Non-Disclosure Agreements

Why Confidentiality Agreements (or NDAs) are important if you want to protect confidential or sensitive information

Expert knowledge means success

Contents

1. Introduction
1. The Basics of a Non-Disclosure Agreement
2. Structure of an NDA
2. Conclusion
3. Further Information

Note: This publication has not been updated since it was last published. Some of the hyperlinks may have changed and may need updating. In addition, some of the information in this publication may be out of date.

Introduction

Sooner or later, an entrepreneur may have to disclose his/her ideas to a third party in order to obtain finance for development or help in commercially exploit them. But, without adequate legal protection, when you tell someone else about your ideas, you run the risk of losing those ideas and seeing them being exploited by others.

Designed to prevent outside use or disclosure of confidential information shared between parties as they explore or enter into a business relationship, non-disclosure agreements, or "NDAs," are often executed early in a business relationship.

The need for these agreements in corporate finance transactions is well understood. Investment banks and other advisers often require confidentiality agreements before they will circulate information (usually of a commercially sensitive nature) about a transaction to potentially interested parties. Such agreements are designed to protect the information provider by regulating or prohibiting disclosure and use of the information regarded as sensitive.

Although common, confidentiality agreements are often subject to strenuous and time-consuming negotiation by the parties concerned. Given the common market practices associated with dealing with confidential and commercially sensitive information, the small changes in wording which may be achieved through negotiation tend to lead to minimal benefit in practical terms.

A confidentiality or non-disclosure agreement is crucial for an inventor or any other party who needs to protect confidential information. As the importance of the confidential information increases, so does the relative complexity of the Agreement.

The Basics of a Non-Disclosure Agreement

A non-disclosure agreement is used when your otherwise unprotected idea is to be shown to a third party and you want the information you share with them to remain undisclosed to other parties. You ask the other party to agree two things:

1. That they will not disclose any information about your idea, except as may be allowed in the agreement with you; and
2. That they will not compete with you by producing or selling your idea.

NDAs are perhaps the lowest cost of protection for an invention or new business idea. Often a simple agreement can be obtained for little to no cost.

NDAs provide broader protection than patents, which is a reason justifying simultaneous use of NDAs and patent applications.

It is obviously safest to use an NDA with those people of known high integrity. One, evaluating the benefits and risks of NDAs, should keep squarely in their mind whether ultimate protection may include a patent. NDAs on their own are very risky for protecting an invention. Problems with a flaw in the signing process, unexpected impact of law, inadvertent mistakes by the discloser or disclosee could affect the prospects of obtaining a patent.

Why use an NDA?

Once you have told anyone in public about your idea, the chances of being able to patent it are slim. An NDA keeps your ideas “private” and, since the receiving party is obliged to observe confidentiality, there is no public awareness about them – this means that, when the time is right, you can apply for a patent to secure protection under the law.

If you do take out a patent and accompanying Intellectual Property insurance, remember that your insurer should also sign a non-disclosure agreement.

NDAs – what are they?

A non-disclosure agreement (NDA) is an essential tool when trying to protect sensitive business information or valuable intellectual property. Usually, NDAs are one-way agreements whereby the recipient of defined information agrees not to make any disclosure to anyone else (other than professional advisors) certain information, except under terms as described in the agreement.

NDAs can also be two-way allowing both parties to exchange information and ideas to a common goal.

NDAs differ depending on the nature and scope of the disclosure and the value of the trade secret. However, all NDAs should include:

- A good description of the trade secret or sensitive information;
- Permissible uses of the secret material and information;
- A duty of confidentiality;
- A remedy for non-compliance with the agreement (including injunctive relief); and
- The term of the agreement (which may last indefinitely or for a specific period of time).

How effective is it?

A non-disclosure agreement is as good as the word of the person with whom you share the information. Although you do have the legal right to enforce your NDA, legal disputes can be costly and take a long time to resolve. If you are proposing to talk with a person or company that you don't know very well, ask to talk to other people they've worked with in confidential situations before you tell them about your idea.

Refusals to sign NDAs

Many organisations and investors refuse to sign NDAs as a matter of policy. It is not unusual for this to happen. This is because many new ideas are similar to concepts they have already seen and companies may already have something in development that's close to your idea.

When a company you want to deal with refuses to sign an NDA this is very tricky ground. You need to look at them carefully:

- Could they have something similar?
- Could one of the companies they've invested in be developing something to compete with your idea?

Structure of an NDA

The broad structure of an NDA is usually as follows:

- Definition - The most important part of the confidentiality agreement is the definition of what is "Confidential Information". Although the NDA should specify the scope of information covered by the agreement, the disclosing party may be reluctant to describe the information in the contract, for fear that some of the confidential information might be revealed in the contract itself;
- Purpose - confidential information should only be revealed to another party for a specific purpose. The agreement should say what the purpose is;
- No Other Use - some NDAs omit this important element. The Discloser wants to make sure the Recipient doesn't use the disclosed information for any purpose other than that as specified in the agreement;
- No Disclosure - the recipient must agree not to disclose the information to third parties. The extent of this provision to a large extent controls the effectiveness of the NDA;
- Exclusions -most NDAs put a limit on the type of information that is deemed as being confidential, such as:
  - The Recipient already knew the information before it was revealed by the Discloser;
  - The information was revealed to the Recipient by a third party, information that becomes publicly known;
  - Information that is requested by order of a government agency or other legislative authority;
  - Information that is independently developed;
- Term - the term must be long enough to protect the interests of the Disclosing party but should not be unduly burdensome on the Recipient.

Other provisions that are commonly found in confidentiality agreements include:

- Allowing the remainder of an agreement to stay in effect even if a part of the agreement is found to be unenforceable;
- The agreement is binding on heirs and assigns;
- Return of confidential materials after use by Recipient;
- Giving the Discloser the right to receive an injunction from a court if the agreement is breached;
- How disputes are to be resolved; and
- A provision governing the controlling law for the contract.

Conclusion

Low cost and broad protection make the NDA a valuable tool in appropriate circumstances. An NDA should always be used to protect trade secrets but has limited value as the risks increase for protecting patentable subject matter.

We can provide outline non-disclosure agreements but their use is no substitute for obtaining appropriate professional advice.

Key NDA terms

Certain terms are likely to crop up in non-disclosure agreements. It is a good idea to understand these terms and their definitions:

- Confidentiality
  a legal principle that maintains secrecy between parties.
- Owner or discloser
  the name of the person, organisation or business disclosing the information.
- Recipient
  the name of the person, organisation or business that is receiving the information and that is responsible for ensuring its confidentiality.
- Statement of reasons
  a short paragraph defining the context in which the information will be disclosed and why the parties want to make the information the subject of a contract.
- Subject
  the information and documents that will be the subject of the confidentiality agreement.
- Penalty clause
  this is an optional way of fixing an amount of compensation that the owner or discloser is paid if the recipient breaches the agreement.
- Confidentiality clause
  this is an optional clause that requires both parties to keep the existence of the confidentiality agreement a secret.
- Term of agreement
  how long the obligations of the contract last for.

Further Information

This guide is for general interest - it is always essential to take advice on specific issues. We believe that the facts are correct as at the date of publication, but there may be certain errors and omissions for which we cannot be responsible.

The UK Intellectual Property Office provides information about confidentiality and non-disclosure agreements including a sample agreement at:
www.ipo.gov.uk/patent/info/cda.pdf

The IPR-Helpdesk is a project of the European Commission DG Enterprise, co-financed with the fifth framework programme of the European Community.
www.ipr-helpdesk.org/

Important Notice

Publication issued or updated on:
1 February 2012

Ref: 615