

Practical Aspects of Secrecy

Secrecy Agreements concerning disclosure of know-how must be carefully drafted, consider circumstances and parties' positions

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In a preceding paper*, Hans B. Thomsen explained very clearly why it is necessary to protect know-how under a secrecy agreement. This paper will present practical aspects of how to obtain such a protection. However, because of limited space here, do not expect coverage in detail. On the other hand, being based on experiences from one particular technological field, this paper may provide guidance which may be useful for other technological fields.

A Model Form of a secrecy agreement has been developed for use in our company. In this connection, a warning may be appropriate. A secrecy agreement like any other agreement should always be drafted in due consideration of all circumstances under which it is to be used and with due regard to the two parties' position. Accordingly, a secrecy agreement drafted for one particular situation should only be used for a different situation after a careful adaptation. Similarly, a Model Form of a secrecy agreement will always require certain modifications to suit a particular situation. In other words, an ideal secrecy agreement has to be tailor-made.

In this paper, the above Model Form will be discussed and relevant parts of it will be quoted. However, as already stressed, it is important to know the situation for which a secrecy agreement will be used. Therefore, a brief explanation of the circumstances for which the Model Form has been developed and for which it is being used will be given.

SECRECY AGREEMENTS IN LICENSING OF CHEMICAL PROCESS TECHNOLOGY

Basis for this discussion of practical aspects of secrecy agreements are experiences from licensing in the field of chemical-process technology. The products in this field are basic chemicals manufactured in bulk form and in big quantities. These products may be

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solid, liquid, or gaseous. Typical products are ammonia, methanol, urea, sulphuric acid, hydrogen, and formaldehyde. The processes during which these products are manufactured are typically conducted continuously and to a great extent in the presence of catalysts. Normally, each product is manufactured during a series of consecutive processes based on the use of a specific catalyst.

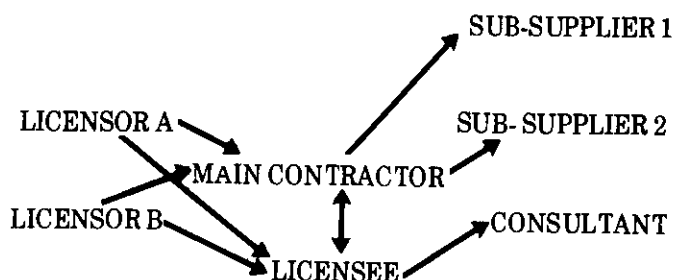
A plant for a product like one of those mentioned above has to be designed specifically for this product and with a view to optimizing energy and material balances. This can only be achieved during a high degree of integration of the consecutive processes. Consequently, a potential licensee who is planning to manufacture one of these products will have to acquire much more than just a license to operate a single process or to manufacture a product. Licensing in the field of chemical process technology is associated with a number of other activities required for constructing and operating a chemical process plant.

This complexity of activities, particularly during the construction phase, also affects the preceding phase, i.e. the phase during which a potential licensee is seeking information from the licensor for evaluation. During this phase, the licensor's know-how will have to be disclosed not only to the potential licensee, but also to third parties who have to be involved in the evaluation at this stage.

The diagram shown below serves to illustrate the flow of information during the evaluation phase. Typically, the potential licensee, who is planning to set up a new plant, will ask a main contractor to submit an offer for the plant. This offer may be based on a process technology obtained from one licensor or normally from more licensors. The main contractor may have to obtain offers for the supply of equipment and engineering services from a number of sub-suppliers. In some cases, the licensee will seek assistance from a consultant for a technical and economic evaluation of

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FLOW OF INFORMATION



the offer. Accordingly, during the evaluation phase, the know-how of a licensor will be disclosed to a number of different parties as shown on this diagram. A corresponding number of secrecy agreements for protecting the know-how will, therefore, have to be signed.

In addition, it is quite normal for a potential licensee to invite several competing main contractors to submit offers. The number of main contractors may typically vary from two to five. The same process licensor may be involved in more than one offer for the same plant. However, to avoid further complication only one main contractor has been indicated on the diagram.

This was a brief explanation of a typical situation in which secrecy agreements are used in connection with licensing of chemical process technology. Our company is currently licensing technology of our development as well as technology acquired from others. Accordingly, we have experience in disclosing know-how as well as receiving know-how. This experience will be the basis for the discussion presented in this paper.

FORM OF SECRECY AGREEMENT

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Secrecy commitments should normally be undertaken in writing. The applicable secrecy agreement can be drafted in various forms. Very often it is drafted as a letter agreement to be sent in duplicate from the disclosing company. When this letter has been acknowledged and accepted by the receiving company, the secrecy agreement has been executed. Under other circumstances, it may be appropriate to draft a secrecy agreement as a formal agreement to be executed by two parties, the disclosing company and the receiving company.

In spite of the obvious differences in form, the content of a letter agreement is rather similar to the content of a formal agreement. The agreement, like the formal agreement, should give the designation of the parties by their company names. An introductory part of the letter agreement serves the same purposes the whereas-clauses of the formal agreement. The operative clauses may in both cases have the same content, although they will be drafted in a different form. In the letter agreement, reference to the parties in the clauses may be given by personal pronouns (first and second person). In the formal agreement, reference to the parties normally will be given by abbreviated designations as defined in a preamble. The Model Form referred to earlier and discussed in the following has been drafted as a letter agreement.

However, before this discussion, a third form under which secrecy commitments can be undertaken will be mentioned for the sake of completeness. Under certain circumstances, it may be practical to use a declaration signed only by one party, the receiving company. The content of this declaration may follow very closely the content of the letter agreement mentioned above. The main difference, of course, is that the declaration unilaterally imposes obligations on the part of the receiving company without imposing any obligations on the disclosing company.

PREAMBLE

Whichever form of secrecy agreement is used, the circumstances related to the disclosure of know-how

should be carefully stated in a preamble. In a formal agreement, the whereas-clauses will normally serve this purpose. In a letter agreement, a brief introduction will serve the same purpose. The preamble should state the background for the disclosure and explain the position of the two parties. Such statements may prove useful for a later interpretation of the agreement. Therefore, much care should be taken in drafting the preamble, and the circumstances of each case should be duly taken into account. This applies to a secrecy agreement to the same extent as it applies to a license agreement, or any other agreement.

As an example of a preamble, the introductory part of the Model Form is quoted together with some basic definitions as follows:

Dear Sirs,

Secrecy Agreement

We understand that you are interested in obtaining technical information on our _____ technology in order to evaluate its incorporation in a future _____ plant which you are contemplating to set up for the manufacture of _____. For this purpose, we are prepared to disclose to you, either directly or through a party authorized by us to do so, the necessary proprietary technical information concerning our _____ technology, which we have developed over many years and in which we have invested substantial time and money. In consideration of our disclosure to you of such information for above purpose, we hereby ask you to agree as follows:

1. PROCESS shall mean a process for the manufacture of _____ as developed by us and briefly described in _____.
2. TECHNICAL INFORMATION shall mean data, plans, specifications, flow sheets, drawings, operating instructions, and information relating to PROCESS.

EXCLUSIONS FROM SECRECY OBLIGATIONS

In the paper referred to earlier, Mr. Thomsen has already emphasized that you should avoid to claim secrecy in respect of information which is available in the public domain. Similarly, you should avoid preventing the receiving company from using its own information and from receiving information which has been lawfully obtained from a third party. Accordingly, it is important to exclude such information from the secrecy obligations.

For this purpose, the secrecy obligations of the Model Form provide certain exclusions as follows:

3. You agree to hold in confidence and not to disclose to third party any part of TECHNICAL INFORMATION furnished directly or indirectly, in writing or otherwise, to you by us, except such parts:
 - (a) which at the time of the disclosure to you by us are in the public domain, or which later on become part of the public domain through no breach of this Agreement.
 - (b) which you can show were in your possession prior to the disclosure to you by us and were not previously obtained by you directly or indirectly from us, or
 - (c) which you can show were received by you after the time of disclosure hereunder from a third party who did not acquire such information directly or indirectly from us.

It is relatively easy to determine, when exclusion (a) will apply. The availability of information in the public domain can normally be proved without too much difficulty. With respect to exclusions (b) and (c) there is a problem of how to prove when they are applicable. In the above example, the burden of proof is placed on the part of the receiving company.

Depending on the circumstances it may be desirable to stipulate certain criteria for qualifying specific information for being excluded from the secrecy obli-

gations. Particularly, specific obligations only, if crucial elements of it is within one of the exclusions of paragraph 3. This would be clarified by the following provision of the Model Form:

4. It is understood that specific TECHNICAL INFORMATION disclosed to you by us shall not be deemed to be within any of the three exceptions (a), (b), and (c) of Paragraph 3 of this Agreement, merely because it is embraced by more general information within one of these exceptions.

Paragraph 3 quoted above does not specify a limitation of the secrecy period. Whether or not such a limitation is required, will depend very much on the type of technology involved and on other circumstances related to the disclosure of know-how. There may be cases where there should be no limitation. The exclusions provided in Paragraph 3 will provide the necessary possibilities for releasing the receiving company from the secrecy obligations as the know-how gradually becomes available in the public domain. This will also apply in cases where a patented invention is associated with the know-how. In such cases, of course, the position is determined by the patent laws of the country in question. After expiration of the patent, the invention belongs to the public domain and can be freely exploited irrespective of the secrecy agreement.

On the other hand, there are cases where an infinite secrecy period would be obviously inappropriate. The period which is eventually agreed upon between the parties may be anything from a few years till 20 years or longer and can be incorporated in the Model Form by amending first line of above Paragraph 3 as follows:

3. For a period of x years, you agree . . .

A secrecy agreement will often include provisions concerning the position of the receiving company's employees who will have access to know-how of the disclosing company. Two variations of a suitable Paragraph 5 included in the Model Form are the following:

5. You agree to assume responsibility for the actions of such of your executives and employees who may have access to TECHNICAL INFORMATION.

5. (Alternative)

You agree to make known to such of your executives and employees, to whom TECHNICAL INFORMATION may be disclosed, the conditions of this agreement and to ensure that they are under obligation to be bound thereof.

The first variation makes the receiving company responsible for the conduct of its employees. However, to what extent it is necessary for the receiving company to take steps to make the employees aware of and to be bound by the secrecy obligations is left to be decided at the discretion of the receiving company. The second variation is more specific in this respect. It stipulates that the employees shall be informed about and shall be bound by the secrecy obligations.

In rare cases, the receiving company may be asked to obtain individual secrecy agreements on a prescribed form from all its employees who will have access to know-how of the disclosing company. This may cause problems, not the least in the event that the prescribed form contains provisions in contravention of the laws of the receiving company's country. In such cases, of course, proper attention should be paid to a study of applicable employment acts.

Normally, a secrecy agreement does only concern disclosure of know-how. In order to underline that no license or any other rights are implied under the

secrecy agreement, the following paragraphs are included in the Model Form:

6. This Agreement shall not be construed as granting to you any license rights or other rights relating to PROCESS, except as expressly provided herein or specifically agreed to by us in writing.

7. You agree to make no commercial use of and not to incorporate in any plant any part of TECHNICAL INFORMATION, except if within any of the three exceptions (a), (b), and (c) of Paragraph 3 of this Agreement or except if specifically agreed to by us in writing.

For a thorough and complete evaluation of disclosed know-how, it will often be necessary for the receiving company to disclose certain parts of the information to third parties who will participate in the evaluation. This would be the case when know-how is disclosed to a potential licensee who is considering to set up a chemical process plant. In such a case, information may have to be disclosed, partly or in whole, to a main contractor, one or more sub-suppliers, a consultant, and possibly other third parties as already indicated on the diagram referred to previously.

Consequently, further secrecy agreements are required for protecting the licensor's know-how. When the circumstances for further disclosure are known at the time of drafting the secrecy agreement, it may be appropriate already at this stage to include provisions for disclosure to certain third parties and to give instruction regarding secrecy agreements which are required for such third parties. Such provisions would necessarily vary from case to case and for this reason they have not been included in the Model Form.

The Model Form has no provisions for arbitration, governing law, and consequences of breach of agreement. Whether such provisions are necessary, will depend very much on the circumstances and may be decided upon from case to case.

The concluding part of the Model Form, which provides space for acknowledgement by the receiving company, reads as follows:

If the foregoing terms and conditions are acceptable to you, please indicate your confirmation by signing and returning to us the acknowledgement copy of this letter.

Yours faithfully,
DISCLOSING COMPANY

Accepted and agreed to:
RECEIVING COMPANY:

As emphasized in the introduction of this paper, this discussion of various aspects of secrecy agreements has been based on our experiences in the field of chemical process technology. These experiences and the conclusions which can be drawn from them may not necessarily be valid for other fields. Therefore, they should at least be critically judged with due regard to differences which may exist from one field to another. This is the reason why some time has been spent on explaining characteristics of licensing in the field of chemical process technology.

Provisions and other relevant parts of a Model Form of a secrecy agreement have been quoted in this paper as a basis for the discussion. However, as underlined previously, a Model Form should not be used without a critical consideration of the circumstances under which — and the purpose for which — it will be used. Additional provisions may be needed and, above all, a proper adaptation should be made.