

Entrepreneurs Beware!
Pitfalls in marketing to a former employer's clients

By Panda L. Kroll¹

Entrepreneurs should tread carefully before using their knowledge of their former employer's client addresses, pricing, unique requirements, or other such information. Such knowledge may be considered proprietary and confidential if not outright trade secrets.² Entrepreneurs may be liable for the use of such information, if such use is deemed an unfair business practice and/or wrongful misappropriation of the employer's trade secrets.³

While it is unfair and unlawful for a California employer to seek to enforce an employee's agreement not to *compete*,⁴ no such limitation exists on enforcing an employee's implied or express *confidentiality* agreement. Such agreements may broadly define the employer's trade secret information. Agreements not to use trade secrets to solicit customers (or employees, for that matter) are also generally enforceable. The employer who perceives a competitive threat from former employee-entrepreneurs may threaten or pursue litigation to prevent the continued use of trade secret information and for the recovery of any lost profits allegedly resulting from such use, attorney's fees, and even punitive damages.

Entrepreneurs who are careful not to use their former employer's trade secrets may also limit their liability by contacting their former employer's clients for the limited purpose of informing them of the new enterprise. Such a contact may be permissible even if the entrepreneur is under an obligation restricting him or her from directly "soliciting" such clients.

Factors affecting an entrepreneur's liability include the following:

¹ Ms. Kroll is an associate of Norman, Dowler, Sawyer, Israel, Walker & Barton. Before attending Boston University Law School, she worked in Silicon Valley.

² See Civ. Code §§ 3426 et seq. [Uniform Trade Secrets Act].

³ See *Thompson v. Impaxx, Inc.*, 113 Cal. App. 4th 1425, 1429-30 (2003) [upholding an employer's right to restrict employees from soliciting clients if such clients' identities were trade secrets]; *Courtesy Temporary Service, Inc. v. Camacho* (1990) 222 Cal.App.3d 1278, 1292, [stating that "the cases are legion holding that a former employee's use of confidential information obtained from his former employer to compete with him and to solicit the business of his former employer's customers, is regarded as unfair competition,"]; see also Bus. & Prof. Code § 17200 [prohibiting unfair trade practices].

⁴ See Bus. & Prof. Code § 16600 ["[E]very contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void."] The California Legislature's refusal to enforce most employee non-compete agreements is unusual, and laws interpreting contracts made in other states are often much more favorable to the employer.

1. Does the client information constitute a “trade secret”

Trade secrets are defined in California’s Uniform Trade Secret Act as “information, including a formula, pattern, compilation, program, device, method, technique, or process, that [d]erives independent economic value, actual or potential, from not being generally known to the public or to other persons who can obtain economic value from its disclosure or use.”⁵ Databases or hard copy lists of client addresses, pricing or other unique requirements, although not expressly mentioned in the Act, have been found to constitute trade secrets, especially where the compilation of client information is “not readily ascertainable, but only discoverable with great effort, and the patronage of such customers was secured through the expenditure of considerable time and money.”⁶

Entrepreneurs have less, if any, liability for their competitive use of non-secret client information. For example, the entrepreneur may market to a list of trade association members that is publicly available, even if it contains the same clients that he or she served on behalf of the former employer. Moreover, the former employer will have the burden of showing that it has taken reasonable efforts to protect any so-called “trade secret” information through contract or even a log or similar sign-out system.⁷ An employer who has failed to assert (in an employee handbook if not in a signed employment contract) that specific client information is proprietary, confidential, and a trade secret may not be successful in subsequent efforts to prevent or obtain damages for the competitive use of the information.

What if the client information is gleaned not from a list or database obtained during the former employment, but instead, from the entrepreneur’s memory? A former employee probably may not reconstruct trade secret information from memory,⁸ but the employee’s “general business know-how” is not considered an employer’s proprietary or trade secret information.⁹

⁵ Civ. Code, § 3426.1.

⁶ See *Morlife, Inc. v. Perry* (1997) 56 Cal.App.4th 1514, 1522; see also *American Paper & Packaging Prods., Inc. v. Kirgan* (1986) 183 Cal. App. 3d 1318, 1325; *MAI System Corp. v. Peak Computer Inc.* (9th Cir. 1993) 991 F.2d 511, 521-522.

⁷ See Civ. Code, § 3426.1(d)(2) [limiting the definition of trade secrets to information that is “the subject of efforts that are reasonable under the circumstances to maintain its secrecy”].

⁸ See *Klamath-Orleans Lumber, Inc. v. Miller* (1978) 87 Cal.App.3d 458, 466 [affirming preliminary injunction against former employee who misappropriated confidential customer information by recreating former employee’s customer list from memory and mailing brochures to such customers, where customers’ identities were trade secrets]; *Greenly v. Cooper* (1978) 77 Cal.App.3d 382, 392; *Morlife, supra*, 56 Cal.App.4th at p. 1522.

⁹ See *In re Providian Credit Cards* (2002) 96 Cal.App.4th 292, 309.

An entrepreneur's use of his or her general knowledge of former clients is necessary not only to facilitate beneficial competition in the marketplace, but also to allow him or her to survive after an employment separation. Unless the knowledge can be shown to be an actual trade secret, an entrepreneur may successfully argue that the interest in preventing him or her from using such knowledge is outweighed by the negative effects of restraining trade and limiting the entrepreneur's right to earn a livelihood.

2. Is the intended contact a "solicitation"

If the entrepreneur expressly agrees not to solicit his or her former employer's clients, or if there is an employee handbook in force at the time of employment restricting such solicitation (an implied agreement), the employer may be successful in limiting the entrepreneur from using trade secrets to market to such clients. An entrepreneur may not necessarily circumvent such a restriction merely because he or she had developed personal relationships with certain clients.¹⁰ Even assuming the existence of an express or implied agreement not to solicit, however, nothing prevents an entrepreneur from sending out *announcements* to former clients, and from receiving any resulting business, provided the announcements do not amount to overt *solicitations*.¹¹ Specifically, where bound by an agreement, an entrepreneur may not personally petition, importune and entreat former customers to call him or her for information and for assistance.¹² Where the entrepreneur is under no express or implied obligation, a former employer probably cannot claim damages for even an overt solicitation, provided no trade secrets are violated.

In summary, an entrepreneur should examine all agreements made with his or her former employer(s) as well as employee handbooks in force during the time of employment to ascertain the existence of provisions limiting future use of confidential information and/or solicitation. Contact with former customers should generally be limited to an "announcement" of the new enterprise. Nothing limits a former employee-entrepreneur from doing business with clients who independently contact the entrepreneur or respond to his or her announcement.

\\polydeuces\data\DOCS\PLK\memo05_0208.wpd

¹⁰ See, e.g., *American Credit Indemnity Co. v. Sacks* ("American Credit") (1989) 213 Cal.App.3d 622, 636 ["Providing personal service to a customer whose identity is a trade secret does not thereafter render that customer fair game for solicitation"].

¹¹ Compare *Moss, Adams & Co. v. Shilling* (1986) 179 Cal. App. 3d 124, 130 ["Merely informing customers of one's former employer of a change of employment, without more, is not solicitation"] with *American Credit, supra* at pp. 630-633 [finding a solicitation where former employee informed former employer's customers of the "interesting competitive alternative" offered by her new employer, and inviting their inquiry about these new options when they were ready to repurchase].

¹² *American Credit, supra*, 213 Cal.App.3d at 633.