynamics* to mean what it appears to say—that the defendant cannot use the subject information following termination, regardless of who owns it—and then to decide whether the agreement is enforceable in cases where the defendant happens to own the information. Professor Denicola has argued that such an agreement should be unenforceable under section 41 comment d of the *Restatement (Third) of Unfair Competition*.[40] This section states that nondisclosure agreements encompassing information "in which the promisee has no protectable interest, such as a former employee's promise not to use information that is part of the employee's general skill and training may be unenforceable as an unreasonable restraint of trade"[41] because "[t]he employer has no legitimate justification for restricting a former employee's use of information that the employer does not own."[42] Like the strategy of interpreting the agreement in favor of the employee, this solution avoids the conflicting interests problem by assigning ownership to the employee while eliminating the contractual obligation of secrecy. Given the courts' general reluctance to enforce post-termination restrictions on account of their potential anticompetitive nature,[43] this solution may hold out the most promise as a principled means of avoiding the conflicting interests problem.

I am not so sure that this solution would apply in every case, however. The Restatement does not precisely define the terms

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40. Letter from Robert C. Denicola, Professor of Law, University of Nebraska College of Law, to Thomas F. Cotter (Jan. 29, 1997) (on file with author) (citing RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 41 cmt. d (1995)).

41. RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 41 cmt. d (citations omitted); *cf.* FLA. STAT. § 542.335(b) (Supp. 1996) (stating that a person seeking enforcement of a restrictive covenant must prove the "existence of one or more legitimate business interests justifying the restrictive covenant").

42. Denicola, *supra* note 40.

43. *See supra* note 24.

"protectable interest" and "general skill and training."[44] The resulting ambiguity leaves open the possibility that, under the right circumstances, a court might enforce an agreement forbidding the former employee from using or disclosing his own secret. An illustration of the ambiguity surrounding these terms is provided by some of the case law discussing the enforceability of contract provisions, known as holdover clauses, that require the employee to assign to the employer inventions created within a period of time *after* termination of employment. Like other post-termination restrictions, these provisions are enforceable only if, among other things, the employer is deemed to have a protectable interest in the subject information, and the information is not considered to be merely part of the employee's general skill and training.[45] At least two courts have nevertheless concluded that, in some instances, the employer may have a protectable interest in an employee's post-termination invention, even though the invention is attributable only to the employee's earlier exposure to the employer's non-trade-secretive information.[46] But if an

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44. *See* RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 42 cmt. d (discussing "general skill and training"); *id.* cmt. e (appearing to draw a distinction between a trade secret owned by an employee and that employee's general skill and knowledge).

45. *See, e.g.*, Ingersoll-Rand Co. v. Ciavatta, 542 A.2d 879, 887-88 (N.J. 1988) (stating that a holdover clause is unenforceable if it: "(1) extends beyond any apparent protection that the employer reasonably requires; (2) prevents the inventor from seeking other employment; or (3) adversely impacts on the public").

46. *See id.* at 893-94:

> Ingersoll-Rand . . . argues that it is inequitable to limit an employer's "protectable interest" solely to trade secrets and other confidential information. Today, large corporations maintain at great expense modern research and development programs that involve synergistic processes. Such "think tanks" require the free and open exchange of new ideas among the members of a research staff using the employer's body of accumulated information and experiences. This creative process receives its impetus and inspiration from the assimilation of an employer's advanced knowledge and a spontaneous interaction among colleagues, co-employees, and superiors. Ingersoll-Rand argues that it maintains this creative atmosphere in its research and development effort at great expense and that it should be allowed to protect itself against a former employee who invents a unique, competing concept attributable to such brainstorming. . . .
>
> We agree with Ingersoll-Rand that the protection afforded by holdover agreements such as the one executed by the parties in this lawsuit may under certain circumstances exceed the limitation of trade secrets and confidential information.

See also Campbell Soup Co. v. Conagra, Inc., 801 F. Supp. 1298, 1305 (D.N.J. 1991) (recognizing that employers may have legitimate interests in protecting "information that is not 'a trade secret or proprietary information, but highly specialized, current information not generally known in the industry, created and stimulated by the research environment furnished employer can have a protectable interest in information that (1) is created by the employee after termination, and (2) would, in the absence of an enforceable assignment, clearly belong to the employee, it is difficult to understand why the employer in a case like *Structural Dynamics* cannot have a protectable interest in information that (1) is created prior to termination, and (2) would, in the absence of a nondisclosure agreement, clearly be subject to disclosure and use by the employee. It seems odd, in other words, to countenance enforcing promises to assign inventions to employers, while at the same time categorically refusing to enforce promises only to refrain from using or disclosing those inventions for a limited period of time. I should think, then, that it might be possible for a court to enforce some post-termination restrictions on the employee's use or disclosure of his own secret.[47] Enforcing such restrictions, of course, would finally bring us squarely within the boundaries of Region II.

A court choosing this final option of enforcing the restriction on the employee's use or disclosure of his own secret would then have two further choices to make: either to enjoin both parties from using the secret without the other's consent (as in the blocking patent situation), or to impose some form of cross-licensing arrangement. Perhaps the *Structural Dynamics* case can be read as authority for this latter resolution as well. In the last portion of the opinion, the court declined to enjoin the defendants from further use of the program.[48] Instead, the court required the defendants to pay a 15% royalty on all of EMRC's sales for a three-year period, reasoning that it would have taken a competitor three years to duplicate the program by independent research.[49] The result was that both SDRC and EMRC were able to continue exploiting the secret, without having to negotiate over terms, upon compliance with the court's order. Perhaps an outcome of this

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by the employer, to which the employee has been "exposed" and "enriched" solely due to his employment' ") (quoting *Ingersoll-Rand*, 542 A.2d at 894), *vacated on other grounds*, 977 F.2d 86 (3d Cir. 1992).

47. I have no idea how frequently courts might be willing to enforce such restrictions, however. I note that in *Ingersoll-Rand*, the court, after discussing the rules relating to holdover clauses, found in favor of the defendant employee. *See Ingersoll-Rand*, 542 A.2d at 892-96.

48. *Structural Dynamics*, 401 F. Supp. at 1120.

49. *Id.* at 1119-20. By the time the opinion was handed down, the three-year period, which the court concluded should begin running from the date of EMRC's contacts with its customer American Motors Corporation in March 1973, had only six more months to go. *Id.* at 1120. Perhaps the brevity of the remaining time period was a factor in the court's decision not to enjoin the defendants, but rather to condition their further use upon the payment of a royalty. *Cf. infra* note 57 (discussing the "exceptional circumstances" under which a court may permit the misappropriator of a trade secret to continue using the secret upon payment of a reasonable royalty).

nature can be viewed as more in keeping with the rough equities of a difficult case.

Whether a court faced with a genuine Region II case should feel free to fashion some sort of equitable remedy as in *Structural Dynamics*, or should instead leave it up to the parties to draw up their own terms for exploitation of the secret, is a difficult issue. In the analogous case of blocking patents, Congress and the judiciary have opted for the latter option over a compulsory licensing scheme. Professor Merges has defended this choice of what is referred to in the law and economics literature as a "property rule" on the following grounds:

> [A] property rule makes sense for patents because: (1) there are only two parties to the transaction, and they can easily identify each other; (2) the costs of a transaction between the parties are otherwise low; and (3) a court setting the terms of the exchange would have a difficult time doing so quickly and cheaply, given the specialized nature of the assets and the varied and complex business environments in which the assets are deployed. Hence the parties are left to make their own deal.[50]

Merges also argues that compulsory licensing systems tend to discourage the formation of voluntary institutions, such as patent pools[51] (or, in the copyright field, organizations such as ASCAP and BMI) which can efficiently reduce the transaction costs that otherwise threaten to inhibit voluntary bargaining.[52] Thus, if Merges and other advocates of the present patent system are correct in asserting that compulsory licenses are economically inefficient, courts in future Region II cases may be well-advised to leave the parties to their own devices.[53] Indeed, one

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50. Merges, *supra* note 4, at 78.

51. Robert P. Merges, *Of Property Rules, Coase, and Intellectual Property*, 94 COLUM. L. REV. 2655, 2662 n.27 (1994) ("Patent pools are industry-wide agreements, often accompanied by administrative structures, to centralize all firms' patents for automatic out-licensing or to cross-license each others' patents.").

52. *Id.* at 2662-63, 2667-73.

53. I should emphasize that the reasons suggested above for rejecting a compulsory licensing system as a response to the blocking patent phenomenon do not necessarily imply that construing a nondisclosure agreement so as to give rise to a conflicting interests phenomenon, and then relying upon the parties to that agreement to work out a solution to the ensuing problem, is the optimal response to cases such as *Structural Dynamics*. As discussed above, it may be optimal in all or most such cases to construe the agreement so as to avoid preventing the party whom the court determines to be the owner of the subject information from using and disclosing it, or else to find the contract unenforceable. *See supra* notes 31-43 and accompanying text. The argument above merely suggests one possible path for the court to take once it decides, rightly or wrongly, that the case falls within Region II.

might argue that, if we can bear the risk of doing without compulsory licensing in patent law, we can certainly do without it in trade secret law, assuming that the value of the typical patented invention—and hence the social value that is lost if the invention is not exploited—is greater than the value of the typical trade secret.[54]

Other scholars disagree with the current rules relating to blocking patents, however, arguing that a variety of obstacles may inhibit the original patentee and the improver from reaching agreement, such that compulsory licenses are a necessary stick with which to force an agreement that benefits the public.[55] Applying game theoretic principles, Professors Ayres and Talley also have suggested that, in the blocking patent scenario, the parties may be more likely to reach efficient private bargains in the shadow of a compulsory licensing rule because the existence of compulsory licensing as a fallback encourages them to be more forthcoming in disclosing information concerning the value they place upon their innovations.[56] Moreover, the argument that compulsory licenses in patent law would discourage the formation of voluntary institutions that can facilitate transactions more efficiently than under a system of nonvoluntary rules may not seem so forceful in the context of the conflicting interests problem described herein. The development of voluntary institutions to deal with this problem (other than the routine use of advance assignment agreements) may be unlikely if, among other things, the problem arises much less frequently than the blocking patent phenomenon. Finally, it may not be beyond the institutional competence of the courts to create compulsory trade secret licenses, particularly if the typical trade secret is less complicated than the typical patent. The drafters of both the Uniform Trade Secrets Act and the *Restatement (Third) of Unfair Competition* clearly expected the courts to be capable of determining the amount of a reasonable royalty when necessary.[57]

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54. *But see* David D. Friedman et al., *Some Economics of Trade Secret Law*, 5 J. ECON. PERSPECTIVES 61, 63 (1991) (arguing that trade secret law does not necessarily protect only "a class of lesser inventions").

55. *See, e.g.*, Julian-Arnold, *supra* note 4, at 365-67; Oddi, *supra* note 4, at 466; Sanzo, *supra* note 4, at 1259-61. Merges agrees that the parties *may* fail to reach agreement, and he recognizes that such failures can cause substantial social losses when the improvement at issue constitutes a radical advance over existing technology. Merges, *supra* note 4, at 91. Merges argues, however, that an expanded use of the reverse doctrine of equivalents—a rarely-invoked patent doctrine that permits the trier of fact to absolve an ostensible infringer from liability when the accused device performs a substantially different function from the original device—would be preferable to the adoption of compulsory licenses. *See id.* at 91-99.

56. Ayres & Talley, *supra* note 4, at 1092-94.

57. *See* Unif. Trade Secrets Act § 2(b) (1985) ("In exceptional circumstances, an injunction may condition future use upon payment of a reasonable royalty. . . . Exceptional

As noted above, it may be the case that there simply are not enough instances of Region II cases to cause us to worry about how to handle the few that arise. Employers can avoid Region II cases by expressly requiring advance assignments,[58] and when this option fails, courts still can avoid these cases by means of several strategies.[59] Analysis of the conflicting interests problem nevertheless may be helpful in understanding the ways in which various rights and duties can affect the optimal use and disclosure of trade secrets.

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circumstances include, but are not limited to, a material and prejudicial change of position prior to acquiring knowledge or reason to know of misappropriation that renders a prohibitive injunction inequitable."); *see also* RESTATEMENT (THIRD) OF UNFAIR COMPETITION §§ 44 cmt. c, 45 cmts. b & g (1995) (similar). But then so did the drafters of the Patent Act. *See* 35 U.S.C. § 284 (1994) (stating that the court shall award the prevailing patent claimant "damages adequate to compensate for the infringement, but in no event less than a reasonable royalty for the use made of the invention by the infringer, together with interest and costs as fixed by the court," and permitting the court to "receive expert testimony as an aid to the determination . . . of what royalty would be reasonable under the circumstances").

58. *See supra* text accompanying note 31.

59. *See supra* text accompanying notes 32-43.