Federal Trade Commission protects trade secrets

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There has been an uproar about the Federal Trade Commission's proposed ban on noncompete provisions. A noncompete clause means a contractual term between an employer and a "worker" that prevents the worker from seeking or accepting employment with a competitor after the worker's employment ends.

The FTC proposes to add a new subchapter J, consisting of part 910, to chapter 1 in title 16 of the Code of Federal Regulations defining a "worker" as a natural person who works, whether paid or unpaid, for an employer. The term includes, without limitation, an employee, independent contractor, intern, volunteer, apprentice, or sole proprietor who provides a service to a client or customer.

Why do companies use noncompetes in the first place? The shibboleth: Noncompete agreements are necessary to protect trade secrets. Years ago this may have been true but not today.

Section 5 of the FTC Act (15 USC 45) prohibits unfair or deceptive acts or practices in or affecting commerce. The proposed new FTC rule deems it an unfair method of competition for an employer to enter or attempt to enter into a noncompete clause with a worker; maintain with a worker a noncompete clause; or represent to a worker that the worker is subject to a noncompete clause where the employer has no good faith basis to believe that the worker is subject to an enforceable noncompete clause.

For years, post-employment provisions in an employment agreement have been used to block workers from freely switching jobs, suppressing wages, hampering innovation, and blocking entrepreneurs from starting new businesses.

The FTC estimates that a ban on noncompetes would expand career opportunities for 30 million Americans and increase wages by nearly $300 billion annually. See the FTC Press Release, Jan. 5, 2023.

Companies use noncompetes for workers across industries and job levels, from hairstylists and warehouse workers to doctors and business executives. In many cases, employers use their outsized bargaining power to coerce workers into signing boilerplate noncompete contracts ("If you want to work for the company, you have to sign the noncompete agreement").

Imposing post-employment restrictions on at-will employees hurts competition in the U.S. labor markets by blocking workers from pursuing better opportunities and by preventing employers from hiring the best available talent.

The evidence also shows that noncompete clauses hinder innovation that include preventing would-be entrepreneurs from forming competing businesses and inhibiting workers from bringing innovative ideas to new companies.

A trade secret audit must be deployed to identify and protect trade secret assets. There are no shortcuts in trade secrets law.

The FTC has used its Section 5 authority against Michigan-based security companies to prohibit the enforcement of noncompete agreements with any employees. See FTC Press Release, March 8, 2023. The FTC also entered consent orders with two glass container manufacturers from illegally imposing noncompete restrictions on workers across a variety of positions. See FTC Press Release Feb. 23, 2023.

So why do companies use noncompetes in the first place?

The shibboleth: Noncompete agreements are necessary to protect trade secrets. Years ago, this may have been true but not today. Today, every state has enacted the Uniform Trade Secrets Act (UTSA) — except New York — and the federal statute for the protection of trade secrets is the Defend Trade Secrets Act of 2016 (DTSA).

Therefore, prohibiting the use of noncompete clauses will have no negative impact on trade secrets law. Just the opposite is true. Companies must now establish internal trade secret control committees charged with the responsibility to establish corporate policies, practices and procedures for the identification, classification, protection, and valuation of trade secret assets.

Today, companies cannot evade their corporate responsibility to identify and protect trade secret assets by requiring every employee to sign a boilerplate noncompete agreement and then using coercive tactics and litigation to intimidate former employees and other workers into submission often at great cost to the former

employee or worker who must retain counsel and pay substantial legal fees and expenses. The corporate trade secret protection program cannot boil down to one noncompete clause in a boilerplate contract of adhesion that the employee or worker must sign on a take it-or-leave-it basis.

The same analysis holds true for non-disclosure agreements. Banning non-disclosure agreements between an employer and employee or other worker that are written so broadly that the NDA effectively precludes the worker from working in the same field after the worker's employment is a de facto noncompete agreement because it prohibits the former employee or other worker from seeking or accepting employment with a new employer after the employment.

Once again, the trade secret protection rationale falters. The employer can protect against the actual or threatened misappropriation of trade secrets under the UTSA, the DTSA, or both. However, using a blanket NDA as a subterfuge for trade secret protection — when the employer often does not even know what is the trade secret — constitutes unfair competition. The employer has not taken reasonable measures to protect trade secrets, the employee cannot pursue new job opportunities, and the public interest is hurt by decreased competition and innovation.

Trade secrets protect any information that can be used in the operation of a business or other enterprise and that is sufficiently valuable and secret to afford an actual or potential economic advantage over others.

The courts apply a six-factor test to determine whether an alleged information asset qualifies as a statutory trade secret:

> Factor 1: The extent to which information is known outside the company (the more extensively the information is known outside the company, the less likely that it is a protectable trade secret).
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> Factor 2: The extent to which the information is known by employees and others involved in the company (the greater the number of employees who know the information, the less likely that it is a protectable trade secret).
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> Factor 3: The extent of measures taken by the company to guard the secrecy of the information (the greater the security measures, the more likely that it is a protectable trade secret).
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> Factor 4: The value of the information to the company and competitors (the greater the value of the information to the company and its competitors, the more likely that it is a protectable trade secret).
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> Factor 5: The amount of time, effort and money expended by the company in developing the information (the more time, effort and money expended in developing the information, the more likely that it is a protectable trade secret).
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> Factor 6: The ease of difficulty with which the information could be properly acquired or duplicated by others (the easier it is to duplicate the information, the less likely that it is a protectable trade secret).

A trade secret audit must be deployed to identify and protect trade secret assets. There are no shortcuts in trade secrets law. Using coercive tactics and costly litigation to identify and protect trade secret assets is the wrong course. Trade secret asset management is the right course.

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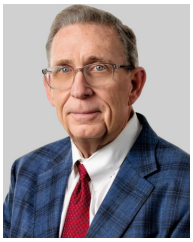
About the author



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