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TRADE SECRETS PROTECTION IN INDIA: EVALUATING NON-COMPETE AGREEMENTS AND LEGAL CHALLENGES

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Abstract

Trade secrets are a vital part of intellectual property, helping businesses safeguard confidential information that provides a competitive advantage. In India, their legal protection is primarily based on the Indian Contract Act, 1872, and common law principles of equity and confidentiality. Non-compete agreements, though enforceable if reasonable in scope and duration, are closely scrutinized by courts to prevent undue restrictions on trade and employment. However, these agreements alone are insufficient to protect trade secrets, particularly in cases without a contractual relationship. Key challenges include difficulty in securing damages and inadequate procedural safeguards against disclosure in litigation. To strengthen trade secret protection, businesses should implement confidentiality agreements, restrict access, and enhance security measures. This paper explores these concerns in light of existing Indian jurisprudence.

Key Words– confidentiality, non-compete agreements, enforceability, common law, equity, contractual relationship, litigation challenges.

Introduction

The World Intellectual Property Organization (WIPO) defines trade secrets as, "intellectual property rights over confidential information that can be sold or licensed."¹⁵¹ In layman's terms, a trade secret is a trade or business secret that is known only to a small number of people and has commercial value. For example, consider the recipe for Coca-Cola beverages. Following the liberalisation in 1991, India joined the World Trade Organisation (WTO), and in 1994, it signed the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). The TRIPS Agreement required all member states to protect trade secrets/undisclosed information in accordance with Article 39. There was no specific law enacted in India to protect trade secrets and confidential information, and

there still isn't one. It is based on both equity and common law.

What are Trade secrets?

A **trade secret** is any confidential business information that provides a company with a competitive advantage and is not generally known to the public. It includes formulas, processes, designs, methods, or any proprietary knowledge that derives value from its secrecy.

World Trade Organization (WTO) – TRIPS Agreement (Article 39.2):

"Natural and legal persons shall have the possibility of preventing information lawfully within their control from being disclosed to, acquired by, or used by others without their consent in a manner contrary to honest commercial practices, so long as such information:

(a) is secret, in the sense that it is not generally known among or readily accessible to persons

¹⁵¹ World Intellectual Property Organization, "Trade Secrets: Frequently Asked Questions", WIPO, available at https://www.wipo.int/trademarks/en/trademarks_faqs.html (last visited on Feb. 5, 2025).



within the circles that normally deal with such information;

(b) has commercial value because it is secret; and

(c) has been subject to reasonable steps to keep it secret by the person lawfully in control of the information.”

A trade secret is a valuable business information that is not generally known and is generally subject to reasonable efforts to preserve confidentiality. These are information that companies keep secret to give them advantage over the competitors. Examples of trade secret include customer's identities, preferences, vendors, product pricing, marketing strategies, finances, manufacturing processes, and other competitively valuable information.

Essentials of a Trade Secret:

- It should have commercial value.
- It is only known by a select group of people.
- Reasonable steps should be taken by the owner to keep the information private.

Non-compete clause in Agreements

Non-Compete Clauses are a common part of employment agreements, particularly with senior executives. They are also a common part of mergers and acquisitions (M&A) deals. In a non-compete agreement, founders or key executives leaving the business are subject to certain restrictions. A non-compete clause requires a person to agree not to start a new business or take up employment, or to engage in any way with another competing entity. These restrictions are typically limited by a period and by geography, meaning that the person will not be allowed to work in a competing business for a certain period of time within the defined geographical area. The reason why senior executives are bound by non-compete clauses is that they may have access to sensitive and proprietary information and intellectual property related to the company that they may use during the service

to a competing entity, which may result in an unfair business advantage for the acquirer. Similarly, in an M&A deal, if exiting founders begin or join a competing entity, the value of the deal becomes compromised and it results in the loss of a competitive advantage.

And after losing valuable information and several employees to competitors, employers all over the world require their employees to sign a 'non-compete agreement'. A non-compete agreement is an agreement between the employer and employee restraining the latter to work with the competitor of the former employer. This agreement restricts the employee to divulge any trade secret of the former employer. Therefore, it can be stated that non-compete agreements is the most widely used mechanism to prevent the divulgence of a trade secret by an employee or ex-employee of a particular company. This agreement takes the form of a restrictive covenant. Other restrictive agreements include non-solicit agreement, non-disclosure agreements, and confidentiality covenants. Definition of confidential information, exclusions from confidential information, and obligations of receiving party, time periods, and miscellaneous provisions are few of the important elements which exist in a restrictive covenant such as a non-compete agreement for the protection of trade secrets of a company. The essential question to be answered here is, when an employee who has had access to your key information and trade secrets walks out your door and into the door of your competitor, is it better to have an agreement restraining him from disclosing information to your competitor or is trade secret law adequate to protect the former employer.

Covenants such as non-compete agreements are contractual in nature. Valid covenants not to compete may prevent a former employee from working for a competitor, seeking out clients or copying ones products for a specified time and geographic region. Trade secrets protection on the other hand, need not have a time period specified. In some instances, the



former employee does not even have to disclose the trade secret but merely be in a position where 'inevitable disclosure' of the trade secret could occur.

A number of legal experts and jurists favor the trade secret law system over the idea of restraining agreements. As will be mentioned later, it is important to remember that the majority of instances involving trade secret disclosure have only been adjudicated on the basis of an employer-employee contract violation.

CRITERIA FOR CHOOSING BETWEEN PATENTS VS TRADE SECRETS.

When deciding how to protect IP, businesses must evaluate many factors to determine whether to choose patents or trade secrets. Among the key considerations are:

Is the knowledge patentable because it meets the requirements of originality, non-obviousness, and usefulness? If not patentable, trade secrets may be the sole alternative.

A. Term of Protection – Patents are valid for 20 years from the date of filing. On the other hand, trade secrets might theoretically endure indefinitely if kept secret. This makes trade secrets more suited to securing continued improvements.

B. Enforcement – Patents involve proving infringement in court, which may be difficult and costly. Whereas trade secret theft is based on circumstantial evidence. Enforcing multinational patents is likewise quite difficult.

C. Injunctions – After 2006, injunctions for patent infringement became discretionary, reducing deterrence. Trade secret injunctions confront similar international restrictions.

D. Disclosure – Patents divulge information when granted, giving rivals with insights. Trade secrets mitigate this disclosure risk at the expense of continuous confidentiality obligations.

E. Costs – Procuring patents is often far more expensive than establishing trade secret processes such as NDAs (non-disclosure agreements) and security measures.

Weighing these essential variables, may assist businesses in determining the best type of IP protection for any particular situation. Patents and trade secrets both play crucial roles in different situations.

Reasonableness of non-compete agreement clause in employment

The employer's ability to use non-compete restraints in this way is not unlimited. The employee cannot be restrained entirely from working for competitors of the employer, only from working in a role that involves competition with the employer's business and to which the confidential information is relevant.¹⁵²

The golden rules created by judicial pronouncement for protection of weaker party are also applied in the non-compete agreement.

The rule that says 'terms should be reasonable' was created in the case of *Central Inland Water Transport Corporation Vs. Vrajana*¹⁵³ the rule says that the terms in the contract should not be in favour of one party of the contract and they should provide equal protection to both the parties to the contract.

Legal position in India

As per section 27 of Indian Contract Act, 1872 "An agreement by which a person is prohibited from engaging in a legitimate profession, trade or business is void to the extent that it falls within the narrow exception provided for by the law."¹⁵⁴ The fundamental principle underlying this provision is that a person has the right to engage in his legitimate trade or calling whenever he pleases and that the law protects the freedom of contract from any interference with trade. But there is exception to this clause that "One who sells the good-will of a business may agree with the buyer to refrain from carrying on a similar business, within specified local limits, so long as the buyer, or any person deriving title to the good-will from him, carries on a like business therein, provided that such

¹⁵² Cadgroup Austl. Pty Ltd v. Snowball, [2016] NSWSC 22 (Austl.).

¹⁵³ Cent. Inland Water Transp. Corp. v. Brojo Nath Ganguly, (1986) 3 S.C.C. 156 (India).

¹⁵⁴ Indian Contract Act, § 27, No. 9 of 1872, India Code (1872).



limits appear to the Court reasonable, regard being had to the nature of the business.”¹⁵⁵

If the business is dependent upon the goodwill and the proprietor or owner of the business has worked hard for the goodwill then the person who took efforts to create brand value of the business is entitled for the fruits of his hard work.

TRIPS Mandate

Article 39 of the TRIPS Agreement requires member states to protect undisclosed information (trade secrets) in pursuance of Article 10 of the Paris Convention, 1967. ‘Undisclosed information’ is one of the categories of intellectual property as defined in Article 1(2) of TRIPS. The obligation established under Article 39(1) is limited to the protection of undisclosed information against unfair competition as provided in Article 10 of the Paris Convention. The act of unfair competition may be defined as: “any act that a competitor or another market participant undertakes with the intention of directly exploiting another person’s industrial or commercial achievements for his own business purposes without substantially departing from the original achievement.”

Inadequacy of Trade Secret Law in India

In India, protection of trade secrets is largely common law based. The law relies on common law principles such as breach of trust and breach of confidence. The only statutory provision governing trade secrets law is Section 27 of the Indian Contract Act, which states that “every agreement by which a person is restrained from carrying on any trade, business or profession, is invalid.”¹⁵⁶ This provision brings within its ambit non-disclosure and non-compete agreements, which are indispensable for the protection of trade secrets. Other avenues where the law on trade secrets may be located include the Securities Exchange Board of India (Prohibition of Insider Trading) Regulations, 1992, which renders the use and disclosure of confidential (undisclosed) information by an insider subject to prosecution

under the Securities Exchange Board of India Act. This clearly underlines the need for a comprehensive legislation on trade secrets, in compliance with Article 39 of TRIPS. A brief discussion on the law regarding trade secrets in other member countries will further elucidate this point.

Implied contract – no need for contract to protect trade secrets

The requirement of contract for non-disclosure was not required. *Tipping v Clarke*¹⁵⁷ it was held that everyone employed is under an implied contract that he will not make public that which he learns in the execution of his duty as an employee. This duty is further pronounced in view of the later judgment in *Sanders v Parry*¹⁵⁸ which held that there was an implied duty upon an employee to serve his master (employer) with good faith and fidelity.

Springboard Doctrine

In *Saltman Engineering v Campbell Engineering*¹⁵⁹, the expression ‘consent’ was used for the first time and it was held that if a defendant is proved to have used confidential information, directly or indirectly obtained from the plaintiff, without the consent, express or implied of the plaintiff, he would be guilty of an infringement of the plaintiff’s right. Subsequently, this very principle was given the name of ‘springboard doctrine’ and was held that the person cannot be allowed to use the information as a springboard for activities detrimental to the person who made the confidential communication.” However, in *Peter Pan Manufacturing Co v Corsets Silhouette*¹⁶⁰ it was held that if the defendant has only knowledge of and has not wrongly used the information before it became public then the doctrine does not apply to him and he is subject to no special restraint. Finally, in *Saltman v Campbell*, the very basis of the development of the law of trade secrets was enunciated and it was said that the law depends on broad

¹⁵⁵ *Id.*

¹⁵⁶ Indian Contract Act, § 27, No. 9 of 1872.

¹⁵⁷ *Tipping v. Clarke*, (1835) 67 Eng. Rep. 157 (K.B.).

¹⁵⁸ *Sanders v. Parry*, [1967] 1 W.L.R. 753 (Eng.).

¹⁵⁹ *Saltman Eng’g Co. v. Campbell Eng’g Co.*, [1963] 3 All E.R. 413 (Eng.).

¹⁶⁰ *Peter Pan Mfg. Co. v. Corsets Silhouette Ltd.*, [1964] 1 W.L.R. 96 (Eng.).



principles of equity and that he who has obtained information in confidence shall not take unfair advantage of it. But, subsequently it was realized that there could not be universal applicability of this principle and importance of contract was emphasized.

Indian Law

At the very outset, it is submitted that not enough direct Indian case law has surfaced on the issue of trade secrets. Only Indian case which has surfaced on the issue of confidential information is *Diljeet Titus, Advocate & Ors Vs. Alfred A Adebare*¹⁶¹. As there is no specific law on trade secrets penalizing use of confidential information, the plaintiffs moved the High Court of Delhi for infringement of copyright. The High Court held that the element of 'control' had to be identified in every case for deciding upon the nature of information used. If the information was obtained in the course of contract of service and not contract for service then such information would get adequate protection. The Court did not delve into the issue of importance of pre-existing contract or the distinction between trade secret and confidential information. So, this case cannot be considered as a strong precedent for the pressing issues in trade secrets. Therefore, still Indian courts, when faced with the issue of trade secrets, would have to rely on foreign case laws.

The validity of agreements such as non-compete agreements, non-disclosure agreements etc. have to be examined at the altar of Section 27 of The Indian Contract Act, 1872. The Supreme Court in *Niranjan Shankar Golikari v Century Spg & Mfg Co, Ltd*¹⁶² enumerated the tests to determine the validity of agreements in terms of Section 27. In the instant case, a foreign producer collaborated with a company manufacturing tyre cord yarn by an agreement which stated that the company would maintain secrecy of all technical information. In pursuance of the agreement, the respondent company signed a

non-disclosure agreement with the appellant, at the time of his employment. Clause 9 of the agreement provided that during the continuance of his employment as well as thereafter the employee shall keep confidential and prevent divulgence of any and all information, instruments, documents etc., of the Company that might come to his knowledge. Clause 17 further provided as follows: "In the event of the employee leaving, abandoning or resigning the service of the company in breach of the terms of the agreement before the expiry of the said period of five years he shall not directly or indirectly engage in or carry on of his own accord or in partnership with others the business at present being carried on by the company and he shall not serve in any capacity, whatsoever or be associated with any person, firm or company carrying on such business for the remainder of the said period."

The agreement was held to be valid. The defendant was accordingly restrained from serving anywhere else for the duration of the agreement. The restriction imposed in the present case was limited as to time, the nature of employment and as to area, and cannot therefore be said to be too wide or unreasonable or unnecessary for the protection of the interests of the respondent Company. The Court held that there is an implied term in a contract of employment that a former employee may not make use of his former employer's trade secrets. But subject to the exception, he is entitled to compete.

Employer-Employee Conflict

Indian IT companies are using their bargaining power and weaving in non-compete clauses into fresher's contracts. Experts have said this tactic used for campus hires is not enforceable in the country. Quoting legal experts reported that tech employers are coercing campus hires into signing agreements can at best, act as a deterrent. In most cases, this doesn't go beyond serving a legal notice. But "An employee cannot be restrained from leaving employment and joining a competitor. However, where monetary compensation is paid to an employee in

¹⁶¹ *Diljeet Titus, Advocate v. Alfred A. Adebare*, 130 (2006) D.L.T. 330, 2006 (32) P.T.C. 609 (Del.).

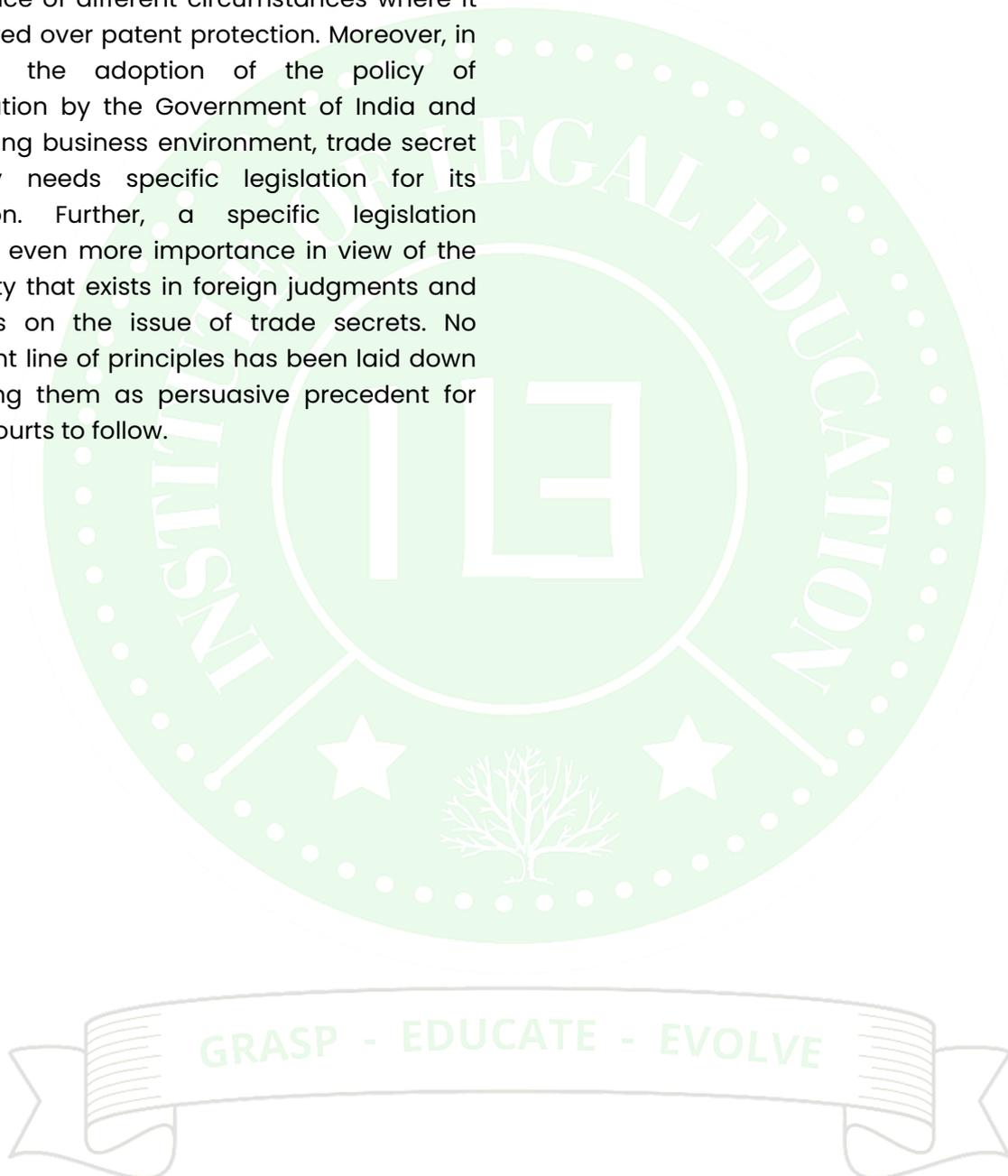
¹⁶² *Niranjan Shankar Golikari v Century Spg & Mfg Co, Ltd* IR 1967 SC 1098.



consideration of non-compete, it may be possible to claim a reasonable part of the monetary benefit in case of loss occurred due to violation of the non-compete obligation.”¹⁶³

Conclusion

Protection of trade secret has acquired great importance in the present scenario due to the emergence of different circumstances where it is preferred over patent protection. Moreover, in view of the adoption of the policy of globalization by the Government of India and the existing business environment, trade secret definitely needs specific legislation for its protection. Further, a specific legislation acquires even more importance in view of the ambiguity that exists in foreign judgments and decisions on the issue of trade secrets. No consistent line of principles has been laid down for setting them as persuasive precedent for Indian Courts to follow.



¹⁶³ IT Freshers Beware! Non-Compete Clauses Woven into Contracts Are Unenforceable in India, Experts Say, The Economic Times (Jan. 9, 2024), <https://economictimes.indiatimes.com/jobs/fresher/it-freshers-beware-non-compete-clauses-woven-into-contracts-are-unenforceable-in-india-experts-say/articleshow/106660774.cms>.