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CONFIDENTIALITY AGREEMENT UNDER COMPANY LAW A CRITICAL ANALYSIS

ABSTRACT¹

The confidentiality agreement is something that is used to protect sensitive information that may be related to the company, employee, or employer. The concept of confidentiality came in the early independent days in India as it is the growing time for the business and it became basic and the most important feature during the era of globalization as it protects sensitive information along with the trade secrets which plays a major role in the business. The non-disclosure agreements and confidentiality agreements serve the same purpose but confidentiality agreement is of higher notion as it is more complex and provide much protection and widely used in the companies. The purpose of the confidentiality agreement came to light when there is a need to discuss the sensitive information among the employer and employees of the company as its disclosure to the outside might lead to serious damage to the company. Especially the company would be at stake if any employee who is working it has resigned and started working with the competitor company of the same field knowing all the secrets of the former company so to overcome this kind of problems the contract of confidentiality is used. So in this paper, I want to deeply research the topic of confidentiality agreements and how it is helping companies in the contemporary world in the perspective of company law and how these contracts are valid under contract law.

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I. INTRODUCTION

In the contemporary world, all the companies are sustained based on new ideas and innovative thoughts as they play a vital role in deciding the future and sustainability of a company in the particular field. These are considered as most precious information that needed to be kept in secrecy by the employees of the company, generally, the secrets that are exclusively related to a company are known as trade secrets of that company. For example, the formula of the Coca Cola which is considered as one of the most precious trade secrets has been protected by the company by keeping it in one of the world's toughest lockers.

In *Coca-Cola Bottling Co. of Shreveport, Inc. v. the Coca-Cola Co.*² after working for a year they resigned and started working in the competitor company for which the company sued the employees for breach of confidentiality and investigation has been laid down. Later it was found that the three employees were found guilty of sharing the secret of Coca-Cola Company with other competitors. To protect the company and its secret there is a need to establish a proper agreement between the employee and employer to safeguard the sensitive information of the company. After the globalization and the rapid development of innovative ideas and startups in the 20th century, it became mandatory for employers to protect the secret information between them and their employees.

To save themselves from that kind of fraud it became a basic thumb rule for the companies to include the non-disclosure or non-competition clauses in hiring the employees under a particular company. The companies if needed based on the necessity started introducing confidentiality agreements between the company and its employees. The employees and the trade secrets are considered as the two major attributes and the assets of a company to run it successfully.

II. HISTORICAL BACKGROUND

The usage of non-competition and non-disclosure clauses started even from the early stages of the establishment of corporate structures in the 1950s. In the early times, the usage of these clauses is to protect themselves from the competition that they have to face in the market. The non-competition clause doesn't mean to protect them from the lawful traders but from the clutches of unfair competition as no person is restraint from the lawful trade as mentioned in

² *Coca-Cola Bottling Co. of Shreveport, Inc. v. the Coca-Cola Co.*, 107 F.R.D. 288, 227 U.S.P.Q. (BNA) 18 (D. Del. 1985) o

Indian Contract Act, 1872³. In the 1980s and 1990s, the usage of these agreements became more prominent to save themselves from the hands of former employees as there is always a threat from the ex-employees. The main aim for using these confidentiality agreements is to save the private information of the company which if leaked leads to serious damage to the affairs of the company. Companies also try to save the pattern of the working system of a company as even its disclosure to its competitors may also lead to serious damage to the company.

III. OBJECTIVES/AIMS OF THE STUDY

- The main of this project is to understand the need for the creation of Confidentiality agreements
- To understand the need for the introduction of non-disclosure clauses along with non-competition clauses.
- They understand the importance of creating confidentiality agreements under the company law and contract law of India

IV. SCOPE OF THE STUDY

The researcher has limited herself to the confidentiality agreements under company law and Contract law of India as it is a wide topic to explain the use and evolution of the same in the modern-day world among the corporate structures.

V. LITERATURE REVIEW

- 1) **Radack, David V. "Understanding confidentiality agreements." JOM 46.5 (1994): 68.**

In this article, the author has stressed the use of confidentiality agreements and how it is useful for employers in order to save sensitive information along with the ways how one can deal with the breach of confidence.

- 2) **Bast, Carol M. "At what price silence: are confidentiality agreements enforceable." Wm. Mitchell L. Rev. 25 (1999): 627.**

³ Section 27 of Indian Contract Act, 1872.

In this article, the author explained the enforceability of the confidentiality agreements by giving much emphasis on the different measures that have to be taken care of and how to deal with different breaches of confidentiality agreements.

VI. NEED FOR CONFIDENTIAL AGREEMENTS TO PROTECT COMMERCIAL SECRECY

Types of confidential information

Employee information

Confidentiality agreements are generally found in between the employees and employer to safeguard the secrets of the company but we often forget that the information provided by the employees should be protected as they also provide the personal information and sensitive information to the company in the process of acquiring the job in the company. For example, if the information provided by the X may be used by the Y to get access to the confidential documents which may lead to undesired consequences. As there are more chances of misappropriation and commission of frauds the company should equally protect the personal data of the employees.

Business information

The business information is related to any trade secrets that are unique to a particular company and these have to be protected with utmost care and caution as they play a serious role in the affairs of the company. The trade secrets will give a competitive edge to the company as they are unique to the company and the revelation of the same to the outside world may ruin the company by giving an edge to the other competitors. Generally, the employees who are working in the technical group or any employees will have access to this information to which the public doesn't have access. So the company will enter into confidentiality agreements and non-disclosure agreements with the employees in before hands to protect the same.

In some of the cases where the two companies are merging or if any one of the company is acquiring the other company in which the target company is holding some shares then there is a need to enter into the confidentiality agreements between both the parties as the acquiring company will have the access to the confidential information of the target company.

Management information

The information regarding the management of a company is also important sometimes though it is not illegal per se it has paramount importance when the employees are considered as the precious assets of the company. For example, if A has used the information of the disciplinary committee regarding B may somehow affect the reputation of B. so the company has to maintain some secrecy in its regular affairs which are sensitive.

VII. LEGAL PROVISIONS THAT MANDATE THE CONFIDENTIALITY AGREEMENTS

Under Contract law

The law related to the confidentiality and protection of Trade secrets is not well developed in the case of India when compared to the US and UK. US has separate legislation known as Uniform Trade Secrets Act (UTSA) which exclusively protects trade secrets. As most of the Indian laws are derived from English law the concept of confidentiality is more of common law countries than contractual law.

However, any agreement made between the two parties as a confidential agreement that is abiding by the Indian Contract law is considered valid in the Indian courts. For example in the case of Sunil Mazumdar v. Aryodaya Spinning & Weaving Mills Co. Ltd.⁴ The defendant was a diploma holder and qualified technician in the textiles industry and entered into a contract for working in a spinning mill for a term of 5 years in the plaintiff company and has signed and started working accordingly. After the completion of work for a year, he left the job and started working in the other spinning mill company that is a competitor of the plaintiff. He not only started working but he has the exact information of spinning of the cloth through the particular breeding season that is used in the plaintiff industry and has revealed the same to the competitor. This was considered as a breach of confidential information along with the breach of terms and conditions of the employment and the court has granted the injunction.

The main criteria to grant an injunction in the particular case is a breach of confidential information or revealing of a trade secret but not merely the vague restraint of trade as that is not acceptable under sec 27 of the Indian Contract Act, 1872. In the other case Magan Lal v.

⁴ (1964) A. Guj. 115)

Ambica Mills⁵ the court did not grant the injunction as there was no element of trade of secret and held that mere competition and the employee's own skills (personal) are not considered as the valid reason for restraining the other party.

Under competition law

Section 57 of the Competition Act, 2002 deals with the Restriction on disclosure of information.

Without the prior written permission of the enterprise, no information relating to any enterprise, which has been obtained by or on behalf of [the Commission or the Appellate Tribunal] for this Act, must be divulged other than in compliance with or for this Act or any other law now in effect.⁶

Later it was amended in the year 2007 Competition amendment Bill as Clause 44 states. This section proposes to amend Section 57 of the Competition Act of 2002, which deals with restrictions on information disclosure. As a result of the proposal to create a new Chapter VIII-A via Clause 43 of the Bill, it is proposed to put the Appellate Tribunal under the ambit of Section 57 of the Competition Act, 2002. The suggested change has a significant impact.

The main purpose of introducing these laws is to protect the trade secrets and thereby maintaining the commercial secrecy of business rivals.

In the Sterile industries v. Designated authority⁷ it was held that in the situation where there is no trust or anti-trust issues exists it is mandatory to keep the confidential information protected by the designated authority as it is the only way to prevent it from exploitation through competitive authorities. Section 41(3) of the Competition Act helps in safeguarding the information during its investigation. This section can be applied under Section 240 and Section 240-A of Companies Act, 2013 if the investigation activities are undertaken in pursuance of the Director-General.

Section 57 of the Competition Act, 2002 provides the information about the exceptions where confidentiality can be not claimed or the information has to be disclosed.

(i) Waving of the right by the enterprise itself; and

⁵ (1964) A. Guj. 215)

⁶ Sec 57 of Competition Act, 2002

⁷ (2006) 10 SCC 386 : (2003) 158 ELT 673

(ii) For this Act or any other law for the time being in force.

Disclosure of the Identity of the Informant- The proviso to Regulation 6(a) of the Competition Commission of India (Lesser Penalty) Regulations, 2009 provides for the conditions under which the identity of the applicant may be disclosed, if:

- (a) The disclosure is mandated by law; or
- (b) The applicant has voluntarily consented to disclose in writing; or
- (c) The applicant discloses it publically.

Grounds for Taking Away the Privacy of an Enterprise. During a Proceeding—Regulation 47 of the Competition Commission of India (General) Regulations, 2009 requires the proceedings before Commission not to be open to the public. However, the Commission may direct otherwise and record the reasons for the same. The factors to be taken into account by the Competition Commission of India (CCI) while deciding on this matter are:

- (a) If no significant harm is caused to the party owing to the disclosure.
- (b) Level of encouragement in publishing the information.
- (c) Efficiency and smooth functioning of the proceeding.
- (d) Considerations for the Commissions such as its resources.

According to Rule 7(3) of the Customs Tariff (Identification, Assessment and Collection of Anti-Dumping Duty on Dumped Articles and for Determination of Injury) Rules, 1995, if the designated authority concludes that the information does not need the protection of confidentiality, he can 'disregard that information'.⁸

In *LM Ericsson (PUBL) v. Competition Commission of India*⁹ there was an issue of apprehension of leakage of confidential information which was provided to the Commission. The Delhi high court held that the Director-General and Employees of the company have a duty to protect the confidential information and they have to take care of additional measures to safeguard the information.

Under company law

⁸ Bhumesh Verma, Managing Partner and Shashank Saurabh, Student Researcher, Corp Comm Legal (2020) PL (CL) March 80

⁹ 2016 SCC OnLine Del 1951.

Generally in company law, the confidential agreement plays a vital role during the merging and acquisitions of a company.

During the merger and acquisition, a company that is acquiring the target company has much access to its information. So it is necessary to an agreement with the company that it will not reveal the trade secrets of the target company and it will save the unpublished information within themselves. The people who have access to this unpublished information and any insider information may misuse them for their gains. To control these kinds of acts the Security Exchange Board of India has introduced some regulations. SEBI regulations 2015 provided information about the prohibition of Insider trading (PIT) and access to the Unpublished Sensitive Information (UPTI)

Code of conduct of companies and fair disclosure

Every company should draft its code of conduct and that should be per Schedule-A of PIT Regulations. PIT Regulations set some minimum regulation standards such as equality policy publications related to dividends etc., In the companies which are listed the Board of Directors have to take responsibility of monitoring and reporting the process of trading

Concept of Chinese walls

The company should adopt the Chinese wall policy to protect confidential information. In this policy the people who have continuous access to the confidential information must be separated from the people who deal with the sales and marketing, investing departments, and other such areas. The SEBI should restrict trading if the companies are trading through the client accounts and designate such a list as a grey market/ restricted list. If the company is holding an assignment for the listed company in any other securities with prior information of UPTI can also be restricted. These are restricted under Competition Act, 2002 which is replaced by MRTP Act, 1969. They restrict all the anti-competitive agreements along with abuse of dominance.

Confidentiality under Insolvency law

Under Insolvency and Bankruptcy Code, 2016 Clause 21 of Schedule 1 Prevent the insolvency professional from disclosing the information. However, he has every right to disclose the information whenever required by the law. Along with this, Section 29 (2) also speaks about keeping the information confidential.

Section 29(2) of Insolvency and Bankruptcy Code, 2016 is read as follows:

The resolution professional shall provide the resolution applicant with access to all relevant information in both physical and electronic form, provided that the resolution applicant agrees to (a) comply with current law relating to confidentiality and insider trading; (b) protect any intellectual property of the corporate debtor it may have access to, and (c) abide by the resolution professional's recommendations.¹⁰

VIII. SPRING BOARD THEORY

This concept was first introduced in the *Terrapin v. Builders supply Ltd*¹¹ in this case, was held that a person who has obtained any information which ought to be confidential should not be used in the springboard activities as it is considered a confidential communication. In this, the person who knows the information should not use that information for his gain even after the information was made public. It has been protected a long way and if at all there is leakage of this information to a competitor then the theory of springboard will protect the owner of this information from those who are trying to obtain it from illegal sources.

IX. PRESENT SCENARIO AND THE EVOLUTION OF LAW EXPLAINED THROUGH SUNGRO CASE LAW

Generally, the employers will try to protect the confidential information of the company by entering into confidential agreements with the employees. The general mistake of the companies is they try to fill all the needs with one single template which leads to uncertainties in most cases.

*Sungro Seeds Ltd. v Dr. S.K. Tripathi & Ors.*¹²

In this case, the plaintiff has employed 2 employees who are arrayed as defendants 1 and 2 of this case. The facts of this case include that the plaintiff company has developed a plant variety of Cauliflower and the defendants are the employees working in the same team who had some access to the sensitive information and signed an employment agreement to keep it confidential. The plaintiff has registered the specific plant variety of cauliflower SCFH 130 under the Protection of Plant Variety and Farmer's Rights Act, 2001 for the protection and ownership. During the pendency of this application for the registration, the plaintiff got to know that the

¹⁰ Sec29(2) of Insolvency and bankruptcy code, 2016

¹¹ R.P.C. (1967) p.375

¹² (CS(OS) NO. 1163 of 2013)

Nuziveed seeds Co. has also applied for the registration of a new plant variety of Cauliflower with the same characteristics that were produced because of leakage of information of Plaintiff Company by defendants who are working as employees.

The plaintiff also alleged that defendant no. 3 has taken place in unfair competition by secretly obtaining the wrongful information from the plaintiff company by illegal means. The name of the plant variety developed by the plaintiff is Katreena and whereas the name of the new hybrid developed by the Nuziveed seeds Co. is Riya which was pending registration. The court in this regard held that since the registration is still pending the plaintiff cannot maintain the suit to restrict the defendants. But the court has responded on the part of misappropriation of confidential information by the defendants as.. in its eagerness to safeguard such a claimed right, the Courts would overstep the mandate of the Constitution if they accepted the plaintiff's sweeping presumption that it owns confidential information in something that is manifestly part of the community's material resource.

In this scenario, the court has rejected the suit for lack of cause of action and referred to some of the cases where the action has been taken related to the employment agreements. We should always keep in mind that unlike the intellectual property rights like trade law and patent law the trade secrets and confidential agreements doesn't have any specific law.¹³

In *Niranjan Shankar Golikar v Century Spinning & Manufacturing Co. Ltd.*¹⁴ the court has held that the employee who has access to any special process of work in which employee has acquired the knowledge through training by the employer then it is necessary that the employee should not work in the same kind of company and that restriction is considered as reasonable and just. Later in the case of *Percept D'Mark (India) (P) Ltd. v Zaheer Khan*¹⁵ the Supreme Court held that the period of restraint from the work and its reasonability is difficult to weigh as it is subjective and depends on the facts of the case. However, it was held that any reasonability will not come under the purview of section 27 of the Indian Contract Act as any restriction on trade is void.

Because the plaintiff's rights had not solidified under the PPVFR Act or any other statutorily recognized right in India, the High Court of Delhi in the *Sungro* case found that there could not be a blanket assumption of confidentiality because the plaintiff's rights had not formed under

¹³ *Navigators Logistics Ltd. v Kashif Qureshi* (254 (2018) DLT 307)

¹⁴ (AIR 1967 SC 1098)

¹⁵ (2006) 4 SCC 227)

the PPVFR Act or any other statutorily recognized right in India. Employee agreements require a separate approach under Indian law, based on the results in the Sungro case and consideration of relevant case laws.

Any restriction restricting an employee's right to trade, profession, or business would be void under Section 27 of the Indian Contracts Act, even if the employee agrees to it. As a result, protective clauses should be constructed in light of the Supreme Court's rulings in various cases. Furthermore, any intellectual property that has been registered under the PPVFR Act, Patents, Trademarks, Copyright, or Design regulations cannot be claimed as confidential. The employee agreement should include a distinction between the information that the employer has withheld as secret and the information that has been submitted for registration under any of the above laws.

It is therefore critical to personalize employee agreements in India so that they stay enforceable and do not become a dead letter even though they have been signed and acknowledged by both the employer and the employees.

X. CONCLUSION

In India, it is still a much-heated debate whether to consider the trade secrets and confidential information under intellectual property rights or not as the concept is so perplexed and revolves around the rights and duties of parties. There is no particular statutory law that deals exclusively with these trade secrets and confidential agreements. There is only a judicial approach that is enhanced through various case laws which are purely based on the common law and equity principles. Though there is no solid comprehensive law established till now on this issue but the agreements can be enforceable as same as any other contracts under Indian Contract Act, 1872. As India is developing rapidly at a global level and there is a huge inflow of foreign investments, it is considered as a dire need to fulfil the said lacunae as it boosts the Multi-National Companies (MNC) to increase their investments in India.
