



3 Major Points to Consider When Deciding Whether to Sue Over Restrictive Covenants and Trade Secret Violations

Insights

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Restrictive covenant and trade secret litigation is on the rise, and it typically involves an extremely public dispute that can require you to expend significant resources without any certainty of a favorable outcome. Moreover, a failed lawsuit can actually do more harm than good to your enforcement efforts because a highly public – and potentially precedential – decision may embolden more employees with similar restrictions to discount them. Therefore, company leaders must study and carefully decide whether to venture publicly into a dispute forum with a former employee who has misappropriated the company's trade secrets or violated non-competition and other restrictive covenant provisions. What are the top three points you should consider when deciding whether to litigate?

1. Decide What is at Stake and Know Your Company's Goals

Was the stolen trade secret hugely important to your company, such as insider knowledge regarding a lucrative product being developed or service to be offered? The more significant and valuable the information, the more likely litigation is an important and necessary course to protect the company's interests – and time may be of the essence. Remember, to prevail in restrictive covenant and trade secret litigation, a court must find that valid and valuable confidential information has been misappropriated and that the company has taken reasonable efforts to protect that interest.

Know your company's goals in seeking to litigate. Consider the following questions:

- Are you looking to sue and obtain a quick and public settlement agreement with the former employee and their new employer agreeing they will not use your confidential information under threat of sanctions for violations?
- Are you seeking to go the distance because the non-compete issue at stake is that important? That was the case in *DNOW v. Eoff*, where a Texas jury recently awarded the former employer \$9 million in damages against former employees who conspired to steal the company's trade secrets.
- Are you seeking to use a lawsuit to warn other employees that you will enforce violations of written restrictive covenants, non-disclosure or confidentiality agreements, and applicable federal and state statutory protections (such as the federal Defense of Trade Secrets Act and state statutory trade secret laws)?

Clearly identifying your goals facilitates the necessary litigation analysis. For example, if the goal is to make a point and warn other employees about the importance of compliance with their trade secret obligations, then it is wise to choose a strong and provable violation as the best test case.

2. Perform an Evaluation of the Risks and Likely Rewards Before Litigating

Restrictive covenant and trade secret litigation is time consuming and cost intensive. Indeed, the American Intellectual Property Law Association studied trade secrets litigation costs and found that where the financial risk at issue ranged between \$10-25 million, the average litigation cost was \$4.1 million.

Before embarking on litigation, the prudent employer will obtain a risk/reward (or pros/cons) evaluation with a competent and savvy litigation team that will analyze the facts, the likely applicable law, and the jurisdictions in which a lawsuit could be brought. The team should ascertain the likelihood of prevailing on the merits and the costs (both human and economic) and risks (both legal and non-legal) associated with proceeding in a public forum. The factors to consider in the analysis include, but are not limited to, the following:

The Forum

Oftentimes, the company will have a choice of forums in which to sue – leading to questions about whether to bring suit in federal or state court, and even potentially which state in which to litigate. It is important to choose a forum that is known for protecting a company’s valuable confidential and trade secret information.

The Current Political Climate and Agency Perspectives

The current political climate and agency perspectives must likewise be considered. Many states are enacting legislation to prevent litigation that restricts a former employee’s ability to become re-employed or that is perceived as being an unwarranted restriction on competition. Likewise, agencies are becoming very active in opposing restrictive covenants, including non-compete, confidentiality, and non-disparagement provisions.

For example, the Federal Trade Commission has proposed a rule to ban all non-compete agreements nationwide. Similarly, the National Labor Relations Board takes the position that broad confidentiality provisions unlawfully interfere with an employee’s Section 7 rights (including the right to engage in protected concerted activity) under the National Labor Relations Act. Although there is a growing public sentiment that restrictive covenants are unfair restraints of trade, a surprising number of companies prevail as plaintiffs in trade secrets litigation.

The Strength of the Facts, Supporting Documentation, Expert Witnesses, and Customer Considerations

Another factor to consider is the enforceability of the contract at issue, as contracts that have been in place for a number of years may not comport with the requirements of current law. Be certain your contract doesn't overreach. If it does, show willingness to be reasonable and blue pencil it (to lighten the restrictions) in negotiations with the other side.

Also consider the level or particular involvement of the former employee against whom your company would initiate suit. Are you seeking to restrict a person in a position to do damage to your company, such as a C-Suite executive, key marketing and salesperson, or an employee who is otherwise in a position to effectively use the confidential information to your company's detriment? And know whether your company has "clean hands," as a skeleton in your company's closet could negatively impact the outcome of the case.

Have strong proof. The quality and quantity of proof matter greatly, so you should consider:

- Are your facts solid?
- Are your witnesses believable?
- Do you have a qualified expert to testify in support of your company's position?
- Do you have good forensic evidence, such as emails showing the departing employee stole your company's confidential information?
- Does a forensic review of the employee's company-issued computer show sensitive files were copied to external devices shortly before the employee's departure?

The stronger your evidence is, the greater the likelihood of prevailing. Moreover, recognize that litigation might necessarily involve and even inconvenience or annoy your customers (for example, involving your customers and vendors in non-compete litigation against a sales representative might greatly irritate them). If you are not willing to run that risk, you may need to forgo litigation for business reasons.

The Commitment of Human and Economic Resources

Make sure your company has the bandwidth and resources to vigorously pursue litigation.

- Do the key witnesses have the necessary time to devote to pursue litigation?
- Are they immediately available for emergency injunctive proceedings?
- Will they be available for the duration of the litigation, including for depositions, hearing preparations, and trial?

The involvement of strong, key company witnesses is a necessity and will make a significant difference in whether the company ultimately prevails. If the company's key witnesses are too busy on more important projects, a lawsuit may not be a high enough priority to warrant pursuit.

Likewise, litigation costs can be substantial, including attorneys' fees, potential expert witness fees (such as economists' fees for modeling lost revenues for a new product when the former employee misappropriated the product details and beat the company to market), forensic review fees, and the like.

When analyzing whether to sue, it is also important to consider the likelihood of whether the defendant(s) will assert counterclaims, which can also impose significant costs and some risks to mounting a successful defense.

Definition of a Successful Outcome

Assess the injunctive relief and damages that are available and whether the likely recovery will make litigation worth the effort.

- One main purpose in pursuing trade secret litigation is to act swiftly to protect any confidential information that has been misappropriated and obtain an injunction before the information can be used against the company.
- Another purpose can be to prevent a former employee from working for a competitor for a period of time.
- A third purpose can be to secure monetary damages.

You must assess whether an investment of the required time and resources would be worthwhile under the applicable facts and circumstances.

The Risk of Potential Public Disclosure of a Trade Secret

Consider how highly confidential your company's trade secret is and whether the court can provide adequate protection from disclosure. Some courts are reticent to provide broad-sweeping confidentiality orders because of the inherent conflict with the constitutional right to public access to the proceedings and documents.

The U.S. Supreme Court has noted that "public access plays a significant positive role in the functioning of the particular process in question" and that the public's right to access can be overcome "only by an overriding interest based on findings that closure is essential to preserve higher values and is narrowly tailored to serve that interest." However, SCOTUS has also held that "the publication of materials that could result in infringement upon trade secrets has long been considered a factor that would overcome the strong presumption" of public access to court proceedings.

The Risk of an Adverse Decision

No universal formula exists for what you must prove to win a trade secret misappropriation case, and depending on the forum, courts may generally require proof of two to six elements (including reasonableness of the measures, validity and value of the trade secret claim, wrongful conduct/misappropriation, etc.). Oftentimes, the company is pursuing the claim based on the former employee's contractual obligations, which may be present in other employee contracts.

You must consider the impact of a possible adverse decision, especially a finding that the contract provisions are unenforceable. Such a decision could have wider ramifications than just the case at hand. If you are suing for the first time to enforce fairly uniform contractual and/or statutory obligations, it is wise to make sure you have selected the best test case for enforcement of your rights.

3. Consider Additional Steps Before Commencing Suit

Assuming your risk assessment supports litigation, you should nevertheless engage in certain additional steps before suing. It is wise to warn the departing employee of their contractual obligations in an exit interview and to even make clear you will take action to enforce your company's legal rights. Giving notice of the restrictive covenants to the potential or new employer may also be advisable depending on the circumstances, as doing so can preserve future claims against the new employer if it engages in or encourages conduct that violates the covenants' terms. Cease and desist letters can also serve this valuable purpose.

Try to resolve the dispute pre-suit if possible. Oftentimes, parties are able to agree on injunctive terms that protect the company's interests without the need for prolonged (and expensive) litigation. Courts may also require the parties to attempt resolution before issuing temporary restraining orders. Even if initial settlement attempts are not required, it helps to get the court on your side if you can show you tried to secure a compliance agreement short of protracted litigation but were met with abject resistance. Be prepared to show reasonableness on your company's part.

Be ready with public relations, investor relations, and media responses. If the suit will be high profile, you should anticipate the need to make statements addressing the situation, not only outward-facing but also internal statements to advise employees about what's going on.

Conclusion

Just as a prudent person only runs a marathon after significant preparation, so too does the wise company get all of its ducks in a row before litigating the restrictive covenant or trade secret violation case. Only then can you put yourself in the best position to achieve a highly favorable outcome.

We will continue to monitor the latest developments on protecting your trade secrets and other confidential information, so you should ensure you are subscribed to [Fisher Phillips' Insight System](#) to gather the most up-to-date information. If you have questions, please contact the authors

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Barbara Jean D'Aquila
Partner
612.216.2743
[Email](#)

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