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## Security and Protection of Information in Commercial Law Relationships

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## **Security and Protection of Information in Commercial Law Relationships**

### **Abstract:**

*The article addresses the protection of information in relationships that are entered in pursuant to commercial law and are expressed in the concepts of trade secrets, confidential information and an independent obligation to preserve confidentiality. The author points to differences between these concepts in theoretical and practical terms alike. He finds the basis for his reasoning in pertinent case law and in drawing comparisons between previous and current court opinions vis-a-vis disputes involving the enforcement of rights to the protection of information.*

**Key words:** *Trade secret, Confidential information, Obligation to preserve confidentiality, Commercial Code*

Legislative developments in commercial law take account of the fact that selected concepts in commercial law are governed by mandatory provisions with clear-cut applications both in theory and practice. On the other hand, the law provides for an appropriate measure of freedom of contract when it comes to concepts whose importance must be assessed by each party to a contract on an independent basis. Issues that are governed by legislation will in reality be dealing more with the creativity of companies in drafting contracts than with the positive law. Included is the security and the protection of information in relationships governed by commercial law, that is facts which must be protected between business associates and shareholders, as well as with respect to company employees, including information revealed during negotiations with the potential parties of a contract.

The crux of the security and protection of information within Slovakia's body of laws is addressed primarily in the Commercial Code (Act no.

513/1991 Coll. as ammended). This code essentially makes a distinction between three contract concepts that are not merely an empty gesture of legislation. Instead, they are actual tools that may be employed in their original form as set forth in the law or in an „enhanced” form in contracts. These three concepts are the trade secrets, confidential information and the obligation to preserve confidentiality. The aforementioned areas will be interpreted in this article in gradual fashion - as autonomous instruments as well as contributing options conducive towards the simultaneous protection of internal facts - but I will also provide a brief interpretation of how to ensure compliance with obligations that arise from such provisions.

A trade secret is the most characteristic contract concept that is presumed to demonstrate the greatest degree of effectiveness in ensuring the security and protection of information. Despite the fact that its essence is comparatively straightforward, it is prone to frequent misinterpretation by the business sector, with one-off and relatively simple contracts proving to be no exception to this. Such a state of affairs is partly due to the fact that the respective legislation has not been in effect for long and that it was not until recently that the Commercial Code completed the second decade of its existence. In much of its wording, the Code draws inspiration from German and Austrian commercial law, but the generally accepted method of its practical application and subsequent case law could not come into being until after the parties concerned had used the Code for a certain period of time. What naturally, albeit not correctly, followed was a tendency to protect almost any information in relationships in commercial law via the concept of the trade secret. With this in mind, I will provide an interpretation of a trade secret in accordance with how it should be addressed in contracts so as to warrant recognition of a trade secret in the event of a lawsuit.

Items that are often misinterpreted include the scope of information that may be subsumed under the term ‘trade secret’. The business sector and employers have for a long time been susceptible to the illusion that a contract is sufficient for a trade secret to be created. In contract drafting, this assumption has tended to translate into the so-called ‘general clause’ stipulating that

any and all facts contained in the contract concerned will be deemed a trade secret by the parties to the contract. Consequently, this led to what was only presumed to be protection of highly commonplace information such as the names of the parties to a contract, information on companies' statutory bodies, the names of individual contracts, etc. Entrepreneurs acting in this way went on to lose practically all lawsuits in which they sought to pursue what they viewed as damages arising from the fact that their contracting partners had used for their benefit, or had made accessible to third parties, information contained in the contracts concerned. Ever since such lawsuits first appeared, the courts have been correct in their opinions, that is they have not endorsed the use of trade secrets for the protection of any information, but only for information that complied with legal requirements. A Supreme Court ruling dating back to 1999 was a breakthrough in this respect, as the court ruled that *„the agreement of parties to a contract that certain items contained in a contract are the subject of a trade secret does not suffice for such facts to become a trade secret unless they comply with characteristics set forth in Section 17 of the Commercial Code,,<sup>1</sup>*. As a result, businesses had to focus on the interpretation of a provision contained in Section 17 of the Commercial Code, including all its particulars, which gave rise to perceptions of a trade secret as more of a restrictive rather than a welcome concept. Not only courts, but also periodical specialized literature contributed to a more accurate interpretation, which, however, continued to take more into consideration the superficial use of a trade secret while disregarding specific features pertinent to companies and the requirements of employers. For the sake of a more comprehensive interpretation, I will list selected arguments.

<sup>1</sup> A ruling by the Supreme Court of the Slovak Republic, as contained in reference file no. 5 Obo 98/99: *„The concept 'business secrets' as set forth in Section 17 of the Commercial Code is defined as the subject of an entrepreneur's rights, i.e. intangible protected property to which the owner possesses absolute property rights that apply with respect to everyone else. Other unprotected intangible assets are eligible to become the subject of a business secret only if they meet the conditions defined in Section 17 of the Commercial Code. Not all information that is to be kept confidential can be deemed a business secret; instead, only information that unequivocally meets the conditions defined in Section 17 of the Commercial Code. This is what renders a business secret different from confidential information and facts, the disclosure of which may incur damages to the company”*.

First, it is worth indicating that the first sentence contained in Section 17 of the Commercial Code is of surprisingly little effect in practical application, as it only generally defines facts that can come under a trade secret: the law stipulates that this may include *"all the facts of trading, manufacturing and technological nature related to the enterprise"*. It is not difficult, however, to comply with this wording, as in a competitive environment every fact is considered to be a piece of manufacturing, technological or – in the most general sense – trading information. When it comes to lawsuits, therefore, it is necessary to fulfill additional requirements that will be subject to examination and the procedure of taking of evidence will take place. As a consequence, before a fact enjoys protection as a trade secret it must meet all of these characteristics:

- it has actual, or at least potential, tangible or intangible value,
- it is not normally available in the respective industry,
- the entrepreneur wishes that the same are not disclosed,
- the entrepreneur adequately provides for the confidentiality thereof.

Pursuant to (a), it must have real entrepreneurial substance whose current or at least potential value will constitute means to achieve a profit. This feature lies at the core of a trade secret as such, as entrepreneurs have often tended to protect facts of little substance, which has led to the so-called „coercive law enforcement“. This used to occur commonly when, by way of example, one party to a contract would sue its contracting partner demanding a contractual penalty (often higher than usual) for disclosing an unimportant piece of information or information in the public domain. The requirement for momentary or at least potential profit has narrowed down the scope of such a provision to facts that are of tangible entrepreneurial and thus economic value.

The requirement that information should not be normally available (b) does not mean that the respective information is absolutely unique; instead, it is a condition for such information not to be generally well known. If, for instance, a baker considered „his“ recipe for bread rolls to be a trade secret, the Commercial Code would not provide him with legal protection, as such

a recipe has been well known for a long time – on the other hand, if it concerned a novel or otherwise extraordinary recipe with special ingredients and a specific taste, it could indeed constitute a trade secret provided that the requirement of it not being normally available and other characteristics were met. In this connection, it is worth noting that there has been a tendency recently to view ‘information not normally available’ as information that cannot be found using internet browsers, but according to the law this is not the primary determining factor: for example, even though a piece of information about an innovative chemical composition of a type of washing powder may not be found on the internet, most experts working in this field may view this information as generally well known. Such a state of affairs prevents one from using a trade secret for the purpose of protecting the composition of the washing powder concerned – as it is not the „unavailability” of information among the target group of the product that is decisive; rather, it is its lack of availability among „relevant circles of experts” that deal with the production and distribution of the goods concerned. In other words, specialists, not customers, are decisive in this regard, as when it comes to an assessment of the interpreted requirements, customers are viewed as laypeople in terms of both the law and technology.

The third and fourth conditions for protecting a specific piece of information via the concept of a trade secret overlap to some extent. One of the conditions is that a given entrepreneur is required to demonstrate to the relevant people (as a rule, this concerns business associates as well as employees who will handle this information while carrying out their work) the will to ensure that the piece of information concerned is to be deemed a trade secret. This assumption is related to the previous condition, which lies in the subsequent actual protection of such information (a safe, alarm unit, software protection, etc. dependent on the nature of the information under protection). A number of civil lawsuits have been unsuccessful due to the fact that the security measures of the entrepreneur concerned vis-a-vis internal information were insufficient, or alternatively the people concerned were not advised of the intention to protect the information in such a manner. This is especially the case with, for example, general meetings

of companies that, aside from the presentation of other information, also feature presentations of the entity's strategy for the foreseeable future, plans for external marketing operations, proposed volumes of public procurements with the company's potential involvement and related pricing, etc. A company's failure to make its intention to protect such information as a trade secret sufficiently clear and its failure to issue a respective instruction to adhere to the obligation to preserve confidentiality (as a rule, via a statement of an enterprise's associates on adherence to such an obligation) will render it impossible to fulfill the requirement concerned and a trade secret as such. On the other hand, if a company did manifest such an intention and associates did commit themselves to adhering to the obligation of preserving confidentiality, the information concerned might be used by another person possessing access to such information (e. g. a person with the keys to the conference room or associates of a different company holding negotiations in the same room after a general meeting, etc.). The trade secret would not be applied vis-a-vis such persons, as they were not advised of the intention to protect the information concerned and, moreover, the necessary degree of actual protection of such information was not attained, e.g. by collecting the reports distributed at the general meeting and placing them in a locked room or otherwise secure space.

Another essential feature of a trade secret lies in the fact that its protection is not pre-conditioned by an entry in any state registry – the entrepreneur is thereby free from the danger that anybody outside of the company may have access to confidential information, as even protected information in such registries may be consulted by a number of people who may misuse information laid out in such a manner. There are other ways to protect a trade secret: be it via provisions of the Commercial Code or through, for example, employment contracts with employees that impose on them the obligation to preserve the confidentiality of information which falls under the trade secret. It needs to be noted again, however, that this may only concern information that meets all requirements set out in Section 17 of the Commercial Code.

As the full use of a trade secret is pre-conditioned by meeting the aforementioned conditions, which makes it somewhat of a rigid instrument, „con-

fidential information” is viewed as a considerably more flexible concept. A surprisingly more extensive description of confidential information is needed in order to provide an appropriate interpretation of this concept and, compared to a trade secret, it is based on completely different assumptions. Confidential information is governed by Section 271 of the Commercial Code, while this provision is not primarily aimed at providing an accurate definition of protected information but instead stipulates the circumstances under which it is well advised to protect such information. The aforementioned provision is aimed at creating pre-contractual certainty for entities that have entered into pre-contractual negotiations with the knowledge that the contracts under negotiation may not necessarily be concluded in the end. As parties interested in concluding the respective contract will, in an effort to persuade their contracting partner, also have to present internal information about, for example, their suppliers, pricing policy, technological processes, etc., they need to possess appropriate guarantees that their future contracting partner will not exploit such information for its own benefit or for the benefit of another entity, particularly in cases in which negotiations on the conclusion of a respective contract are unsuccessful. In such cases, the Commercial Code allows for the conclusion of an agreement whereby the negotiating parties commit themselves to deeming all information presented during pre-contractual negotiations confidential with their potential disclosure penalised by a contractual fine, entitlement to compensation or a combination thereof. The arrangement involving the protection of information presented during pre-contractual negotiations loses its effect over time, because the availability of information about, by way of example, foreign suppliers is substantially greater nowadays than was previously the case. Considering the currently limitless internet-based communication and information platforms, it is now more difficult than ever to prove the misuse of past information. A vast number of lawsuits end unsuccessfully for the entitled party on account of its inability to deal with the burden of proof effectively, i.e. it is unable to prove that the defendant was in possession of the respective information exclusively from the plaintiff and could not have obtained it in any other manner. Naturally, the



defendant defends himself by claiming that the initially protected information came gradually into his possession from other sources in the public domain or alternatively from other contracting parties. The party demanding the protection of information presented in pre-contractual negotiations tends to lose its chances of winning the lawsuit at this stage. As the stated arguments point to certain legislative flaws in Section 271 of the Commercial Code, it is well advised to make use of what continues to endure successfully in the provision concerned and demonstrates a robust ability to endure even in harsh practical application. This equates to a requirement needed in order for confidential information to come into being – unlike a trade secret, it is possible to view anything that parties to a contract agree on as confidential information. The law does not require that any other particulars are met, i.e. it may concern a piece of information that is generally available, has no tangible economic value and may not have special protection. As indicated above, thanks to this very feature confidential information is becoming a flexible tool for protecting any information that is to remain the subject-matter of internal communication between the parties of a contract. The scope of a trade secret is not so broad, as confidential information is more extensive in its application. This means that the final provisions of any contract may contain a general provision whereby all facts included in the contract become confidential information - and for an indefinite term. The factor of the passage of time is a positive aspect of confidential information, as a given trade secret remains in effect only while all legal requirements are observed. As a result, a number of trade secrets have lost their legal protection after several years, but this danger is not imminent in the case of confidential information.

The use of freedom of contract for creating the concept for preserving confidentiality constitutes another option for protecting information in relationships concluded pursuant to commercial law. This obligation is fully in conformity with the law, and this is the case not only thanks to the private-law principle of *„everything that is not forbidden is allowed“*, but also thanks to the inclusion of this obligation in a specific type of contract – the business agency contract. Section 657 of the Commercial Code sets out the legal ob-

ligation of the business agent to preserve the confidentiality of all facts, of which the disclosure would be at variance with the interests of the principal. As is the case with confidential information, the primary legal arrangement of this concept is weakened by actual application among entrepreneurs, as on one hand the Commercial Code itself demonstrates efforts to protect one of the parties to a contract, but on the other it ushers in an undesirable subjective element into the business agent's decision-making process as to which information should come under the obligation of confidentiality (and which should not). That is why in practical application this state of affairs is remedied by the enumeration of facts in the contract that will be deemed internal and must not be made available to third parties without the prior consent of the contracting partner. While the reviewed Section 657 of the Commercial Code provides for an imperfect platform, this can be modified via a contract in a positive manner. Such an enhanced platform has not been, for a long time, the domain of business agency contracts only; instead, it is a standard part of most contracts concluded pursuant to commercial law. As is the case with confidential information, the obligation to preserve confidentiality is not pre-conditioned by compliance with any special attributes or other requirements associated with such information.

The definition of the protection of internal information using any of the aforementioned concepts does not by itself guarantee the smooth performance of the contract concerned. The psychological effect of pecuniary penalties, which are usually subsumed under the so-called contractual fine, is another appropriate element of properly-worded contract clauses. Various modifications of the contractual fine are included in almost every contract concluded pursuant to commercial law. Under the current legal state of affairs as well as established case law, such a pecuniary penalty must be proportionate to the value of the obligation that is provided for by the contractual fine. Adherence to this rule is free from problems in, for example, contracts of sale<sup>2</sup> or works contracts, as in such cases the level of the contractual fine is based on the

<sup>2</sup> See also: Dulaková, D., Dulak, A., Jurčová, M.: *Contracts on Ownership Transfer. Contract of Sale and Contract of Exchange, Consumer Purchase Contract. Consumer Sales Contract, Contract on Donation. A Commentary.* C. H. Beck, Praha, 2011

purchasing price or the price of carrying out the work, respectively<sup>3</sup>, but it is not a simple matter to determine the „value” of the commitment of parties to a contract to preserve confidentiality. Cases in which the commitment of confidentiality is priced much higher than, for instance, delays in the supply of goods or a party’s failure to adhere to previously-agreed quality standards are a common occurrence in practical application. The Commercial Code lacks provisions governing such situations, hence the opinions of individual courts become decisive. In their assessment of the level of contractual fines vis-à-vis infringed confidentiality commitments, the courts concerned address the extent of damage that could have been incurred through the breach of confidentiality, while this does not necessarily concern financial damages but also threats to the reputation and name of the party that demands such protection. It is impossible, however, to provide accurate calculations of an appropriate level for the contractual fine with a view to protecting internal information. The fact that a contract that is not worded in a professional manner may nullify a compensation claim in its entirety constitutes just as problematic an element in the correlation between a contractual fine and a compensation claim. This is due to the subsidiary application of provisions of the Civil Code (Act no. 40/1964 Coll. as amended) which stipulate that if a breach of any contract obligation results in a pecuniary sanction (a contractual fine), the injured party must settle for the contractual fine agreed while losing its compensation claim. This legal assumption may only be altered by an agreement between the contracting parties whereby the injured party to the contract will have its compensation claim preserved in its entirety alongside the contractual fine.

The aforementioned legislation for the concepts concerned translates in practice into a compound of all options for protecting the internal information of companies through a network of contractual relationships concluded between the company and members of its statutory bodies, members of the supervisory board, business associates, employees as well as potential con-

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<sup>3</sup> See also: Klee, L.: *Determining the Price in the Works Contract for a Construction Project*. *Obchodněprávní revue*. C. H. Beck, Praha, 2011

<sup>4</sup> See also: Majdiš, M.: *On the Deficiencies of the Works Contract*. *Justičná revue*. Bratislava, 2010, no. 10, pp. 1099-1107

tracting partners entering into business negotiations. However, absolute legal certainty is unattainable in such cases, particularly if even the most foresighted of contracts turns out to be inadequate in situations when one of its contracting partners lacks even the most fundamental propriety in business relationships.

## **Literature:**

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