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Employment Law for Businesses – Easy Steps to Protect Your Business

Protecting Your Trade Secrets and
Maintaining a Competitive Advantage

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Today's Agenda

- I. What Is a Trade Secret?
- II. Importance of Restrictive Covenants.
- III. How to Get the Most from Your Restrictive Covenants.
- IV. How to Protect Assets in Absence of Restrictive Covenants.
- V. How Can Insurance Protect Your Company's Assets.
- VI. Steps to Take When Employees Resign.

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I. What Is a Trade Secret?

- Information that:
 - Has economic value;
 - Based on its secrecy (e.g., not publicly available); and
 - Is protected by reasonable efforts.



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I. What Is a Trade Secret?

- Not everything is a trade secret.
- Illinois courts look at the following to determine existence of a trade secret:
 1. Extent to which info is known outside the business.
 2. Extent to which info is known within business.
 3. Extent of measures to guard secrecy of info.
 4. Value of info to business and competitors.
 5. Amount of effort or resources used to develop information.
 6. Ease or difficulty with which info could be properly acquired or duplicated by others.

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▪ Examples:

- Production/technical methods and processes
- Research and analysis
- Strategic plans
- Customer information



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II. Importance of Restrictive Covenants

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What are restrictive covenants?

- Provisions that restrict an employee's conduct during and after employment.
- Three primary types:
 - Covenants not to compete.
 - Covenants not to solicit.
 - Covenants not to disclose confidential information.

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When are restrictive covenants enforceable?

- To be valid, a restrictive covenant must:
 - Reasonably/narrowly tailored;
 - Protect legitimate business interests; and
 - Supported by adequate consideration.



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When are restrictive covenants reasonably tailored?

- Geographic scope.
- Temporal scope.
- Prohibited activity.

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Geographic Scope

- Case by case analysis.
- Area should correspond with where the employer conducts business.
- Nationwide restrictions enforced.
- Local restrictions not enforced.



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Temporal Scope

- Fact specific.
- Determined by amount of time to develop relationship.
- Generally, restrictions of 1-2 years are enforced in Illinois.

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Prohibited Activity

- Activities must be limited and specified.
 - Restricting an employee from working in any capacity for a competitor would be invalid.
 - Restricted activity should be narrowly tailored to employee's job or similar duties.

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What is a legitimate business interest?

- Customer information and customer lists are generally held to be protectable interests.
- Must have a “near-permanent” relationship with customer with whom employee would not have had contact but for employment.
- Employee acquired trade secrets or confidential information by virtue of employment.

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**Reliable Fire Equipment Co.
v. Arredondo**

- Upgraded the “legitimate business interest” test.
- Reaffirmed the old rule that “near permanent customer relations” and “employee’s acquisition of confidential information” establish legitimate business interest.



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**Reliable Fire Equipment Co.
v. Arredondo**

- Added that those are only two of several ways to establish legitimate business interest.
- Need to look at “totality of facts and circumstances.”
- No single determining factor.

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What this means to employees?

- Lower burden than before to establish a legitimate business interest.
- Employers can argue broader categories of protectable interests.
- Courts less likely to grant motion to dismiss.

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Adequate Consideration

- All contracts, including restrictive covenants, must be supported by consideration.
- Examples of adequate consideration:
 - Part of initial offer of employment.
 - Increase of pay, promotions, bonuses conditioned on execution of restrictive covenant.
 - Continued employment in some states and under some circumstances.

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III. How Can Employers Get the Most from Their Restrictive Covenants

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First Things to Decide

- Determine whether you need non-solicitation, non-compete, non-disclosure or all of them.
- Ensure the covenant is enforceable under state law.

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Bad Non-Compete

Employee agrees that, during his employment and for **3 years** thereafter, whether termination is voluntary or involuntary, he will not **become employed** by an person or entity **who competes with** employer in the state of **Illinois**.

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Better Non-Solicitation

Employee agrees that, during his employment and for **18 months** thereafter, he will not directly or indirectly solicit or accept business from any person that (1) was a customer of employer **during the last year of employee's employment** with employer and (2) **with whom employee had contact** or **about whom employee had confidential information** during the last year of his employment.

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Other Suggestions

- Secure restrictive covenant during pre-hire negotiations.
- Draft restrictive covenant with enforcement in mind.
- Venue & forum selection clauses.
- Choice of law provision.
- Savings clause.
- Avoid arbitration.
- Attorney fee & injunction provision.

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Other Suggestions

- Take immediate action (“First-Filed” Rule).
- Employment agreement must be executed by proper parties.
- Do not materially breach employment contract.

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**IV. How to Protect Assets in
Absence of Restrictive
Covenants**

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Legal Theories to Protect Company Assets

- Illinois Trade Secrets Act.
- Tortious Interference with Prospective Economic Advantage.
- Employee's Breach of Fiduciary Duty of Loyalty.
- Tortious Interference with Contract.
- Tort of Unfair Competition.
- Computer Fraud & Abuse Act.

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Internal Security Measures

- Fine line between being too protective and not protective enough.



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Internal Security Measures

- What is necessary?
 - Confidentiality/Non-Disclosure Agreement.
 - Restrictive Covenants (and enforce them).
 - Policies providing for monitoring of computers and other company assets.
 - Intellectual Property Assignments/ Other Protections.
 - Keep trade secrets under lock & key/limited disclosure.

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Other Internal Security Measures

- Surveillance of employee email.
- Monitoring employee's use of computers.
- Security cameras.
- Surveillance of telephone calls and usage.
- Installation of software on remote computers to wipe data out, if necessary.



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Practical Pointers

- Draft provision in employee handbook addressing trade secrets and confidential information.
- Have employee execute an acknowledgement form.

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Practical Pointers (cont'd)

- Limit access to trade secrets & confidential information.
- Tighten computer security.
- Implement document handling procedures.
- Train company employees on security measures.
- Conduct annual trade secret/confidential information audit.

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V. How Can Insurance Protect Your Company's Assets

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Cyber Liability Protection

Cyber Environment:

- 497 million records containing Personal Information were breached in the U.S. from 2005-2009.
- Organized crime responsible for 85% of stolen data in 2009.
- Annual Hacker/security expert DEFCOM.

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Cyber Liability Protection

What does "Cyber" Mean?

- "Cyber" means the use of computers, internet, computer networks and electronic information databases. The more we use these items the more exposure we have to a cyber liability claim.

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Cyber Liability Protection

How are you exposed?

- These items create an exposure for your business:
 - E-commerce
 - Being connected to the Internet
 - Websites
 - Credit card Processing/On-line Payment
 - Website Design and Data Storage

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Cyber Liability Protection

Two types of Cyber Risk:

- First Party Losses—losses suffered by an organization such as extortion, employee theft or system failure.
- Third Party Losses—hacker theft of data, intellectual property infringement, etc.

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Cyber Liability Protection

What is a data/privacy breach?

- A security incident, in which confidential or sensitive information is stolen, copied, viewed or transmitted by unauthorized individuals. Financial information and personal health information are some of the most common breaches.

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Cyber Liability Protection

Coverage available:

- **First Party—Loss of Digital Assets:** We will indemnify you for loss you incur, in excess of the applicable deductible, including specials expenses, as a direct result of damage, alteration, corruption, distortion, theft, misuse, or destruction of your digital assets, directly caused by a covered cause of loss.

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Cyber Liability Protection

Typical Causes of Loss:

- **Accidental Damage or Destruction** (Power Failure or Physical Damage of data).
- **Operational mistakes** (Entry/Modification of your data).
- **Computer Attacks/Crime** (Malicious code introduction, unauthorized access, unauthorized use or denial of service attack).

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Cyber Liability Protection

- **Third Party—Network Security and Privacy Liability:** Damages and claim expense arising from an alleged breach of security or privacy breach. Your company is hacked and customer financial information is stolen.

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Cyber Liability Protection

Security Event Cost:

- Sub limits are typically provided for:
 - Customer notification of a privacy breach.
 - Credit monitoring costs.
 - Public relations costs.

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Cyber Liability Protection

Claim Example:

- Cyber Liability—Data Security
 - A part-time hospital employee gained unauthorized access to confidential electronic patient records and discussed with co-workers an individual's HIV status. The individual sued the hospital for lack of adequate IT security measures in protecting digital patient records. The hospital was held liable for \$250K and \$85K was spent on defense.

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Cyber Liability Protection

Claim Example:

- Cyber Liability—Missing Data
 - An employee of a financial institution loss their laptop with sensitive client data. Multiple lawsuits pending by individuals whose data has been compromised. Total defense cost exceeds \$700M.

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Cyber Liability Protection

What can you do to protect your company?

- Firewall, Virus protection.
- Cyber Risk Assessment.
- Awareness Training.
- Purchase Cyber Liability Coverage.

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VI. Steps to Take When Employees Resign

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What to Do When Employee Resigns

- Almost 60% of employees steal company information when they leave.
- Protective measures are needed before and after employee departs.
- Steps can be modified/reduced based on company/industry/position.

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Practical Pointers

1. Ensure return of records and property.
2. Discontinue remote electronic access.
3. Discontinue local electronic access.
4. Escort from premises at termination.
5. Quarantine employee's computer if misconduct is suspected.

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Practical Pointers

6. Inform and transition employee's clients quickly.
7. Interview co-workers.
8. Pay final compensation.
9. Social media research.
10. Exit interview – remind employee of obligations.

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Exit Interview Checklist

- Reinforce & highlight obligations under restrictive covenants.
- Documents or computer files may not be taken.
- Check home or property for company property.



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Exit Interview (cont'd)

- Must return all company property (computers, laptops, PDA's, cell phones).
- Keep record of all returned property.
- Do not copy any client lists from computer or rolodex.
- Do not contact clients to inform of departure while still employed at employer.

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Exit Interview (cont'd)

- Continue to dedicate efforts to employer while still employed.
- Must communicate customer calls, leads & business opportunities to employer while still employed.
- Do not delete or modify anything from computer without prior express & written approval of supervisor.

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Attorneys at Law

Questions?

ARNSTEIN & LEHR LLP
Attorneys at Law

E. Jason Tremblay
Arnstein & Lehr LLP
120 South Riverside Plaza
Suite 1200
Chicago, Illinois 60606
Work: (312) 876-6676
Cell: (773) 710-3438
ejtremblay@arnstein.com



Carolyn Hanna
Corkill Insurance Agency, Inc.
25 Northwest Point Boulevard
Suite 625
Elk Grove Village, IL 60007
Work: (847) 437-2831
channa@corkillinsurance.com
