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Trade Secret Piracy

Martin A. Levitin*

A RASH OF RECENT CASES of alleged piracy of trade secrets has made headlines in trade publications, newspapers and magazines. A sampling of recently decided and still pending cases include the "Space Suit Case" in which the B. F. Goodrich Company enjoined a former employee from divulging space suit fabrication techniques and other trade secrets to a competitor;¹ the Delaware case between two of the largest American chemical companies to determine the merits of a suit to prevent the revealing of trade secrets in a pigment manufacturing process;² the multimillion dollar suits of large American drug manufacturers against Italian drug manufacturers resulting from theft of antibiotic drug manufacturing processes;³ and the "pressurized shaving soap case" in which damages totaling nearly \$10 million were awarded for misappropriation of trade secrets and patent infringement.⁴

What has provoked this apparently startling increase in activity in the trade secret field, which has been a subject of litigation for 500 years or more?⁵ Formulas several generations old

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¹ B. F. Goodrich Co. v. Wohlgemuth, 117 Ohio App. 493, 192 N. E. 2d 99 (1963); 137 United States Patents Quarterly (U.S.P.Q.) 804 (1963) reversing 137 U.S.P.Q. 389 (Ohio Com. Pls. 1963). Issues and facts in this case are dramatically presented in Brooks, *Annals of Business*, New Yorker, January 11, 1964, p. 37.

² E. I. du Pont de Nemours and Company v. American Potash and Chemical Corporation, 200 A. 2d 428 (Del. 1964); Bowen, *Who Owns What's in Your Head?*, *Fortune*, July 1964, p. 175; *Dismissal Refused in Trade Secrets Case*, *Chemical and Engineering News*, May 11, 1964, p. 23; *Legal Hurdle for Job Hoppers*, *Business Week*, June 1, 1963, p. 95.

³ *Two Convicted in Merck Trade Secret Case*, *Chemical and Engineering News*, July 6, 1964, p. 28; *Kobler, Who Stole the Formula?*, *Saturday Evening Post*, June 29, 1963, p. 82; *Piracy—A Rising Worry for U. S. Business*, *U. S. News*, September 3, 1962, p. 83; *Daniel, Spies Invade Big Business*, *Reader's Digest*, January, 1962, p. 93.

⁴ *Carter Products Inc. v. Colgate-Palmolive Co.*, 214 F. Supp. 383 (D. C. Md. 1963); *Smith*, *Business Espionage*, *Fortune*, May, 1956, p. 118.

⁵ *Note, Trade Secrets, Customer Contracts and the Employer-Employee Relationship*, 37 *Ind. L. J.* 218 (1962); *Prager, History, Background and Foundation of American Patent Law*, 5 *Am. J. Legal Hist.* 309 (1961); *Barton, A Study in the Law of Trade Secrets*, 13 *U. Cin. L. Rev.* 507 (1939).

for products such as Coca Cola, Chanel No. 5, Angostura Bitters and Lea & Perrin's Worcestershire Sauce have for the most part experienced little difficulty in protection of their secrets.⁶ But these are the exception. The burgeoning American technology since World War II has grown as the result of the competitive pressures to develop technical innovations by research and development expenditure in nearly every kind of manufacturing business.

Research and development expenditure by government and private industry has skyrocketed from \$5.1 billion in 1952 to \$18.5 billion in 1962, with spending projections calling for \$25 billion in the year 1970.⁷ The stakes of the game having gone up, many professional players from all over the world have been attracted to it.

Attitudes toward trade secret pilfering vary to great extremes; as for example, in Japan there is no law protecting against stealing of trade secrets and some premium has even been put upon doing the job well.⁸ This may explain at least in part why nearly four times as many patent applications are filed in Japan as are filed in the U. S. where the current rate of filing has declined to about 50,000 applications per year. International markets for stolen industrial secrets have developed in Japan and Switzerland and the great productivity of American research and development has been a fertile field for marketable data.

Industrial espionage has thus become a subject of grave concern to American business. This is evidenced by the attendance of nearly 2500 people at the 1962 convention of the American Society for Industrial Security.⁹ On the international scene, the International Chamber of Commerce is investigating adoption of uniform international laws to halt the stealing of trade secrets. These proposed laws would make illegal the disclosure, transmission or use of the trade secrets of another company. The game of watching the competitor's progress from a distance has taken on some new dimensions.¹⁰ The attitude expressed by

⁶ They've Got A Secret, *Time*, February 22, 1963, p. 87.

⁷ Industrial Spying Goes Big League, *Business Week*, October 6, 1962, p. 65.

⁸ School for Spies, *Time*, December 14, 1962, p. 82.

⁹ Cook, *The Corrupt Society—Part VI*, 196 *Nation* 474, 475 (1963).

¹⁰ Brenton, *They Spy for Industry*, *Popular Mechanics*, May, 1962, p. 102; Jones, *How the Auto Makers Spy on Each Other*, *Popular Science*, February, 1958, p. 133; Gehman, *Executive Spies*, *Cosmopolitan*, February, 1958, p. 70.

many that they would not hire a man who offered competitive data for sale, since he might leave in a few months and go elsewhere to sell, is undergoing some careful scrutiny. A study made by a student group at the Harvard Business School reported an astonishingly large use of competitive intelligence information by business men in their decision-making processes.¹¹

A second contributing factor to the rise of litigation over trade secrets is an apparent decline in the usefulness and importance of patents in the protection of the products of research and development and a corresponding increase in the use of trade secrets as an alternative to patents. The procedural difficulties and the long delay and expense of obtaining patents outweigh in many instances the dangers incurred by relying on trade secrets for the protection of the competitively advantageous position.¹²

A third factor with possible impact on the situation is the shortage of qualified technical personnel available for research programs. This shortage, especially marked in connection with skills needed in government-sponsored weapons programs, has led to raiding of employee talent as contract awards shift from company to company.¹³ With this personnel movement comes movement of ideas which might be considered by former employers to be protectable trade secrets.

Law of Trade Secrets¹⁴

Trade secrets may consist of formulas, patterns, devices or compilations of information which are used in a business and which enable it to obtain advantages over competitors who do not know or use the secrets. Trade secrets need not be patent-

¹¹ Alden, *Business Intelligence*, CI Associates, Watertown, Mass., 1959; *Spying for Profit*, Time, July 27, 1959, p. 59.

¹² Herald, *Trade Secrets as an Alternative to Patents*, 9 Am. Law S. Rev. 1107 (1941); and see also Scherer, *Patents and The Corporation* (2nd ed. 1959).

¹³ Coleman and Sole, *The Effect of Shifting Employment on Trade Secrets*, 14 *Business Lawyer* 319 (1959).

¹⁴ See generally, Turner, *Trade Secrets* (1962); Ellis, *Trade Secrets* (1953); Nims, *The Law of Unfair Competition and Trade Marks*, Chapter 10 (1929); Callmann, *Unfair Competition and Trademarks* (2nd ed. 1950); Fox, *The Law of Master and Servant in Relation To Industrial and Intellectual Property* (1950); 1 Oleck, *Modern Corporation Law, Protection of Ideas*, Sec. 32 (1958); 5 Williston, *Contracts* Sec. 1628 et seq. (Rev. ed. 1937); 56 C. J. S. 483, *Trade Secrets*, Sec. 72; 35 Am. Jur. 525, *Master and Servant*, Sec. 97; Stohr, *Trade Secrets in Processes and Machines*, 8 St. Louis U. L. J. 117 (1963).

able to warrant protection by courts of equity. The various concepts used by the equity courts to justify protection of employers from the wrongful compromise of their trade secrets are the protection of a property right,¹⁵ implied contract (unjust enrichment)¹⁶ and breach of confidence (fiduciary relationship).¹⁷ Whatever the rationale for the court's decisions, it is a well settled rule of law that an employee has an absolute obligation both during and after his term of employment not to disclose to others or use to his own advantage or to the detriment of his former employer the trade secrets of his former employer.¹⁸ This is the case whether or not a written agreement has been signed by the employee.¹⁹

The Fine Line

Often in suits in equity, however, the tests are not as clear. In a given case are there actually trade secrets warranting protection? Questions to be determined are the extent to which the supposed trade secrets are known both outside the company and within; how much effort and money was put into developing the secret and guarding it after discovery; how valuable the secret is to its owners and competitors; and how difficult it would be

¹⁵ *B. F. Gladding & Co. v. Scientific Anglers, Inc.*, 245 F. 2d 722, 113 U.S.P.Q. 497 (6th Cir. 1957); *Ferroline v. General Aniline & Film Corp.*, 207 F. 2d. 912 (7th Cir., 1953). Also see Note, *Equitable Protection of Trade Secrets*, 23 Colum. L. Rev. 164 (1923).

¹⁶ *Morgan's Home Equipment Corp. v. Martucci*, 390 Pa. 618, 136 A. 2d 838 (1958), Note, *Trade Secrets*, 7 Kan. L. Rev. 222 (1958). Also see 43 A. L. R. 2d. 94, 185 (1955).

¹⁷ Opinion of the Comptroller General of the U. S., 136 U.S.P.Q. 321 (1963); *Hahn U. Clay v. A. O. Smith Corp.*, 320 F. 2d 166, 138 U.S.P.Q. 369 (5th Cir., 1963); Note, *Obligation of a High-Level Employee to His Former Employer*, 29 U. Chi. L. Rev. 339 (1962); *Standard Brands Inc. v. U. S. Partition Corp.*, 199 F. Supp. 161, 130 U.S.P.Q. 258 (E. D. Wisc., 1962).

¹⁸ *Carter Products Inc. v. Colgate-Palmolive Co.*, *supra* n. 4. Also see generally, *Stedman, Trade Secrets*, 23 Ohio S. L. J. 5 (1962); *Vitro Corp. of America v. The Hall Chemical Co.*, 292 F. 2d 678, 131 U.S.P.Q. 90 (6th Cir. 1961); *Kalinowski, Key Employees and Trade Secrets*, 47 Va. L. Rev. 583 (1961); *Symposium, Intellectual Property*, 9 Clev.-Mar. L. Rev. 1 (1960); *Gertner, Trade Secret Remedies*, 3 Tr. Law Guide 29 (1959); *Restatement (second)*; *Agency* § 396 (1958); *Restatement, Torts* § 757 (1939).

¹⁹ *Blake, Employee Agreements Not to Compete*, 73 Harv. L. Rev. 625 (1960); *McTiernan, Employees and Trade Secrets*, 41 J.P.O.S. 820 (1959). For an excellent presentation on restrictive covenants in employment contracts see *Yeager, Company Secrets Have Reasonable Protection, Nation's Business*, October, 1959, p. 14. Forms for employment contract clauses may be found in *Gordon, Employment and Agency Agreements* (1940).

for others to honestly acquire the information.²⁰ The burden of proof is upon the complainant to show that his secret is truly of value and importance, that he is the owner of it by right of discovery, and that the secret was wrongfully appropriated by defendant for his own or another's use.

The court in trade secrets cases is often faced with balancing the equities.²¹

While it is required that equity should lend its aid to the fullest extent to protect the property rights of employers, considerations of public policy and justice demand that such protection should not be carried to the extent of restricting the earning capacity of individuals on the one side, while tending to create or foster monopolies of industry on the other.²²

The point of balance lies somewhere between absolute protection of the property right of the employer and the unrestrained right of the employee to better himself by change of business affiliation.²³

Other Interests

To the struggle between the old employer and his departed employee or the new employer there has recently been added a formidable party in interest. The United States Government by reason of its enormous research and development expenditures (probably greater than 60% of all such expenditures in recent years) is now intimately involved directly and indirectly in many trade secret altercations. Through a process facetiously called "reverse engineering," the Government has been accused of us-

²⁰ Maruchnic, *Industrial Trade Secrets, Their Use and Protection*, 4 Clev.-Mar. L. Rev. 69 (1955).

²¹ *Addante v. Cinelli*, 143 N.Y.S. 2d 244 (Sup. Ct. 1955).

²² *New Method Laundry v. MacCann*, 174 Cal. 26, 161 P. 990, 991 (1916); See also *McClain, Injunctive Relief Against Employees Using Confidential Information*, 23 Ky. L. J. 248 (1935).

²³ *Hays, The California Law of Unfair Competition Takes a Turn—Against the Employer*, 41 Cal. L. Rev. 38 (1953); See also Note, *Trade Secrets*, 74 Harv. L. Rev. 1473 (1961). Cases holding for the employee on various grounds include: *Gabriel Co. v. Talley Industries*, 137 U.S.P.Q. 630 (D. C. Ariz. 1963); *Wexler v. Greenberg*, 399 Pa. 569, 160 A. 2d 430 (1960); *Bryan v. Sid W. Richardson Inc.*, 254 F. 2d 191, 117 U.S.P.Q. 157 (5th Cir. 1958). *Levine v. Johnson & Co.* 107 Cal. App. 2d 322, 237 P. 2d 309 (1951). *Contra, B. F. Goodrich Co. v. Wohlgemuth*, *supra* n. 1; *Hahn & Clay v. A. O. Smith Corp.*, *supra* n. 16; *Vitro Corp. of America v. The Hall Chemical Co.*, *supra* n. 17; *Seismograph Service Corp. v. Offshore Raydist, Inc.* 135 F. Supp. 342 (E. D. La. 1955), *modified* 263 F. 2d 5 (5th Cir. 1958).

ing proprietary data furnished in proposals by one contractor as a basis for requests for bids from other contractors, thereby compromising the property of the first contractor.²⁴

In the backwash of the drug company cases a curious government position was shown.²⁵ The Italian firms accused of buying stolen process data for the production of antibiotic drugs have been supplying the United States Government with large quantities of the drugs at lower prices than bid by American companies. The response to complaints by the American drug companies was an implied threat of investigation for price fixing. It is no wonder that Merck president John Connor is somewhat bitter in his statement on trade secret piracy.

Commercial espionage is a crime. It damages stockholders of the company whose secrets have been stolen by depriving them of their property. It damages the employees by keeping the company from increasing employment and raising wages. And it damages the public if the fruits of research cannot be protected, the incentive to develop new products and improve old ones is bound to suffer.²⁶

In the "Space Suit Case," one of the questions posed was whether confidential information acquired by B. F. Goodrich Company in the performance of a Government research and development contract and subsequently reported to the Government remains confidential so far as a competitor is concerned unless published or otherwise released by the Government. Although the court failed to tackle this question directly, the answer by reason of the decision would appear to be in the affirmative.²⁷

Following the decision in *B. F. Goodrich v. Wohlgemuth*, a Pentagon counsel was quoted as expressing concern about the growth of the trade secret spirit in industry. He likened it to a return to the old guild system of doing business, a system which was supposed to have been eliminated by the patent system.²⁸

²⁴ Harris, *Trade Secrets as they Affect the Government*, 18 Bus. Law. 613 (1963); Klein, *Technical Trade Secret Quadrangle*, 55 N. W. U. L. Rev. 437 (1960).

²⁵ *Supra*, n. 3.

²⁶ Daniel, *op. cit. supra*, n. 3.

²⁷ *B. F. Goodrich Co. v. Wohlgemuth*, *supra* n. 1; Jeter, *Trade Secrets—The Space Suit Case*, 18 Bus. Law. 695 (1963).

²⁸ *Back to the Guild?*, Newsweek, June 3, 1963, p. 62.

A National Aeronautics & Space Administration legal official was also quoted as commenting that no information developed by a company in the course of government work can be labeled a trade secret.²⁹ With this extreme position many would take issue, and the legal periodicals have carried much of the debate.³⁰

Conclusion

In their handling of trade secret cases, courts should be mindful of the dangers in either path they might follow. On the one hand, they must take care that they do not make the discoveries of corporate research unprotectable and of insufficient value to warrant further private research expenditure.³¹ On the other hand, they must take care not to bar engineers and scientists from changing jobs, as a punishment for their own productivities and abilities—a modern form of intellectual involuntary servitude.

²⁹ *Ibid.*

³⁰ Daddario, *Effect of Government Patent Policy on Research and Development*, 45 J. P. O. S. 663 (1963); Daddario, *Patent Policy for a Free Enterprise Economy*, 47 A. B. A. J. 671 (1961); Long, *Government Patent Policy to Serve the Public Interest*, 47 A. B. A. J. 675 (1961); Geoffrey, *Do the Atomic Energy Act and the National Aeronautics and Space Act Promote Adequate Space Advancements?*, 43 J. P. O. S. 624 (1961); Healey, *Current Controversy Over Patent Rights Under Government Research and Development Contracts*, 3 J. A. G. Bull. 3 (1961); *Symposium on Government Contract Patent Policy*, 21 Fed. B. J. 3 (1961).

³¹ Typical opinions in the protection of employer interests in trade secrets are the following:

For the entire course of appellant's conduct the law can offer nothing but censure. Our civilization has passed beyond the era of cutthroat competition. Not only do business men deprecate practices that deprive one's neighbor of his rights, but the ethic that abounds among upright men is to let rivals live and, if a competitor deserves success, so to act as to defeat the piracy of such advantages as he may honorably acquire.

Wallich v. Koren, 181 P. 2d 682, 685 (Calif. 1947).

An employee has the right to take employment in a competitive business and to use his knowledge (other than trade secrets) and experience, for the benefit of the new employer, but a public policy demands commercial morality, and courts of equity are empowered to enforce it by enjoining an improper disclosure of trade secrets known to the employee by virtue of his employment.

B. F. Goodrich Co. v. Wohlgemuth, *supra* n. 1 at p. 500.