



Intellectual Property ADVISORY ■

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Convolve, Inc. v. Compaq Computer Corp.: Federal Circuit Rules on Trade Secret Protection Loss Due to Noncompliance with Confidential Marking Requirement of NDAs

In *Convolve, Inc. v. Compaq Computer Corp.*, No. 2012-1074, 2013 WL 3285331 (Fed. Cir. July 1, 2013), the Federal Circuit held a trade secret will lose its trade secret protection, at the moment of disclosure, if the disclosing party fails to comply with the confidential marking requirement as set forth in a non-disclosure agreement.

In 1998, Convolve and Compaq entered into a non-disclosure agreement (NDA) prior to entering into licensing negotiations regarding Convolve's disk drive technology (Convolve also signed a similar NDA with Compaq's hard drive supplier, Seagate). The Convolve-Compaq NDA required that disclosed information must be either a) marked as confidential at the time of disclosure or b) unmarked, but treated as confidential at the time of disclosure, and later designated as confidential in a writing. The negotiations broke down and the parties failed to enter into a licensing deal. In July 2000, Convolve alleged Seagate and Compaq infringed certain patents and misappropriated trade secrets when Seagate manufactured drives that were subsequently incorporated into Compaq computers.

During the licensing negotiations, Convolve made a number of oral disclosures to Compaq and Seagate. Following presentations on February 10 and April 7, 1999 (after which Convolve sent the defendants slides and a letter discussing the presentation), Convolve failed to state in writing that the disclosures made during or in connection with such oral presentations were confidential.

Because Convolve failed to follow the NDA protocol requiring a written confirmation that the matters discussed were confidential, the Federal Circuit held Convolve failed to properly preserve trade secret protections and therefore, **lost all trade secret protection at the moment of the disclosure.**

Convolve argued that their failure to comply with the NDA marking procedure only precluded their breach of contract claims, and therefore, Convolve's separate state tort law claims for trade secret misappropriation asserted under the California Uniform Trade Secrets Act (CUTSA) should survive. Convolve argued that

under the CUTSA, trade secrets do not have to be marked as confidential in order to retain their trade secret protection, and therefore, the defendants had a separate duty to maintain confidentiality, regardless of the lack of any markings.

The court disagreed, holding that the NDA expressly set the boundaries of the confidential relationship and it would defy common sense to impose a separate duty of confidentiality under the CUTSA. In essence, the NDA trumped any protections that may have been provided by trade secret law. Therefore, because the disclosed information was within the subject matter of the NDA and because *Convolve* failed to comply with the NDA's marking requirement, **Convolve could not assert that the defendants misappropriated trade secrets under a separate state law tort theory.**

Implications

The Federal Circuit opinion has important implications for those intending to disclose and receive confidential information under NDAs. For parties disclosing trade secrets, these are some important considerations:

- The disclosing party may want to propose an NDA that does not require marking and simply assumes that all non-publicly available information disclosed is to be kept confidential (and, if it is a trade secret under the applicable law, it must be kept confidential for as long as the information is considered a trade secret under that law).
- If there is a marking requirement, the disclosing party should consider strict internal controls to ensure that all materials are marked (or, if disclosed orally, followed up with written designation of confidentiality within the time period designated by the NDA).
- The disclosing party should consider language in the NDA that would cover disclosures erroneously not marked, so that there is a procedure to "correct" the oversight and require confidential treatment of information even after the disclosure without marking.

For the receiving party, there are different considerations:

- The receiving party may want to require that the disclosing party clearly mark all confidential information to provide clarity for the receiving party as to what information needs to be protected and to prevent inadvertent or sloppy disclosures by the receiving party's personnel.
- In order to further reduce uncertainty, if the parties agree not to require marking, the receiving party may want to include a procedure to allow them to request the disclosing party to clarify as to what information is confidential after the disclosures are received.

While NDAs are sometimes treated as boilerplate agreements, *Convolve* highlights the importance of careful NDA drafting. Before parties enter into NDAs, they should also consider their internal controls for ensuring strict compliance with any NDA requirements. Above all, parties must understand that under *Convolve*, the NDA contract will effectively preempt trade secret or other protections that otherwise could apply to the information covered by the agreement.

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