

12

Restrictive Covenants, Trade Secret Misappropriation, and Fiduciary Duties

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I. [12.1] Introduction**II. [12.2] Restrictive Covenants**

- A. [12.3] Ancillarity Requirement
- B. [12.4] Consideration in At-Will Employment Agreements
- C. [12.5] Reasonableness
 - 1. [12.6] Hardship to Employee
 - 2. [12.7] Effect on General Public
 - 3. [12.8] Reasonableness of Temporal Scope
 - 4. [12.9] Reasonableness of Geographic Scope
 - 5. [12.10] Reasonableness of Activity Restraints
- D. [12.11] Legitimate Business Interest
 - 1. [12.12] Near-Permanent Relationship with Clients
 - 2. [12.13] Trade Secrets/Confidential Information
- E. [12.14] Termination Without Cause and Employer Breach

III. Interpretation of Restrictive Covenants

- A. [12.15] Ambiguities in Covenants
- B. [12.16] Judicial Modification: “Blue Pencil” Doctrine

IV. Specific Categories of Restrictive Covenants

- A. [12.17] Nonsolicitation of Customers
- B. [12.18] Nonsolicitation of Employees
- C. [12.19] Covenants Ancillary to Sale of Business
- D. [12.20] Injury to Public: Attorney and Physician Specific Covenants
 - 1. [12.21] Law
 - 2. [12.22] Medicine

V. [12.23] Trade Secrets Misappropriation

- A. What is a “Trade Secret”?
 - 1. [12.24] Definition Under Illinois Trade Secrets Act
 - 2. [12.25] Common Law Factors
 - 3. [12.26] Cases Regarding Existence of Trade Secret

- B. What is “Misappropriation”?
 - 1. [12.27] Definition Under Illinois Trade Secrets Act
 - 2. [12.28] Acquisition by Improper Means
 - 3. [12.29] Disclosure or Use of Trade Secrets
 - 4. [12.30] “Inevitable Disclosure” Doctrine
- C. [12.31] Remedial Scheme of Illinois Trade Secrets Act

VI. [12.32] Fiduciary Duties

- A. [12.33] Corporate Officers, Directors, and Employees
- B. [12.34] Shareholders of Closely Held Corporations
- C. [12.35] Members and Managers of Limited Liability Companies
- D. [12.36] General and Limited Partners of Limited Partnerships
- E. Effects of Fiduciary Relationship on Attorney-Client Relationship: Recent Developments in Illinois Law
 - 1. [12.37] Fiduciary Exception to Attorney-Client Privilege
 - 2. [12.38] Settlement Agreements Between Fiduciaries

VII. [12.39] Emergency Injunctive Relief and Appeals Therefrom

VIII. [12.40] Possible Related Claims

- A. [12.41] Uniform Deceptive Trade Practices Act
- B. [12.42] Common Law Unfair Competition
- C. [12.43] Tortious Interference with Contractual Relations
- D. [12.44] Tortious Interference with Prospective Economic Advantage
- E. [12.45] False Representation of Material Fact
- F. [12.46] Malicious Prosecution
- G. [12.47] Antitrust Violations
- H. [12.48] Patent and Trademark Infringement
- I. [12.49] False or Misleading Statements
- J. [12.50] Defamation
- K. [12.51] Conversion
- L. [12.52] Conspiracy
- M. [12.53] Racketeer Influenced and Corrupt Organizations Act

IX. [12.54] Recommended Reading

I. [12.1] INTRODUCTION

This chapter covers restrictive covenants relative to the rights of employers and employees in the areas of competition, non-solicitation of customers and employees, and protection of confidential information. It also discusses how a business may bring a claim for trade secret misappropriation to protect “secret” information from being improperly acquired and disclosed to others. Finally, the chapter addresses possible restriction of competition and the disclosure of confidential or trade secret information through the enforcement of fiduciary duties, *e.g.*, the rights and obligations of corporate officers and directors, shareholders of closely held corporations, members or managers of limited liability companies, and partners of general and limited partnerships who wish to compete with the corporation.

II. [12.2] RESTRICTIVE COVENANTS

Restrictive covenants most often appear in the employment context and typically attempt to control an employee’s actions post-employment. Generally, there are three types of restrictive covenants that may apply to an employment relationship: (a) a covenant not to compete with the employer post-departure; (b) a covenant not to solicit an employer’s customers or employees post-departure; and (c) a covenant not to disclose an employer’s confidential or trade secret information post-departure.

Although the market utilizes restrictive covenants routinely, Illinois courts generally disfavor restrictive covenants, finding them to be unlawful or unfair restraints on trade. *Joy v. Hay Group, Inc.*, No. 02 C 4989, 2003 U.S. Dist. LEXIS 16045 at *30 (N.D.Ill. Sept. 9, 2003); *Kempner Mobile Electronics, Inc. v. Southwestern Bell Mobile Systems, LLC*, No. 02 C 5403, 2003 U.S. Dist. LEXIS 3512 at *59 (N.D.Ill. Mar. 7, 2003). Post-employment restrictive covenants infringe on employees’ economic mobility and their freedom to follow personal interests. *See C.G. Caster Co. v. Regan*, 43 Ill.App.3d 663, 357 N.E.2d 162, 165, 2 Ill.Dec. 185 (1st Dist. 1976); *Wessel Co. v. Busa*, 28 Ill.App.3d 686, 329 N.E.2d 414, 417 (1st Dist. 1975). Under Illinois law, therefore, it is improper to enforce a restrictive covenant merely because the parties agreed to it. *Advent Electronics, Inc. v. Buckman*, 112 F.3d 267, 274 (7th Cir. 1997). Noncompetition and nonsolicitation agreements are enforceable only if they

- a. are ancillary to a valid employment contract or relationship;
- b. are supported by adequate consideration;
- c. impose reasonable restrictions; and
- d. protect a legitimate business interest. *Lawrence & Allen, Inc. v. Cambridge Human Resource Group, Inc.*, 292 Ill.App.3d 131, 685 N.E.2d 434, 226 Ill.Dec. 331 (2d Dist. 1997).

A. [12.3] Ancillarity Requirement

Before enforcing a restrictive covenant, a court must determine whether the covenant is ancillary to a valid agreement or relationship. *Abel v. Fox*, 274 Ill.App.3d 811, 654 N.E.2d 591, 211 Ill.Dec. 129 (4th Dist. 1995). Traditionally, parties satisfied this requirement by establishing that the covenant was ancillary to a written employment contract and subordinate to that contract's main purpose. See, e.g., *Kempner Mobile Electronics, Inc. v. Southwestern Bell Mobile Systems, LLC*, No. 02 C 5403, 2003 U.S. Dist. LEXIS 3512 at *59 (N.D.Ill. Mar. 7, 2003) (ancillarity satisfied when noncompete provisions were ancillary to an employment agreement and were not its primary focus). More recent Illinois decisions, however, have emphasized that an actual contract is not necessary for a covenant to meet the ancillarity requirement, and a restrictive covenant may be upheld even if it is ancillary to an at-will employment relationship. *Woodfield Group, Inc. v. DeLisle*, 295 Ill.App.3d 935, 693 N.E.2d 464, 230 Ill.Dec. 335 (1st Dist. 1998); *Lawrence & Allen, Inc. v. Cambridge Human Resource Group, Inc.*, 292 Ill.App.3d 131, 685 N.E.2d 434, 226 Ill.Dec. 331 (2d Dist. 1997); *Abel, supra*, 654 N.E.2d at 597.

In addition to the employment relationship, restrictive covenants may also be ancillary to a licensing agreement (see *Abbott Laboratories v. Baxter International Inc.*, No. 01 C 4809, 2002 U.S. Dist. LEXIS 5475 at *37 (N.D.Ill. Mar. 26, 2002)); a lease agreement (see generally *J.C. Nichols Co. v. Eddie Bauer, Inc.*, 4 F.Supp.2d 875, 876 (W.D.Mo. 1998)); a shareholder's agreement (see *Central Water Works Supply, Inc. v. Fisher*, 240 Ill.App.3d 952, 608 N.E.2d 618, 622, 181 Ill.Dec. 545 (4th Dist. 1993)); a settlement agreement (see *Herndon v. Eli Witt Co.*, 420 So.2d 920, 923 (Fla.App. 1982)); a consulting relationship (see *Quixote Transportation Safety, Inc. v. Cooper*, No. 03 C 1401, 2004 U.S. Dist. LEXIS 3879 at *9 (N.D.Ill. Mar. 12, 2004)); an independent contractor relationship (see *Eichmann v. National Hospital & Health Care Services, Inc.*, 308 Ill.App.3d 337, 719 N.E.2d 1141, 1146, 241 Ill.Dec. 738 (1st Dist. 1999) (holding that restrictive covenants in independent contractor relationships are analogous to those in employment context, and same standards apply)); a donor/donee relationship (see *Liautaud v. Liautaud*, 221 F.3d 981 (7th Cir. 2000)); and a sale of business agreement (see, e.g., *Health Professionals, Ltd. v. Johnson*, 339 Ill.App.3d 1021, 791 N.E.2d 1179, 274 Ill.Dec. 768 (3d Dist. 2003)). Because courts analyze restrictive covenants ancillary to a sale of business differently than those ancillary to other types of relationships or agreements, these covenants will be discussed separately. See §§12.17 – 12.19.

One novel type of relationship deemed sufficient to satisfy the ancillarity requirement is that of a donor and donee as explained by the Seventh Circuit in *Liautaud, supra*. In that case, Jim Liautaud owned and operated a chain of gourmet submarine shops under the name of "Jimmy John's." Jim attributed the success of his shops to his style of preparing sandwiches and to his business strategies. In 1988, Jim's cousin, Michael, asked Jim for help in opening his own sandwich shop in Madison, Wisconsin. Jim agreed to help and gifted certain information to Michael, subject to an agreement that Michael would open stores only in Madison. In 1991, Michael opened a sandwich shop in Lacrosse, Wisconsin, outside of Madison, and Jim filed suit to enforce the noncompete covenant. The Seventh Circuit found that the transfer of the secrets of success from Jim to Michael established a valid gift relationship. In the gift relationship, the "donor may wish to protect both his generosity and his business interests from exploitation; therefore, he may desire to impose a covenant not to compete on his donee." 221 F.3d at 986. The

court determined that the covenant not to compete was ancillary to the gift transaction — the gift from Jim to Michael being the essential element of the transaction. The noncompetition agreement was subordinate to the main purpose of the transaction and, therefore, satisfied the ancillarity requirement.

B. [12.4] Consideration in At-Will Employment Agreements

After determining whether a restrictive covenant is enforceable, the court next inquires into whether there is sufficient consideration to support the covenant. In the at-will employment context, consideration becomes an important issue because if the employee can be fired without cause at any time, then the employer is not bound by the employment relationship. There is no consideration, therefore, unless the employer has bound itself in some other way.

The courts have recognized several ways to find consideration in the at-will employment context. First, consideration may arise from the fact that the employer initially provided employment to the employee. When the employee signs the restrictive covenant upon being hired, the employment itself for any period of time constitutes the consideration necessary to support the restrictive covenant. Likewise, employment itself will also constitute consideration if a current employee signs a restrictive covenant under the threat of termination. In that situation, the continued employment thereafter is in direct exchange for agreeing to the terms of the restrictive covenant. For example, in *Lawrence & Allen, Inc. v. Cambridge Human Resource Group, Inc.*, 292 Ill.App.3d 131, 685 N.E.2d 434, 438, 226 Ill.Dec. 331 (2d Dist. 1997), the court found valid consideration to support the restrictive covenant at issue when the at-will employee signed the covenant “under threat of termination” even though there was no “change to his job title, responsibilities, or salary.” The continued employment, which he would not have had if he did not sign the agreement, constituted the consideration necessary to support the covenant. *Id.* See also *Woodfield Group, Inc. v. DeLisle*, 295 Ill.App.3d 935, 693 N.E.2d 464, 230 Ill.Dec. 335 (1st Dist. 1998); *Corroon & Black of Illinois, Inc. v. Magner*, 145 Ill.App.3d 151, 494 N.E.2d 785, 98 Ill.Dec. 663 (1st Dist. 1986).

If a current employee does not sign a restrictive covenant under the threat of termination, consideration may still be found in the form of increased benefits or salary, improved work conditions, or possibly, continued employment for a substantial period of time. For “continued employment” to constitute consideration, however, it must be “substantial.” In Illinois, one or two additional years of continued employment generally has been held to constitute a “substantial” period of time. See *Quixote Transportation Safety, Inc. v. Cooper*, No. 03 C 1401, 2004 U.S. Dist. LEXIS 3879 at *9 (N.D.Ill. Mar. 12, 2004) (continued employment for one year considered adequate consideration); *Mid-Town Petroleum, Inc. v. Gowen*, 243 Ill.App.3d 63, 611 N.E.2d 1221, 1227, 183 Ill.Dec. 573 (1st Dist. 1993) (seven months of continued employment not substantial). See also *Woodfield Group, supra*, 693 N.E.2d at 469 (“Factors other than the time period of the continued employment, such as whether the employee or employer terminated [the] employment, may need to be considered to properly review the issue of consideration.”); *Doyle v. Holy Cross Hospital*, 186 Ill.2d 104, 708 N.E.2d 1140, 237 Ill.Dec. 100 (1999) (Illinois Supreme Court upheld employee’s challenge to employer’s unilateral modification of preexisting employee handbook on basis that there was no new consideration in exchange for new language, rejecting hospital’s assertion that employee’s continued employment constituted consideration for new clauses in handbook).

Recently, courts have upheld restrictive covenants contained in employment agreements after the original employer was acquired by a different corporation and the employee did not sign a new noncompete clause. *Unisource Worldwide, Inc. v. Carrara*, 244 F.Supp.2d 977 (C.D.Ill. 2003); *AutoMed Technologies, Inc. v. Eller*, 160 F.Supp.2d 915 (N.D.Ill. 2001). In *Unisource, supra*, a group of employees agreed to noncompete provisions in contracts with their original employer, Distribix. Distribix later merged with Unisource, a national distributor with significantly more product lines and locations than Distribix. The Distribix contracts were silent as to the assignability of the noncompete clause, and the employees did not agree to new restrictive covenants with Unisource following the merge. Nonetheless, the court held that when an employment agreement is silent as to assignability, an acquiring company may enforce the original contract, including its restrictive covenant, regardless of whether an employee agrees to a new restrictive covenant with the new employer.

Courts have, however, refused to enforce restrictive covenants when the employees to whom the covenant is to apply are not parties to the contract that contains the restrictive covenant. In *Freund v. E.D. & F. Man International, Inc.*, 199 F.3d 382 (7th Cir. 1999), a commodities broker entered into a contract with a brokerage firm to become an employee of the firm and to create a special division within the firm. The contract between the parties contained a clause that no employee hired by the broker could remain at the firm upon the broker's termination and the employee could not come back to work for the firm for one year after the termination. The court found the "covenant not to retain" a variant on an employee noncompete covenant. However, instead of the employees being the promisors, as is typically the case, the restricted employees were not parties to the contract. Since it was not made by, or even known to, the employees affected by it, the court refused to enforce the covenant. The court did state, however, that it believed that under Illinois law, if an employer had made a sufficiently substantial investment in the "human capital" of its employees to support a valid covenant not to compete, that employer could also enforce a promise by another employer not to hire away those employees.

C. [12.5] Reasonableness

Once a court determines ancillarity and consideration, it will next inquire into whether the scope of the noncompete covenant is reasonable in light of the facts and circumstances of the particular case. Illinois courts examine the following factors to determine whether a covenant is reasonable:

1. the hardship to the employee;
2. the effect on the general public;
3. the reasonableness of the temporal scope;
4. the reasonableness of the geographic scope; and
5. the reasonableness of the activity restraints. *StunFence, Inc. v. Gallagher Security (USA), Inc.*, No. 01 C 9627, 2002 U.S.Dist. LEXIS 14787 (N.D.Ill. Aug. 9, 2002).

1. [12.6] Hardship to Employee

To determine whether a noncompete is reasonable, a court will consider the hardship it causes the employee. Courts consider undue hardship caused by a noncompete covenant in several different contexts. For example, if the covenant threatens to completely prevent the employee from working in a certain field of business, courts are likely to regard that restriction as unfair to the employee and decline to enforce the covenant. *Lawrence & Allen, Inc. v. Cambridge Human Resource Group, Inc.*, 292 Ill.App.3d 131, 685 N.E.2d 434, 226 Ill.Dec. 331 (2d Dist. 1997); *Sheehy v. Sheehy*, 299 Ill.App.3d 996, 702 N.E.2d 200, 206, 234 Ill.Dec. 34 (1st Dist. 1998) (finding covenant unenforceable because it precluded funeral director from attending cemeteries within 10-mile restricted zone, thereby effectively denying him ability to be employed in his chosen profession). Moreover, if the agreement is more akin to a “do not retain” covenant requiring an employee to be fired rather than merely banned from alternative employment, a greater hardship exists. *Freund v. E.D. & F. Man International, Inc.*, 199 F.3d 382 (7th Cir. 1999) (covenant requiring employer not to retain employees hired by terminated employee struck down because, inter alia, undue hardship to employees).

Kempner Mobile Electronics, Inc. v. Southwestern Bell Mobile Systems, LLC, No. 02 C 5403, 2003 U.S.Dist. LEXIS 3512 (N.D.Ill. Mar. 7, 2003), is representative of the analysis a court applies to determine undue hardship. In *Kempner*, Kempner Mobile Electronics (Kempner) was a sales and service center for Cingular products and services. Kempner sold Cingular products and services from 1989 until 2002, when Cingular terminated the relationship. In 1999, the parties signed an employment agreement, which included several noncompete provisions with specific activity restraints. Kempner brought suit, seeking, in part, to enjoin Cingular from enforcing any of the noncompete provisions. The court considered the provisions one by one, ultimately upholding a restraint barring Kempner from using Cingular’s name and goodwill to sell competing services, and a restraint that prohibited Kempner from selling competing services to Cingular customers for a limited period of time. However, the court concluded that a third provision, which restricted Kempner from selling any competitive services to any new customers, was “oppressive to Kempner” because it barred Kempner from “engaging in its chosen line of business.” 2003 U.S.Dist. LEXIS 3512 at *75. The court held that although Cingular “has protectable interests in . . . its name and goodwill . . . [prohibiting] Kempner from selling any competing cellular product to anyone is not reasonably tailored to protect those interests.” 2003 U.S.Dist. LEXIS 3512 at *73.

2. [12.7] Effect on General Public

To determine reasonableness, a court will also consider a restrictive covenant’s effect on the general public. For example, in *Liataud v. Liataud*, 221 F.3d 981 (7th Cir. 2000), the court found the restrictive covenant in question unreasonable because it was injurious to the public. In that case, a successful sandwich shop owner donated his secrets of success to his brother-in-law to help him open sandwich shops in Madison, Wisconsin. The gift was, however, subject to a noncompete covenant that restricted the donee from opening any type of sandwich shop outside of Madison without the donor’s approval. The court found this complete ban on expansion injurious to the public because it completely restricted competition. 221 F.3d at 988. (It is worthwhile to note that the *Liataud* court followed a three-element approach to reasonableness,

rather than the five-prong approach followed by more recent Illinois decisions. This *Liautaud* approach involves looking at whether the terms of the covenant are greater than necessary to protect the promisee; whether the terms were not oppressive to the promisor; and whether the terms are injurious to the general public.)

3. [12.8] Reasonableness of Temporal Scope

Before enforcing a restrictive covenant, a court will also examine the reasonableness of its temporal scope. Courts vary on the length of time that is reasonable based on the facts and circumstances of the particular case, although two years is frequently cited. For example, in *McRand, Inc. v. Van Beelen*, 138 Ill.App.3d 1045, 486 N.E.2d 1306, 1315 – 1316, 93 Ill.Dec. 471 (1st Dist. 1985), the court upheld a two-year time restriction as reasonable because it took the employer between one and three years to establish an important account. *See also Joy v. Hay Group, Inc.*, No. 02 C 4989, 2003 U.S. Dist. LEXIS 16045 (N.D.Ill. Sept. 9, 2003) (two years); *PCx Corp. v. Ross*, 168 Ill.App.3d 1047, 522 N.E.2d 1333, 199 Ill.Dec. 474 (1st Dist. 1988) (two years); *Millard Maintenance Service Co. v. Bernero*, 207 Ill.App.3d 736, 566 N.E.2d 379, 152 Ill.Dec. 692 (1st Dist. 1990) (two years). However, in certain industries, two years may be overly restrictive. *See Unisource Worldwide, Inc. v. Carrara*, 244 F.Supp.2d 977 (C.D.Ill. 2003) (in the printing industry, where pricing data changes every 6 to 12 months, a two-year restriction is unreasonable because any information that the employer wants to protect is already “stale” after one year). Specifically, in the fast-paced technology sector, a shorter time restriction arguably is appropriate. *E.g., EarthWeb, Inc. v. Schlack*, 71 F.Supp.2d 299, 313 (S.D.N.Y. 1999) (one-year restriction too long given dynamic nature of Web industry and fact that employee’s success with former employer “depended on keeping abreast of daily changes in content on the Internet”), *aff’d*, 2000 U.S.App. LEXIS 11446 (2d Cir. May 18, 2000).

Although the length of a reasonable covenant may vary, a court will not enforce a covenant completely lacking a time limitation when the geographic restriction on the promisor is unnecessarily stringent. In *Liautaud v. Liautaud*, 221 F.3d 981, 987 (7th Cir. 2000), for example, the covenant prohibited the promisor from expanding “anywhere in the world outside of Madison [Wisconsin].” Because the covenant lacked any duration, the court found that, in effect, the promisor would be unable to expand his business beyond Madison for the rest of his life. The court found the covenant unenforceable, stating that the articulated legitimate business interest did not show why the promisor could not expand to other locations and noted that Illinois courts generally refuse to enforce noncompetition agreements that do not limit the duration of the restriction. The court stated that, although it may take time to establish a sandwich shop business and to attract a sufficient customer base to be profitable, the time needed to do this was not in perpetuity. *See also Eichmann v. National Hospital & Health Care Services, Inc.*, 308 Ill.App.3d 337, 719 N.E.2d 1141, 1146, 241 Ill.Dec. 738 (1st Dist. 1999) (striking covenant with no time limitation and no geographical restrictions).

4. [12.9] Reasonableness of Geographic Scope

In addition to a covenant’s temporal scope, a court will also examine the reasonableness of a covenant’s geographic scope. In this regard, Illinois courts have struck down provisions that extend beyond the major area of a former employer’s business. *StunFence, Inc. v. Gallagher*

Security (USA), Inc., No. 01 C 9627, 2002 U.S. Dist. LEXIS 14787 (N.D.Ill. Aug. 9, 2002); *Lawrence & Allen, Inc. v. Cambridge Human Resource Group, Inc.*, 292 Ill.App.3d 131, 685 N.E.2d 434, 226 Ill.Dec. 331 (2d Dist. 1997). For example, in *StunFence, supra*, an employee distributed his employer's fencing products in a limited area of the northeast United States but signed a noncompete with no geographical limitation. The court found that the restrictive covenant's unlimited geographical scope, coupled with its strict activity limitations that completely excluded the employee from participating in the security fencing business, made the covenant unreasonable. Therefore, the court struck down the covenant because its restrictions "exceed[ed] the reasonable limits of what would be necessary to protect any legitimate interest [the employer] had." 2002 U.S. Dist. LEXIS at *20. See also *Roberge v. Qualitek International, Inc.*, No. 1 C 5509, 2002 U.S. Dist. LEXIS 1217 (N.D.Ill. Jan 25, 2002) (striking restriction prohibiting competition for two years with no geographical restriction as overbroad); *Nobel Biocare USA, Inc. v. Lynch*, No. 99 C 5774, 1999 U.S. Dist. LEXIS 23252 (N.D.Ill. Sept. 16, 1999) (striking restriction prohibiting competition in entire United States for two-year period as overbroad).

However, Illinois courts have upheld restrictions concerning fairly large geographical areas if the restriction is reasonably coextensive with the employer's business territory. In *Midwest Television, Inc. v. Oloffson*, 298 Ill.App.3d 548, 699 N.E.2d 230, 232 Ill.Dec. 783 (3d Dist. 1998), the court upheld a noncompete covenant that prohibited competition within a 100-mile radius for a one-year period. In that case, an extremely popular radio personality sought to have the noncompete covenant in his employment contract stricken in part arguing that the geographical restriction was unreasonable. The court disagreed. Because the employer's radio stations generally had a 60-mile broadcast range, the court found that the 100-mile geographical restriction was reasonably coextensive with the employer's business territory. There was a legitimate concern, therefore, that if the employee went to an overlapping station, the employer's listeners and advertisers would follow. In some cases, even the absence of any geographic limitation may not make the covenant unreasonable and unenforceable. See *Medtronic, Inc. v. Benda*, 689 F.2d 645, 650 (7th Cir. 1982) (holding that absence of geographical limitation did not make covenant unreasonable due to nature of plaintiff's pacemaker business).

5. [12.10] Reasonableness of Activity Restraints

Courts will also consider the reasonableness of the activities that a covenant restrains. In *Roberge v. Qualitek International, Inc.*, No. 1 C 5509, 2002 U.S. Dist. LEXIS 1217 at *12 – 13 (N.D.Ill. Jan 25, 2002), the court distinguished "between those agreements that contain a blanket prohibition on competition and those that limit an employee from engaging in particular types of activities with competitors after they leave the employ of the former employer." The *Roberge* court found the restrictive covenant in question unreasonable because it prohibited a former employee from engaging in any type of competition with the employer for two years without geographic limitation. Rather than banning the former employee from the specific activities that he performed for the employer, the covenant contained an unequivocal ban on competitive employment. The court concluded that this blanket restriction was unenforceable. See also *Joy v. Hay Group, Inc.*, No. 02 C 4989, 2003 U.S. Dist. LEXIS 16045 (N.D.Ill. Sept. 9, 2003) (unlimited geographic scope coupled with broad activity restraints made covenant unreasonable). Cf. *McRand, Inc. v. Van Beelen*, 138 Ill.App.3d 1045, 486 N.E.2d 1306, 1315, 93 Ill.Dec. 471 (1st

Dist. 1985) (upholding noncompete provision even without geographical restriction because purpose of covenant was to prevent McRand from losing clients to former employee with special knowledge and information about those clients and that purpose did not necessarily correlate to restriction limited to specific geographic region).

D. [12.11] Legitimate Business Interest

In addition to the ancillarity, consideration, and reasonableness requirements for a court to enforce a restrictive covenant, an employer must also demonstrate a protectable proprietary interest. *See, e.g., Advent Electronics, Inc. v. Buckman*, 112 F.3d 267, 274 (7th Cir. 1997) (vacating district court order granting preliminary injunction enforcing covenant not to compete because district court failed to determine whether legitimate business interest existed). Illinois courts recognize two basic protectable interests: (1) near-permanent relationships with clients, and (2) trade secrets/confidential information.

1. [12.12] Near-Permanent Relationship with Clients

A protectable interest recognized by courts is the near-permanent client relationship. Illinois courts apply two different tests to determine whether a near-permanent relationship exists: the “seven factor” test and the “nature of the business” test. A court may apply either test. *See Outsource International, Inc. v. Barton*, 192 F.3d 662, 667 (7th Cir. 1999). The seven-factor test considers

- a. the time required to develop clients/customers;
- b. the money invested to acquire clients/customers;
- c. the difficulty in acquiring clients/customers;
- d. the extent of personal contact by the employee with clients/customers;
- e. the extent of the employer’s knowledge of its clients/ customers;
- f. the duration of the association between the employer and clients/customers; and
- g. the continuity of those relationships. *See, e.g., Quixote Transportation Safety, Inc. v. Cooper*, No. 03 C 1401, 2004 U.S. Dist. LEXIS 3879 (N.D.Ill. Mar. 12, 2004); *Hanchett Paper Co. v. Melchiorre*, 341 Ill.App.3d 345, 792 N.E.2d 395, 401, 275 Ill.Dec. 164 (2d Dist. 2003) (choosing to use this test because it provided “more complete analysis of the facts at issue”).

The “nature of the business” test is divided into two categories based on the type of the business at issue:

- a. sales — where generally no near-permanent relationship exists with customers (*see Lawrence & Allen, Inc. v. Cambridge Human Resource Group, Inc.*, 292 Ill.App.3d 131, 685 N.E.2d 434, 226 Ill.Dec. 331 (2d Dist. 1997)); and

- b. professional services — where generally a near-permanent relationship is presumed to exist (see *Midwest Television, Inc. v. Oloffson*, 298 Ill.App.3d 548, 699 N.E.2d 230, 232 Ill.Dec. 783 (3d Dist. 1998)).

The Second District Illinois Appellate Court discussed the seven-factor test in *Hanchett, supra*. In *Hanchett*, employee Melchiorre appealed an order granting a preliminary injunction enforcing a noncompete agreement he entered into with his former employer, Hanchett Paper Company (Hanchett). Hanchett is a distributor of packaging products that spends millions of dollars a year developing and maintaining customers and needs from nine months to several years to develop a single customer. Melchiorre worked in sales for Hanchett from 1990 until 2002, when he left to work for a competitor. Melchiorre took Hanchett customers with him and utilized Hanchett's pricing information to give them the same prices they received when buying from Hanchett. Once Hanchett learned of this, it brought a claim to enforce the noncompete agreement it had with Mechoirre.

To determine whether the company had a protectible interest, the *Hanchett* court recognized that a legitimate business interest exists when (a) an employer has a near-permanent relationship with its customers and its employee would not have had contact with the customers absent the employment; and (b) when, ultimately, the employee gained confidential information through his employment that he attempted to use for his own benefit. 792 N.E.2d at 400.

The *Hanchett* court first considered near-permanency. As a preliminary matter, it emphasized that an employer “need not show that its customer relationships are perpetual or indissoluble, that it has an exclusive relationship with its customers, or that a near-permanent relationship existed with each customer.” 792 N.E.2d at 401. The court then applied the seven-factor test, discussed above, and found that the majority of the factors favored Hanchett. It concluded that Hanchett established a near-permanent relationship when it invested millions of dollars and substantial amounts of time to develop its customer base and maintained these customer relationships for many years. 792 N.E.2d at 401 – 402.

The court further concluded that Melchiorre would not have had contact with its customers without his association with Hanchett. By showing that it taught Melchiorre about the packaging industry, provided Melchiorre with its pre-developed customer list, and gave Melchiorre access to customers that had been with the company for years, Hanchett ultimately proved that it had a protectable business interest. 792 N.E.2d at 402 – 403. See also *Outsource International, supra* (applying nature-of-business test to determine if near-permanent relationship existed).

2. [12.13] Trade Secrets/Confidential Information

As stated above, a restrictive covenant is enforceable only if it is necessary to protect a legitimate business interest. In addition to the near-permanent client relationship, an employer may establish a legitimate business interest when it has trade secrets or confidential information that a former employee acquired during employment and subsequently attempted to use for his or her own benefit. *Unisource Worldwide, Inc. v. Carrara*, 244 F.Supp.2d 977 (C.D.Ill. 2003).

To be considered “confidential,” information (a) must not be generally known; (b) must be valuable to competitors; and (c) must be protected or kept secret by the business claiming that it is confidential. 244 F.Supp.2d at 985. Using these factors to determine whether the employer had a protectable interest, the *Unisource* court examined six different types of information, including the employer’s customer information, pricing information, and personnel information. The court found that none of this information was “confidential,” and thus the restrictive covenants in question were not founded on a legitimate business interest and were not enforceable. 244 F.Supp.2d at 989.

E. [12.14] Termination Without Cause and Employer Breach

A restrictive covenant may be upheld if it meets the ancillarity and consideration requirements, does not cause undue hardship to the employee or public, is necessary to protect a legitimate business interest, and is reasonable in both temporal and geographic scope. A restrictive covenant may still be defeated, however, when an employer breaches the implied covenant of good faith and fair dealing. A critical case regarding bad-faith termination in an at-will employment is *Rao v. Rao*, 718 F.2d 219 (7th Cir. 1983). In *Rao*, the employer attempted to enforce a restrictive covenant against an employee whom it terminated ten days before the employee could have purchased 50 percent of the corporation’s stock for one dollar. The termination was not a result of incompetent performance or job-related problems; rather it was for the employer’s personal financial gain. The *Rao* court concluded that “a restrictive covenant is unenforceable when an employee is terminated in bad faith and without good cause.” 718 F.2d at 224. In so holding, the court distinguished enforcement of restrictive covenants in the at-will employment context when the employee left the employment, rather than when the employer terminated the employee. See *Woodfield Group, Inc. v. DeLisle*, 295 Ill.App.3d 935, 693 N.E.2d 464, 230 Ill.Dec. 335 (1st Dist. 1998); *Lawrence & Allen, Inc. v. Cambridge Human Resource Group, Inc.*, 292 Ill.App.3d 131, 685 N.E.2d 434, 226 Ill.Dec. 331 (2d Dist. 1997); *Abel v. Fox*, 274 Ill.App.3d 811, 654 N.E.2d 591, 211 Ill.Dec. 129 (4th Dist. 1995); *Shorr Paper Products, Inc. v. Frary*, 74 Ill.App.3d 498, 392 N.E.2d 1148, 30 Ill.Dec. 280 (2d Dist. 1979).

Similarly, in *Bishop v. Lakeland Animal Hospital, P.C.*, 268 Ill.App.3d 114, 644 N.E.2d 33, 36, 205 Ill.Dec. 817 (2d Dist. 1994), the court held that “the implied promise of good faith inherent in every contract precludes the enforcement of a noncompetition clause when the employee is dismissed without cause.” The *Bishop* court went on to say that a noncompete agreement will be enforceable only if an employee is terminated for cause, or leaves by his or her own accord. 644 N.E.2d at 36 – 37. Other Illinois courts have adopted this approach. See, e.g., *Francorp, Inc. v. Siebert*, 126 F.Supp.2d 543 (N.D.Ill. 2000) (finding restrictive covenant unenforceable when employer materially breached employment agreement by failing to pay several employees for substantial period of time). For further discussion, see Kenneth J. Vanko, “You’re Fired! And Don’t Forget Your Non-Compete . . .”: *The Enforceability of Restrictive Covenants in Involuntary Discharge Cases*, 1 DePaul Bus. & Comm. L.J. 1 (2002).

III. INTERPRETION OF RESTRICTIVE COVENANTS

A. [12.15] Ambiguities in Covenants

When a restrictive covenant is ambiguous, as a general rule, a court must construe and resolve any doubts in favor of the right to compete and against the restriction. *Marwaha v. Woodridge Clinic, S.C.*, 339 Ill.App.3d 291, 790 N.E.2d 974, 274 Ill.Dec. 201 (2d Dist. 2003) (construing ambiguous clause in restrictive covenant against medical clinic attempting to enforce it). *See also Joliet Medical Group, Inc. v. Ensiminger*, 337 Ill.App.3d 1076, 787 N.E.2d 879, 272 Ill.Dec. 693 (3d Dist. 2003) (same result). *But see Lempa v. Finkel*, 278 Ill.App.3d 417, 663 N.E.2d 158, 215 Ill.Dec. 408 (2d Dist. 1996) (construing covenant not to compete in sale of business context against party to be bound under covenant).

B. [12.16] Judicial Modification: “Blue Pencil” Doctrine

If a restrictive covenant is deemed overbroad as written, the “blue pencil” doctrine under Illinois law permits judicial modification in some circumstances. *Sheehy v. Sheehy*, 299 Ill.App.3d 996, 702 N.E.2d 200, 204, 234 Ill.Dec. 34 (1st Dist. 1998). This doctrine is, like restrictive covenants generally, disfavored by the courts. In *House of Vision, Inc. v. Hiyane*, 37 Ill.2d 32, 225 N.E.2d 21 (1967), the Illinois Supreme Court held that, while a court has discretion to modify a restrictive covenant, an unreasonable covenant cannot be judicially modified to make it enforceable. *See also Pactiv Corp. v. Menasha Corp.*, 261 F.Supp.2d 1009 (N.D.Ill. 2003) (court will not modify unreasonable restrictive covenant when degree of unreasonableness makes it unfair to do so); *Lawrence & Allen, Inc. v. Cambridge Human Resource Group, Inc.*, 292 Ill.App.3d 131, 685 N.E.2d 434, 443, 226 Ill.Dec. 331 (2d Dist. 1997) (“as a result of the significant deficiencies in the postemployment restrictive covenant, we decline plaintiff’s request to make any modifications”).

In addition to reasonableness, a court will consider several factors to determine whether the modification of a restrictive covenant is appropriate. *Pactiv, supra*; *Joy v. Hay Group, Inc.*, No. 02 C 4989, 2003 U.S. Dist. LEXIS 16045 (N.D.Ill. Sept. 9, 2003). For example, courts examine whether the provisions in the agreement operate independently of each other such that the provisions are severable. *Pactiv, supra*, 261 F.Supp.2d at 1016. It is unlikely that a court will modify an unreasonable agreement’s terms if, to make the agreement reasonable, the court would be required essentially to draft a new agreement. *Id.*; *Nobel Biocare USA, Inc. v. Lynch*, No. 99 C 5774, 1999 U.S. Dist. LEXIS 23252 (N.D.Ill. Sept. 16, 1999). Additionally, courts acknowledge that they want to encourage narrow, precise drafting and that judicial modification might have the opposite effect. *Pactiv, supra*, 261 F.Supp.2d at 1016; *Roberge v. Qualitek International, Inc.*, No. 1 C 5509, 2002 U.S. Dist. LEXIS 1217, 20 – 21 (N.D.Ill. Jan 25, 2002) (refusing to modify in hopes of “encourag[ing] employers to write contracts that are more narrowly tailored to meet their individual needs, rather than overly broad covenants which restrict competition in the marketplace for qualified employees”).

IV. SPECIFIC CATEGORIES OF RESTRICTIVE COVENANTS

A. [12.17] Nonsolicitation of Customers

Agreements that do not restrict employees from working for a competitor, but rather restrict them from soliciting an employer's customers or clients often are enforceable because they may be perceived as narrow activity restraints and do not completely restrain employees from engaging in their chosen profession. However, such agreements must be reasonable and thus are more likely to be upheld when the individual against whom the agreement is being enforced is a salesperson and the customers or clients are those with whom the employee had contact during employment. *See, e.g., Arpac Corp. v. Murray*, 226 Ill.App.3d 65, 589 N.E.2d 640, 168 Ill.Dec. 240 (1st Dist. 1992) (although noncompete clause was overbroad, order enforcing nonsolicitation restrictions as to customers upheld). Similarly, courts are less likely to find a covenant reasonable and enforceable if it restricts an employee from soliciting customers whom he or she had never worked with while employed with the employer. *See Lawrence & Allen, Inc. v. Cambridge Human Resource Group, Inc.*, 292 Ill.App.3d 131, 685 N.E.2d 434, 441, 226 Ill.Dec. 331 (2d Dist. 1997).

However, as with all restrictive covenants, to enforce a nonsolicitation of customers provision, an employer must establish a protectable interest in the customers or clients at issue. *See, e.g., Dam, Snell & Teveirne, Ltd. v. Verchota*, 324 Ill.App.3d 146, 754 N.E.2d 464, 469, 257 Ill.Dec. 806 (2d Dist. 2001) (covenant not overly broad when it restricted employee from soliciting all clients, including those that she had not previously provided services to, because employer had near-permanent relationship with its clients); *Com-Co Insurance Agency, Inc. v. Service Insurance Agency, Inc.*, 321 Ill.App.3d 816, 748 N.E.2d 298, 303, 254 Ill.Dec. 852 (1st Dist. 2001) (employer has no protectable interest in customers unless employer can show that employee would not have had contact with customers absent his association with employer).

B. [12.18] Nonsolicitation of Employees

Even if an employer does not enter into a restrictive covenant or nonsolicitation of customers provision with an employee, the employer may still wish to obtain an agreement from the employee that he or she will not, after separation, try to lure any other employees to a competitor. Illinois courts uphold such agreements, known as "nonsolicitation of employee" provisions, finding them necessary to protect the investment that the employer made in training its staff and maintaining its workforce. *See, e.g., Arpac Corp. v. Murray*, 226 Ill.App.3d 65, 589 N.E.2d 640, 168 Ill.Dec. 240 (1st Dist. 1992) (covenant restricting solicitation of employer's employees was reasonably calculated to protect its interest in maintaining stable workforce). *Cf. Pactiv Corp. v. Menasha Corp.*, 261 F.Supp.2d 1009, 1014 (N.D.Ill. 2003) (blanket ban on hiring any management-level employees determined overbroad when corporation had over 100 subsidiaries in 20 countries).

C. [12.19] Covenants Ancillary to Sale of Business

Generally, because of differences in the nature of the protectable interest and the equality of the bargaining power, courts are less reluctant to enforce restrictive covenants obtained in

connection with the sale of a business than those contained in other types of relationships. *Health Professionals, Ltd. v. Johnson*, 339 Ill.App.3d 1021, 791 N.E.2d 1179, 274 Ill.Dec. 768 (3d Dist. 2003); *Lempa v. Finkel*, 278 Ill.App.3d 417, 663 N.E.2d 158, 215 Ill.Dec. 408 (2d Dist. 1996). A covenant ancillary to the sale of a business protects the goodwill purchased by the buyer, ensuring that the former owner will not walk away from the sale with the company's customers and goodwill, leaving the buyer with an acquisition that turns out to be less than what was bargained for. *Smith v. Burkitt*, 342 Ill.App.3d 365, 795 N.E.2d 385, 277 Ill.Dec. 18 (5th Dist. 2003) (examining validity of restrictive covenant ancillary to sale of business that prohibited seller from engaging in any competitive business, countywide, for five years following sale); *Hamer Holding Group, Inc. v. Elmore*, 202 Ill.App.3d 994, 560 N.E.2d 907, 914, 148 Ill.Dec. 310 (1st Dist. 1990) (examining validity of covenant not to compete ancillary to employer's sale of business that prohibited employee from competing with employer within 75-mile radius of employer's business for three years following termination of employment). Furthermore, with a covenant ancillary to the sale of a business, the bargaining power of the parties to the sale is not as unequal as it is between parties in other types of relationships. *Health Professionals, supra*.

Like restrictive covenants in other contexts, to be enforced, a covenant must satisfy the ancillary requirement. To determine ancillarity, courts generally examine the parties' intent to protect the integrity of the sale of the business, such as "requiring execution of the agreement as a condition precedent to the sale, and identifying the agreement as a necessary closing document." 791 N.E.2d at 1190 (finding ancillarity when noncompete agreement was necessary at closing as condition precedent to sale). Unlike restrictive covenants in other contexts, however, by establishing that the restrictive covenant is in fact ancillary to the sale of a business, a party proves that it has a valid protectable interest: the value of the goodwill that has been purchased. *Id.* Goodwill represents the advantages a business has because of its name, location, and reputation. *Smith, supra*.

The enforceability of a restraint ancillary to the sale of a business or property also depends on the reasonableness of the restraint as to time, geographical area, and scope of prohibited business activities. *Hamer, supra*, 560 N.E.2d at 915. Courts apply a three part inquiry to determine reasonableness in this context:

1. the restriction must not be greater than necessary to protect the buyer,
2. the restriction must not be oppressive to the seller, and
3. the restriction must not be injurious to the general public. *Id.*

First, for the restraint to be reasonable to the purchaser, it must protect the purchaser in the enjoyment and possession of the goodwill of the property transferred to him or her, and it can cover only the territory to which the goodwill extends or to which it might reasonably be expected to extend while the restraint exists. *Health Professionals, supra*; *McCook Window Co. v. Hardwood Door Corp.*, 52 Ill.App.2d 278, 202 N.E.2d 36, 41 (1st Dist. 1964).

Second, the restraint must not be unduly harsh or oppressive. The duration and territorial scope of the restraint are unreasonable if they impose on the seller a hardship much greater,

relatively speaking, than the ensuing advantage to the purchaser. *McCook, supra*, 202 N.E.2d at 42. Since the seller typically includes the value of the goodwill in the sales price, there must be a substantial hardship before a court will find a restraint unduly harsh or oppressive to the seller. *Id.* For example, a substantial hardship may be found when the seller can no longer earn a living, relocate, or use a special skill. *Health Professionals, supra*, 791 N.E.2d at 1194.

Third, the restraint must be reasonable to the general public. For example, it should not grant the buyer a monopoly, which would eliminate competition.

Whether the contract is reasonable or contrary to public policy is ultimately a question of law. *Russell v. Jim Russell Supply, Inc.*, 200 Ill.App.3d 855, 558 N.E.2d 115, 123, 146 Ill.Dec. 152 (5th Dist. 1990). However, Illinois courts routinely enforce restrictive covenants ancillary to the sale of a business when the covenant is limited in both geography and duration. *Stamatakis Industries, Inc. v. King*, 165 Ill.App.3d 879, 520 N.E.2d 770, 776, 117 Ill.Dec. 419 (1st Dist. 1987) (concluding that restriction preventing employee/former business owner from competing with his employer/purchaser of business for period of two years after termination of agreement and within 1000 miles of Chicago was not per se unreasonable). If a covenant includes a relatively narrow geographical restriction, courts will allow a broader temporal restriction, even validating restraints lasting between five and ten years. *See, e.g., Hubbard v. Logsdon*, 56 Ill.App.3d 366, 372 N.E.2d 101, 14 Ill.Dec. 296 (4th Dist. 1978) (recognizing validity of noncompetition agreement in which sellers of tug service business agreed to refrain for period of ten years from participating in harbor and fleeting business in vicinity of particular city).

In fact, several relatively older cases hold that the provision for an indefinite duration of the restraint is not, by and of itself, sufficient to render the agreement unenforceable since duration is only one factor in whether a restraint is reasonable. *McCook, supra*, 202 N.E.2d at 41. In *Pelc v. Kulentis*, 257 Ill.App. 213, 218 (2d Dist. 1930), the court stated:

[T]he general rule is that where a contract by which a person covenants not to engage in or carry on a particular business is limited as to territory and is reasonable and proper in other respects, the fact that the duration of the restriction is unlimited will not render the contract invalid.

See also Ryan v. Hamilton, 205 Ill. 191, 68 N.E. 781 (1903); *Storer v. Brock*, 267 Ill.App. 138 (1st Dist. 1932), *aff'd*, 351 Ill. 643 (1933).

On the other hand, if the uncertain duration of the restraint is unreasonable under the circumstances of the particular case, the restraint will not be upheld. *Tarr v. Stearman*, 264 Ill. 110, 105 N.E. 957 (1914). For example, the court in *McCook, supra*, found a covenant that provided for restraint of unlimited duration within 150 miles of the particular business location unreasonable because there was no showing that the plaintiff had customers as far away as 150 miles from its plant and the restraint was greater than necessary for the protection of the plaintiff, the purchaser of the stock.

D. [12.20] Injury to Public: Attorney and Physician Specific Covenants

Even if a restrictive covenant meets the ancillarity requirement, is supported by sufficient consideration, is reasonable, and is necessary to protect a legitimate business interest, a court may strike the covenant down on public policy grounds. When considering a covenant's effect on the general public, courts will look to see if the public's ability to obtain the service in question is hindered. *See, e.g., Lawrence & Allen, Inc. v. Cambridge Human Resource Group, Inc.*, 292 Ill.App.3d 131, 685 N.E.2d 434, 443, 226 Ill.Dec. 331 (2d Dist. 1997) (covenant is reasonable because "outplacement service industry is highly competitive and there are other outplacement firms to provide outplacement services"); *Dowd & Dowd, Ltd. v. Gleason*, 181 Ill.2d 460, 693 N.E.2d 358, 230 Ill.Dec. 229 (1998) (covenant unenforceable because its enforcement would violate public policy principles established by attorney's obligations under Rules of Professional Conduct and public's right to hire attorneys of their choice).

Public policy can play an important role in determining the validity of a noncompete covenant. *See Sheehy v. Sheehy*, 299 Ill.App.3d 996, 702 N.E.2d 200, 234 Ill.Dec. 34 (1st Dist. 1998) (covenant unenforceable because precluding funeral director from attending cemeteries within 10-mile restricted zone would violate public's right regarding choice of burial plots and funeral services). Several issues related to public policy and the enforceability of restrictive covenants apply uniquely to the practice of law and medicine. *See Canfield v. Spear*, 44 Ill.2d 49, 254 N.E.2d 433, 434 – 435 (1969).

1. [12.21] Law

In the practice of law, the Illinois Supreme Court has invalidated noncompete covenants on public policy grounds. *Dowd & Dowd, Ltd. v. Gleason*, 181 Ill.2d 460, 693 N.E.2d 358, 230 Ill.Dec. 229 (1998). *Dowd & Dowd* involved a noncompete covenant contained in an attorney's employment contract with the employer law firm. The Illinois Supreme Court found that the covenant was inconsistent with Rule 5.6 of the Illinois Rules of Professional Conduct (RPC). RPC 5.6 prohibits a lawyer from forming a partnership or employment agreement "that restricts the rights of a lawyer to practice after termination of the relationship, except an agreement concerning benefits upon retirement." The court concluded that enforcement of the covenant would violate the public policy underlying RPC 5.6 because the Rule was "designed both to afford clients greater freedom in choosing counsel and to protect lawyers from onerous conditions that would unduly limit their mobility." 693 N.E.2d at 369.

Illinois courts have gone further and struck down agreements that do not, by their terms, prohibit competition but, if departing attorneys compete, deny them compensation otherwise due. *Cummins v. Bickel & Brewer*, No. 00 C 3703, 2002 U.S. Dist. LEXIS 1820 (N.D.Ill. Feb. 6, 2002). For example, in *Cummins*, the court struck a provision denying withdrawing partners earned compensation when they engaged in competitive behavior, holding that the provision clearly violated public policy by hindering the attorney's ability to take on clients and the client's ability to retain counsel of choice.

There is an exception to the prohibition of noncompete covenants in the practice of law, however, when the agreement concerns benefits upon retirement. For example, in *Hoff v. Mayer, Brown & Platt*, 331 Ill.App.3d 732, 772 N.E.2d 263, 266, 254 Ill.Dec. 225 (1st Dist. 2002), the Illinois appellate court upheld a provision in Mayer, Brown and Platt's Retirement, Disability & Death Benefit Program granting retirement benefits only if a member "substantially ceases the active practice of law on a permanent basis or his or her postretirement practice of law is determined by the firm to be consistent with his or her status as a retiree." In upholding the provision, the court relied heavily on the exception for retirement benefits found in RPC 5.6(a)'s general prohibition against restrictive covenants. The court also relied on the Annotated Model Rules of Professional Conduct's interpretation of this exception — that the receipt of retirement benefits entails an assumption that the attorney is truly retiring from practice and, therefore, the lawyer must remain retired as a condition to receiving the benefits. The fact that other states had upheld similar retirement benefit provisions further persuaded the court. Finally, the court noted that it could not say Mayer Brown violated the policy behind RPC 5.6 by denying retirement benefits since the individual "retiring" relinquished the benefits by resigning from the firm and continuing to practice law.

2. [12.22] Medicine

The role that public policy plays in relation to a noncompete covenant in the practice of medicine is not as clear as in the practice of law. In *Canfield v. Spear*, 44 Ill.2d 49, 254 N.E.2d 433, 434 – 435 (1969), the Illinois Supreme Court upheld an agreement not to compete between a doctor and his clinic. *Canfield* involved a group of associated doctors in a Rockford clinic who sued to enforce a restrictive covenant against a former colleague, Dr. Victor Spear. The covenant prevented Dr. Spear from practicing medicine anywhere in Rockford or within a 25-mile radius of Rockford city limits for a three-year period after the termination of his employment. Dr. Spear resigned from the clinic and engaged in conduct that violated the restrictive covenant by opening a new office in Rockford. The court upheld the restriction, stating that Dr. Spear accepted the terms of the covenant when he agreed to the original employment agreement and his acceptance of the covenant's restrictions was a factor in the clinic's agreement to employ Dr. Spear and provide him with a fairly large salary. The court stated that Dr. Spear should have been able to protect his own interests when he signed his employment agreement and he should, therefore, accept the burdens of the contract along with the benefits.

Although *Canfield* upholds the validity of a noncompete covenant in the practice of medicine, recently this conclusion has come into question. In *Carter-Shields v. Alton Health Institute*, 317 Ill.App.3d 260, 739 N.E.2d 569, 250 Ill.Dec. 806 (5th Dist. 2000), the Appellate Court for the Fifth District struck down a noncompete covenant in a physician's contract. In finding the covenant invalid, the court relied on §9.2 of the Opinions of the Council on Ethical & Judicial Affairs of the American Medical Association (1986) (§9.2), which expressly disfavors the use of any restrictive employment or partnership agreement among physicians. The court analogized to *Dowd & Dowd, Ltd. v. Gleason*, 181 Ill.2d 460, 693 N.E.2d 358, 230 Ill.Dec. 229 (1998), stating that §9.2 and RPC 5.6 were similar in scope since RPC 5.6 prohibits noncompetition agreements and §9.2 condemns noncompetition agreements. The court found the public policy arguments applicable to lawyers equally applicable to doctors; that is, an agreement restricting the right of a lawyer to practice law after leaving a firm and the right of a doctor to practice medicine after

leaving a health care provider limited both professional autonomy and the freedom of clients/patients to choose a lawyer/doctor. These considerations, and the close analogy to the practice of law, resulted in the court refusing to enforce the covenant on public policy grounds. The court found previous case law upholding restrictive covenants in the context of medicine inapposite because the cases were decided prior to *Dowd & Dowd* and did not consider §9.2. The Illinois Supreme Court the court considered the Fifth District's opinion in *Carter-Shields v. Alton Health Institute*, 201 Ill.2d 441, 777 N.E.2d 948, 960, 268 Ill.Dec. 25 (2002). However, because the court found the entire employment agreement at issue void and unenforceable from its inception, it did not address the appellate court's holding concerning the general validity of covenants not to compete within physicians' employment agreements. *Id.* The court deemed the appellate court's opinion on this issue "wholly advisory" and because advisory opinions are to be avoided, it vacated this portion of the appellate court's judgment. *Id.*

Not all districts are in agreement with the Fifth District. In *Prairie Eye Center, Ltd. v. Butler*, 329 Ill.App.3d 293, 768 N.E.2d 414, 263 Ill.Dec. 654 (4th Dist. 2002), the Appellate Court for the Fourth District expressly declined to follow the Fifth District holding in *Carter-Shields*. In that case, the court reasoned that although RPC 5.6 and §9.2 were similar, there were important distinctions between the two. First, the wording of RPC 5.6 is mandatory while §9.2 is only advisory in nature. Second, and more important to the court, RPC 5.6 is codified in the rules of the Illinois Supreme Court and has the force of law as well as being indicative of public policy concerning attorney conduct. The court found it important that §9.2 is not codified in the State of Illinois and, therefore, does not establish public policy. The court acknowledged that "there may be no real difference in the concerns of clients in keeping or choosing lawyers of their own choice and patients in keeping or choosing doctors of their own choice, a distinct difference lies in the legal underpinnings of *Dowd* and *Carter-Shields*." 768 N.E.2d at 420 – 421. Although the court sympathized with the rights of patients to choose their own doctors, it refused to extend the public policy rationale to the medical profession.

Scholars suggest that until the Illinois Supreme Court resolves this debate, medical professionals should be cautious when placing reliance on restrictive covenants of their employees or partners. For further discussion, see Stuart Gimbel and Miles J. Zaremski, *Medical Restrictive Covenants in Illinois: at the Crossroads of Carter-Shields and Prairie Eye Center*, 12 *Annals of Health L.* 1 (2003).

V. [12.23] TRADE SECRETS MISAPPROPRIATION

Restrictive covenants often include confidentiality agreements between parties to protect confidential proprietary or secret information. Even without such a covenant, Illinois common law and statutes will protect certain information if that information rises to the level of a "trade secret." Absent a restrictive covenant, the burden on the proponent to establish secrecy is much higher. Unlike enforcement of a covenant not to compete, however, when it is necessary to establish a legitimate business interest (*e.g.*, a near-permanent relationship with customers or "trade secret" information), an action to protect trade secrets does not require proof that an employee signed a restrictive covenant or even an acknowledgment that certain information is confidential. This is because trade secrets long have enjoyed certain protection under common law (*e.g.*, *ILG Industries, Inc. v. Scott*, 49 Ill.2d 88, 273 N.E.2d 393, 395 (1971)), and, more recently, pursuant to statute (765 ILCS 1065/1, *et seq.*).

Trade secret misappropriation consists of three elements:

- a. the existence of a “trade secret” (not generally known in the industry);
- b. “misappropriation” of the trade secret; and
- c. the defendant’s use of the trade secret in its business. *Learning Curve Toys, Inc. v. PlayWood Toys, Inc.*, 342 F.3d 714, 721 (7th Cir. 2003); *Lucini Italia Co. v. Grappolini*, No. 01 C 6405, 2003 U.S. Dist. LEXIS 7134 at *46 (N.D.Ill. Apr. 24, 2003); *David White Instruments, LLC v. TLZ, Inc.*, No. 02 C 7156, 2003 U.S. Dist. LEXIS 331 at *11 (N.D.Ill. Jan. 6, 2003).

A. What Is a “Trade Secret”?

1. [12.24] Definition Under Illinois Trade Secrets Act

The Illinois Trade Secrets Act (ITSA), 765 ILCS 1065/1, *et seq.*, provides statutory protection for trade secrets. The ITSA became effective on January 1, 1988 and is patterned after the Uniform Trade Secrets Act. The ITSA defines a “trade secret” broadly as follows:

(d) “Trade secret” means information, including but not limited to, technical or non-technical data, a formula, pattern, compilation, program, device, method, technique, drawing, process, financial data, or list of actual or potential customers or suppliers, that:

(1) is sufficiently secret to derive economic value, actual or potential, from not being generally known to other persons who can obtain economic value from its disclosure or use; and

(2) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy or confidentiality. ITSA §2.

The ITSA’s definition “codifies two requirements for trade secret protection that had developed under [Illinois] common law, both of which focus on the secrecy of the information sought to be protected.” *Mangren Research & Development Corp. v. National Chemical Co.*, 87 F.3d 937, 942 (7th Cir. 1996). Each requirement, however, emphasizes a different aspect of secrecy. *Learning Curve Toys, Inc. v. PlayWood Toys, Inc.*, 342 F.3d 714, 722 (7th Cir. 2003). The first requirement precludes protection for information generally known within an industry, if not to the general public. *Id.* Anyone with personal knowledge of the industry can testify as to whether such information is generally known within that industry. *Thermodyne Food Service Products, Inc. v. McDonald’s Corp.*, 940 F.Supp. 1300, 1306 (N.D.Ill. 1996). The second requirement ensures that only plaintiffs who take substantial affirmative steps to prevent others from using its information will obtain trade secret protection. *Learning Curve, supra*, 342 F.3d at 722. *But see Hotsamba, Inc. v. Caterpillar, Inc.*, No. 01 C 5540, 2004 U.S. Dist. LEXIS 4882 at *10 (N.D.Ill. Mar. 24, 2004) (“a party seeking trade secret protection need not establish that it took every available precaution to maintain secrecy as long as it made *reasonable efforts* to maintain its software as secret” (emphasis added)).

Both requirements must be satisfied in order for a court to find a protectable trade secret under the ITSA. *See Compuware Corp. v. Health Care Service Corp.*, 203 F.Supp.2d 952 (N.D.Ill. 2002) (holding ITSA inapplicable because company failed to preserve confidentiality of product).

2. [12.25] Common Law Factors

Illinois common law uses a similar but more detailed approach than the ITSA to determine whether a trade secret exists. *See, e.g., Pope v. Alberto-Culver Co.*, 296 Ill.App.3d 512, 694 N.E.2d 615, 618, 230 Ill.Dec. 646 (1st Dist. 1998) (“[t]hese factors parallel the standards under the Act”; applying two of these factors and finding no trade secret); *Stampede Tool Warehouse, Inc. v. May*, 272 Ill.App.3d 580, 651 N.E.2d 209, 215, 209 Ill.Dec. 281 (1st Dist. 1995) (“[s]ection 2(d)(2) of the ITSA is similar to the common law factors used in determining whether information is a trade secret”). Under the common law approach, courts consider six factors:

- a. the extent to which the information is known outside of company’s business;
- b. the extent to which it is known by employees and others involved in the business;
- c. the extent of measures taken by the company to guard the secrecy of the information;
- d. the value of the information to the company;
- e. the amount of effort or money expended by the company in developing the information; and
- f. the ease or difficulty with which the information could be properly acquired or duplicated by others.

If all six factors are satisfied, the court may protect the alleged secret. *See C&F Packing Co. v. IBP, Inc.*, 224 F.3d 1296 (Fed.Cir. 2000) (applying Illinois law). The Seventh Circuit, however, recently established that the factors do not function as a “six-part test, in which the absence of evidence on any single factor necessarily precludes a finding of trade secret protection”; rather, these factors function “as instructive guidelines for ascertaining whether a trade secret exists under the Act.” *Learning Curve Toys, Inc. v. PlayWood Toys, Inc.*, 342 F.3d 714, 722 (7th Cir. 2003). *See also IVS Hydro, Inc. v. Robinson*, 93 Fed.Appx. 521, 527 (4th Cir. 2004) (adopting the same six-factor test and recognizing that “the absence of evidence on any single factor does not necessarily preclude a finding of a trade secret . . . the factors should be weighed together in making that determination” (citations omitted)). In other words, even if one or more of the factors are left unsatisfied, the court still may afford the product or service trade secret protection.

In *Learning Curve, supra*, the plaintiff, PlayWood Toys, claimed that it had a protectable trade secret in its noise-producing toy railroad track, and that the defendant misappropriated the trade secret before the product had been marketed. The court evaluated the six common law factors, and even though not every single factor weighed in favor of PlayWood, it held that overall, PlayWood had shown that it had a protectable trade secret. Throughout its analysis, the court gave deference to the jury’s finding that PlayWood did have a protectable trade secret.

The *Learning Curve* court first looked at whether PlayWood’s concept for a railroad track was known outside of its business. The court found that this factor favored PlayWood for several reasons: no similar track was on the market until the defendant released its product; the product was unique and differentiated PlayWood from its competitors; and the product had sufficient novelty to have warranted patent protection. Second, the court examined the extent to which the railroad track concept was known to others in PlayWood’s business. Again, the court found that this factor favored PlayWood, as only a few key individuals in the company knew about the noise-producing railroad track concept. The court acknowledged, however, that PlayWood was a small business and that the steps necessary to ensure secrecy in a small company are different than those in a large company. Third, the court looked at the measures taken by PlayWood to guard the secrecy of its concept. The court again found that this factor favored PlayWood, as the actions PlayWood had taken were “reasonable under the circumstances.” 342 F.3d at 725. Fourth, the court analyzed the value of the railroad track concept to PlayWood and its competitors. Here it found substantial evidence favoring PlayWood. Fifth, it considered the time, effort, and costs expended by PlayWood in developing its concept. Although PlayWood had not spent much time or money in developing this concept, the court found that large expenditures were not required under Illinois law. Thus, even though this factor did not weigh in favor of PlayWood, it did not preclude the existence of a trade secret. Finally, the court looked at the ease or difficulty with which PlayWood’s concept could have been properly acquired or duplicated by others. The court found that this factor favored PlayWood for two reasons: the concept was not as simple as it appeared and the product was not yet out on the market. Although PlayWood’s railroad track could have been reverse engineered relatively easily, reverse engineering only defeats a trade secret that is publicly sold, which was not the case here. 342 F.3d at 730.

3. [12.26] Cases Regarding Existence of Trade Secret

The threshold issue in trade secret misappropriation is the existence of a trade secret. Therefore, courts have discussed what constitutes a protectable trade secret and what simply is non-protectable information. Some examples include

- a. outdated information (*Applied Industrial Materials Corp. v. Brantjes* 891 F.Supp. 432 (N.D.Ill. 1994) (no trade secret because information was so outdated that it lacked current economic value));
- b. lack of due diligence to maintain secrecy (*David White Instruments, LLC v. TLZ, Inc.*, No. 02 C 7156, 2003 U.S. Dist. LEXIS 331 at *14 (N.D.Ill. Jan. 6, 2003) (no trade secret when plaintiff failed to maintain secrecy and confidentiality within company and failed to keep information in secure location with limited access); *Southwest Whey, Inc. v. Nutrition 101, Inc.*, 117 F.Supp.2d 770, 780 (C.D.Ill. 2000) (no trade secret when failure to take reasonable efforts to maintain secrecy); *Mutual Life Insurance Company of New York v. Veselik*, No. 97 C 6291, 1998 U.S. Dist. LEXIS 990 at *6 (N.D.Ill. Jan. 22, 1998) (dismissing trade secret claims because plaintiff failed to demonstrate that it made reasonable efforts to maintain secrecy and confidentiality of alleged trade secret));

- c. information generally known (*Hamer Holding Group, Inc. v. Elmore*, 202 Ill.App.3d 994, 560 N.E.2d 907, 148 Ill.Dec. 310 (1st Dist. 1990) (customer list had no economic value because anyone could obtain information from telephone book); *but see RKI, Inc. v. Grimes*, 177 F.Supp.2d 859, 874 (N.D.Ill. 2001) (information meeting ITSA “secrecy” criterion includes customer lists that are not readily ascertainable including list of end users obtained through telephone books, catalogues, and other public sources); *see also Learning Curve Toys, Inc. v. PlayWood Toys, Inc.*, 342 F.3d 714, 723 (7th Cir. 2003) (being first or only one to use certain information or implement certain procedure does not necessarily transform information or procedure into trade secret); *Simon v. Oltmann*, No. 98 C 1759, 2001 U.S.Dist. LEXIS 13924 (N.D.Ill. Aug. 31, 2001) (no trade secret protection if based on information known to and readily available within relevant industry even if product operates on enhanced technology));
- d. information not generally known (*Lucini Italia Co. v. Grappolini*, No. 01 C 6405, 2003 U.S.Dist. LEXIS 7134 at *46 (N.D.Ill. Apr. 24, 2003) (information deemed trade secret because it was not readily ascertainable from any source of public information); *Stampede Tool Warehouse, Inc. v. May*, 272 Ill.App.3d 580, 651 N.E.2d 209, 209 Ill.Dec. 281 (1st Dist. 1995) (customer list considered trade secret based, in part, on fact that, although raw data may have come from public sources, list nevertheless required considerable time and expense to assemble));
- e. ease of duplication (*Delta Medical Systems, Inc. v. Mid-America Medical Systems, Inc.*, 331 Ill.App.3d 777, 772 N.E.2d 768, 265 Ill.Dec. 397 (1st Dist. 2002) (customer list not protectable trade secret because information could be derived easily and duplicated with little effort); *Pope v. Alberto-Culver Co.*, 296 Ill.App.3d 512, 694 N.E.2d 615, 230 Ill.Dec. 646 (1st Dist. 1998) (no trade secret based on fact that information was generally known in industry and could be easily duplicated without considerable time, effort, or expense)); and
- g. time, effort, and money expended on development (*Lucini, supra* (fact that information was developed through great time and effort contributed to court’s finding of a trade secret); *see also Strata Marketing, Inc. v. Murphy*, 317 Ill.App.3d 1054, 740 N.E.2d 1166, 1177, 251 Ill.Dec. 595 (1st Dist. 2000)).

B. What Is “Misappropriation”?

1. [12.27] Definition Under Illinois Trade Secrets Act

In addition to establishing that a trade secret exists under law, a proponent of restricting dissemination must also prove that the secret was misappropriated. The ITSA defines “misappropriation” as both

- a. acquisition of a trade secret by improper means, such as theft or breach of a confidential relationship, and
- b. disclosure or use of an improperly obtained trade secret without its owner’s consent. ITSA §2(b).

2. [12.28] Acquisition by Improper Means

Specifically, to be liable for misappropriation under the ITSA, a trade secret must be acquired through improper means. The ITSA defines “improper means” to include “theft, bribery, misrepresentation, breach or inducement of a breach of a confidential relationship or other duty to maintain secrecy or limit use, or espionage through electronic or other means.” ITSA §2(a). The statutory element is defined broadly and essentially includes everything from outright theft to covert “espionage.”

Liability for misappropriation of confidential information or trade secrets from an employer is not limited to physical taking. A trade secret or confidential information can be misappropriated by copying the trade secret information and also by memorization. *See Stampede Tool Warehouse, Inc. v. May*, 272 Ill.App.3d 580, 651 N.E.2d 209, 209 Ill.Dec. 281 (1st Dist. 1995).

3. [12.29] Disclosure or Use of Trade Secrets

The second prong of the ITSA definition of misappropriation requires that the improperly obtained trade secret be disclosed or used without its owner’s consent. To satisfy this requirement, however, the plaintiff need not show that the defendant copied or used every element of the trade secret. The user of the trade secret may be liable, if he or she made his or her own modifications or improvements, as long as the modification or new product was substantially derived from the trade secret. *See Lucini Italia Co. v. Grappolini*, No. 01 C 6405, 2003 U.S. Dist. LEXIS 7134 at *51 (N.D.Ill. Apr. 24, 2003); *Mangren Research & Development Corp. v. National Chemical Co.*, 87 F.3d 937, 944 (7th Cir. 1996); *Thermodyne Food Service Products, Inc. v. McDonald’s Corp.*, 940 F.Supp. 1300, 1306 (N.D.Ill. 1996). In *Lucini*, for example, the plaintiff did extensive work in preparing to launch a line of flavored olive oils. The plaintiff’s research, design and marketing plans, product formulations, and customer information qualified as protectable trade secrets. The defendant used this information to create his own line of flavored olive oils, but did not market the exact same oils that the plaintiff had planned to produce. Even after taking these minor adjustments into account, the court found that the defendant’s products and packaging were “substantially derived” from the plaintiff’s trade secret information. 2003 U.S. Dist. LEXIS 7134 at *51. Although the defendant had made modifications to suit his own needs, he was still liable for misappropriation.

4. [12.30] “Inevitable Disclosure” Doctrine

The doctrine of “inevitable disclosure” allows a court to protect trade secret information in some circumstances even if the evidence is not clear as to the intent to misappropriate the trade secret. The “inevitable disclosure” doctrine appears to be an equitable doctrine used by holders of an alleged “secret” who have no direct evidence of any misappropriation. Moreover, the inevitable disclosure doctrine has been used sparingly. In *PepsiCo, Inc. v. Redmond*, 54 F.3d 1262 (7th Cir. 1995), Pepsi sought to enjoin its former management level employee, William Redmond, from joining another former Pepsi executive at Quaker, where Redmond’s duties would involve marketing Gatorade and Snapple, in direct competition with Pepsi’s “sports drinks” and “new age drinks.” 54 F.3d at 1263 – 1264. Redmond never signed a noncompete

agreement and there was no evidence that Redmond physically took anything from Pepsi. Furthermore, Redmond disclosed to Pepsi that he was considering the Quaker position prior to his departure, and Pepsi took only limited steps in response. Moreover, Redmond signed a nondisclosure agreement with Quaker requiring him to refrain from making any disclosure of Pepsi information to Quaker, as well as a Quaker “Code of Ethics,” which likewise prohibited such conduct.

Pepsi brought suit and the Seventh Circuit affirmed a six-month injunction prohibiting Redmond from engaging in any competitive employment such as that which he contemplated with Quaker. In so doing, the court relied on the following factors:

a. The ITSA (§3(a)) permits broad injunctive relief to prevent “actual or threatened misappropriation.” 54 F.3d at 1267.

b. Redmond had signed a confidentiality agreement with Pepsi, acknowledging his access to trade secrets, even though this agreement did not contain a noncompete provision. 54 F.3d at 1271.

c. Pepsi presented detailed, specific evidence of Redmond’s knowledge of confidential marketing plans and strategies (complete with special code names). 54 F.3d at 1269 – 1270.

d. Quaker and Pepsi were direct competitors, and Redmond’s duties at his new job stood as strikingly similar to his old job. (“PepsiCo finds itself in the position of a coach, one of whose players has left, playbook in hand, to join the opposing team before the big game.” 54 F.3d at 1270.)

e. Redmond arguably lied to Pepsi about his intentions, and Redmond and Quaker presented inconsistent accounts of his new duties at Quaker. 54 F.3d at 1270.

f. Quaker seemed to express an “unnatural interest” in hiring Pepsi’s employees. 54 F.3d at 1271.

The Seventh Circuit agreed with the district court’s assessment that “unless Redmond possessed an uncanny ability to compartmentalize information, he would necessarily be making decisions about Gatorade and Snapple [Quaker’s products], by relying on his knowledge of [PepsiCo] trade secrets.” 54 F.3d at 1269. Faced with this threat of inevitable disclosure, the court imposed a noncompetition injunction on Redmond. 54 F.3d at 1272. For a recent discussion on the doctrine of inevitable disclosure see Michael R. Levinson, *Inevitable Disclosure: Inquiring Into the Minds of Former Employees*, 16 CBA Rec. 34 (May 2002).

In *RKI, Inc. v. Grimes*, 177 F.Supp.2d 859, 876 (N.D.Ill. 2001), the district court established several factors to determine whether the disclosure of trade secrets is “inevitable”:

- a. the level of competition between the former employer and the new employer;
- b. whether the employee’s position with the new employer is comparable to the position the employee held with the former employer and;

- c. the actions the new employer has taken to prevent the former employee from using or disclosing trade secrets of the former employer.

See also *Lucini Italia Co. v. Grappolini*, No. 01 C 6405, 2003 U.S. Dist. LEXIS 7134 at *53 (N.D.Ill. Apr. 24, 2003) (recognizing *PepsiCo* as the law, and applying the three *RKI* factors to prove that the disclosure of plaintiff's trade secrets was inevitable).

Illinois state courts have applied *PepsiCo* as the correct interpretation of Illinois law. In *Strata Marketing, Inc. v. Murphy*, 317 Ill.App.3d 1054, 740 N.E.2d 1166, 251 Ill.Dec. 595 (1st Dist. 2000), the court held that *PepsiCo* correctly interprets Illinois law and found inevitable disclosure to be a theory under which a plaintiff could bring an ITSA claim. Reversing the trial court, the *Strata* court concluded that the plaintiff had pled sufficient allegations to withstand a motion to dismiss by asserting that the employee "could not operate or function without relying on [the former employer's] alleged trade secrets." 740 N.E.2d at 1179. The court distinguished these allegations from allegations that the employee simply had information and that the employer was fearful the employee would use it. See also *Leggett & Platt, Inc. v. Hickory Springs Manufacturing Co.*, 285 F.3d 1353, 1361 (Fed.Cir. 2002) (reinstating claim under Illinois law holding employee would be "hard pressed to avoid disclosing [trade secret] information").

Although inevitable disclosure is a theory available under Illinois law, several Northern District of Illinois cases have rejected claims of inevitable disclosure. In *Zellweger Analytics, Inc. v. Milgram*, No. 95 C 5998, 1997 U.S. Dist. LEXIS 16539 (N.D.Ill. Oct. 9 1997), the court granted summary judgment on a misappropriation claim based on alleged inevitable discovery of trade secrets. In *Zellweger*, the plaintiff argued that former employees would inevitably disclose a clocking source code and testing harness related to water analysis while working for a competitor. The court rejected the claim because none of the evidence indicated inevitable reliance on the employer's testing harness and, further, because the competitor already had an independently derived and functioning clocking source code.

The Northern District also rejected a claim of inevitable disclosure in *Abbott Laboratories v. Chiron Corp.*, 43 U.S.P.Q.2d (BNA) 1695 (N.D.Ill. 1997), finding the mere allegation that employees knew the employer's business and left after being recruited by a competitor did not state a claim for inevitable disclosure. The court found a claim that the employees could misuse the employer's trade secrets and that the employer feared they would is insufficient. Further, in *Dulisse v. Park International Corp.*, 45 U.S.P.Q.2d (BNA) 1688, 1691 (N.D.Ill. 1998), the Northern District ruled that "the mere existence of particularized knowledge cannot render future misappropriation inevitable." The court in *Dulisse* concluded that such a rule "would undermine the maxim that the ITSA 'should not prevent workers from pursuing their livelihoods when they leave their current positions.'" *Id.* (citing *PepsiCo, supra*, 54 F.3d at 1268). See also *Rotec Industries, Inc. v. Mitsubishi Corp.*, 179 F.Supp.2d 885 (C.D.Ill. 2002) (holding evidence establishing employee had some access to employer's valuable trade secrets insufficient to create genuine issue of material fact to support allegation of misappropriation and misuse); *AutoMed Technologies, Inc. v. Eller*, 160 F.Supp.2d 915 (N.D.Ill. 2001) (requiring more than conclusory allegations that employees will necessarily use trade secrets in their new positions).

The Northern District has also refused to extend the doctrine of inevitable disclosure in certain situations. For example, in *Telular Corp. v. Vox2, Inc.*, No. 00 C 6144, 2001 U.S. Dist. LEXIS 7472 (N.D.Ill. May 31, 2001), the court would not apply the doctrine to situations in which the companies were not in direct competition with each other. Furthermore, in *Complete Business Solutions, Inc. v. Mauro*, 58 U.S.P.Q.2d (BNA) 1399, 1404 n.8 (N.D.Ill. 2001), the court found the doctrine inapplicable because the employment agreement between the employer and the employee allowed the employee to “immediately compete with [the employer] and solicit its clients, as long as [the employee] had no contact with the clients for a one-year period prior to his resignation.” The court found that the employee could clearly compete without disclosing trade secrets. The *Complete Business Solutions* court explained which allegations it thought would support a claim of inevitable disclosure. Quoting *Teradyne, Inc. v. Clear Communications Corp.*, 707 F.Supp. 353 (N.D.Ill. 1989), the court stated that an allegation that the defendants said they would use secrets or disavowed their confidentiality agreements would support a claim of inevitable disclosure, as well as an allegation that the defendant could not operate without the plaintiff’s secrets.

C. [12.31] Remedial Scheme of Illinois Trade Secrets Act

The ITSA contains provisions that authorize a court to issue injunctions and award money damages. The ITSA specifically authorizes a court to enjoin actual or threatened misappropriation of trade secrets. ITSA §3. In addition to injunctive relief, the ITSA provides for an award of damages for misappropriation, including “both the actual loss caused by misappropriation and the unjust enrichment caused by misappropriation that is not taken into account in computing actual loss.” ITSA §4(a). Actual damages under §4(a) may include “lost sales as a result of the competitor’s entry into a market, as well as price erosion.” *Lucini Italia Co. v. Grappolini*, No. 01 C 6405, 2003 U.S. Dist. LEXIS 7134 at *56 (N.D.Ill. Apr. 24, 2003).

The ITSA also provides for exemplary damages of up to twice the amount of compensatory damages if there was a “willful and malicious misappropriation.” ITSA §4(b). To determine whether the misappropriation was “willful and malicious,” Illinois courts look at whether the act was intentional or resulted from the conscious disregard of others’ rights. *Learning Curve Toys, Inc. v. PlayWood Toys, Inc.*, 342 F.3d 714, 730 (7th Cir. 2003) (exemplary damages appropriate when defendant had intentionally misappropriated trade secret, then attempted to conceal it by creating false evidence); *Mangren Research & Development Corp. v. National Chemical Co.*, 87 F.3d 937, 942 (7th Cir. 1996) (damages appropriate when just prior to misappropriation, defendant had acknowledged possibility of lawsuit, then chuckled and insinuated that he would be able to win any such case). If a court finds that the misappropriation was willful and malicious, it may award attorneys’ fees as well. ITSA §5. See *Lucini, supra*, 2003 U.S. Dist. LEXIS 7134 at *59 (attorneys’ fees appropriate when defendants had willfully and maliciously misappropriated trade secrets).

The ITSA contemplates a broad range of assistance in preserving secrecy during litigation, including “granting protective orders in connection with discovery proceedings, holding in-camera hearings, sealing the records of the action, and ordering any person involved in the litigation not to disclose an alleged trade secret without prior court approval.” ITSA §6.

Finally, the ITSA states that it “is intended to displace conflicting tort, restitutionary, unfair competition, and other laws of this State providing civil remedies for misappropriation of a trade secret.” ITSA §8(a). See *Hecny Transportation, Inc. v. Chu*, No. 98 C 7335, 2004 U.S. Dist. LEXIS 5417 at *6 (N.D.Ill. Mar. 30, 2004) (“ITSA abolished all common law causes of action for misuse of trade secrets except for breach of contract claims”); *Fox Controls, Inc. v. Honeywell, Inc.*, No. 02 C 346, 2002 U.S. Dist. LEXIS 15663 at *5 (N.D.Ill. Aug. 21, 2002) (claims based on misuse of confidential and proprietary information are preempted by ITSA); *Thomas & Betts Corp. v. Panduit Corp.*, 108 F.Supp.2d 968, 972 (N.D.Ill. 2000) (to extent claims based on misappropriation of trade secrets, they are preempted by ITSA); *J.H. Chapman Group, Ltd. v. Chapman*, No. 95 C 7716, 1996 U.S. Dist. LEXIS 2256 (N.D.Ill. Feb. 26, 1996) (common law breach of confidential relationship claim preempted); *Nilssen v. Motorola, Inc.*, 963 F.Supp. 664 (N.D.Ill. 1997) (common law claims for breach of confidential relationship, unjust enrichment, and quantum meruit preempted); *Pope v. Alberto-Culver Co.*, 296 Ill.App.3d 512, 694 N.E.2d 615, 230 Ill.Dec. 646 (1st Dist. 1998) (unjust enrichment claim preempted). However, some courts have held that a claim for breach of fiduciary duty is not preempted by the ITSA. See *Labor Ready, Inc. v. Williams Staffing, LLC*, 149 F.Supp.2d 398, 415 (N.D.Ill. 2001); *Combined Metals of Chicago Limited Partnership v. Airtek, Inc.*, 985 F.Supp. 827 (N.D.Ill. 1997) (refusing to dismiss breach of fiduciary duty claim based on fact that information may fail to qualify as trade secret, rendering ITSA preemption provision inapplicable at motion to dismiss stage). But see *Hecny, supra* (holding that breach of fiduciary duty claim was preempted by ITSA).

VI. [12.32] FIDUCIARY DUTIES

In addition to contractual restrictive covenants and the statutory protection of trade secrets under the ITSA, fiduciary duties may also restrict employee competition and disclosure of information. Embodied in a fiduciary relationship is the duty of loyalty, a common law theory available to protect employers. The duty of loyalty in a corporate context provides that a fiduciary will not be permitted to usurp an opportunity that was developed through the use of corporate assets. *Graham v. Mimms*, 111 Ill.App.3d 751, 444 N.E.2d 549, 557, 67 Ill.Dec. 313 (1st Dist. 1982). A corporate opportunity exists when a proposed activity is reasonably incident to the corporation’s present or prospective business and is one in which the corporation has the capacity to engage. See *Lindenhurst Drugs, Inc. v. Becker*, 154 Ill.App.3d 61, 506 N.E.2d 645, 649 – 650, 106 Ill.Dec. 845 (2d Dist. 1987); *Petersen Welding Supply Co. v. Cryogas Products, Inc.*, 126 Ill.App.3d 759, 467 N.E.2d 1068, 1072, 81 Ill.Dec. 946 (1st Dist. 1984). Furthermore, an opportunity belongs to the corporation if it was developed through the use of its corporate assets. *Graham, supra*, 444 N.E.2d at 557. In Illinois, if a corporation’s fiduciary wants to take advantage of a business opportunity that is in the corporation’s line of business, the fiduciary “must first disclose and tender the opportunity to the corporation, notwithstanding the fact that the fiduciary may have believed that the corporation was legally or financially incapable of taking advantage of the opportunity.” 444 N.E.2d at 559. See also *Goldberg v. Michael*, 328 Ill.App.3d 593, 766 N.E.2d 246, 262 Ill.Dec. 626 (2d Dist. 2002) (element of usurpation of corporate opportunity is failure to first disclose opportunity to corporation, allowing corporation to act on it).

The following sections describe in detail fiduciary duties owed within different types of corporate entities: corporations, closely held corporations, limited liability companies, and limited partnerships.

A. [12.33] Corporate Officers, Directors, and Employees

One who occupies a fiduciary relationship to a corporation may not acquire, in opposition to the corporation, property in which the corporation has an interest or tangible expectancy or that is essential to its existence. *Sain v. Nagel*, 997 F.Supp. 1002, 1016 (N.D.Ill. 1998); *E.J. McKernan Co. v. Gregory*, 252 Ill.App.3d 514, 623 N.E.2d 981, 191 Ill.Dec. 391 (2d Dist. 1993) (former officers and employees breached their fiduciary duties to corporation by diverting potential clients to their own businesses).

Corporate officers “owe a fiduciary duty of loyalty to their corporate employer not to (1) actively exploit their positions within the corporation for their own personal benefit, or (2) hinder the ability of a corporation to continue the business for which it was developed.” *Veco Corp. v. Babcock*, 243 Ill.App.3d 153, 611 N.E.2d 1054, 1059, 183 Ill.Dec. 406 (1st Dist. 1993). This duty demands that an officer act solely for his or her employer’s benefit and never to the employer’s detriment during employment. *ABC Trans National Transport, Inc. v. Aeronautics Forwarders, Inc.*, 62 Ill.App.3d 671, 379 N.E.2d 1228, 1237, 20 Ill.Dec. 160 (1st Dist. 1978). Moreover, the “resignation of an officer . . . will not sever liability for transactions completed after the termination of a party’s association with the corporation of transactions which began during the existence of the relationship or were founded on information acquired during the relationship.” *Veco Corp. supra*, 611 N.E.2d at 1059. *ABC Trans National Transport, supra*, 379 N.E.2d at 1237 (new employer should be enjoined because immediate income of new employer was derived primarily from plaintiffs former customers).

It is appropriate to enjoin a former officer and his or her new employer from soliciting the former employer’s customers when the former officer has engaged in competitive activities while still employed in breach of his or her fiduciary duties and the employee’s activity resulted in a loss that is not subject to a clear, complete, and efficient remedy, such as a loss of competitive position. *See Cross Wood Products, Inc. v. Suter*, 97 Ill.App.3d 282, 422 N.E.2d 953, 956 – 959, 52 Ill.Dec. 744 (1st Dist. 1981).

Officers and directors are not the only individuals who can breach fiduciary duties. An employee, too, may be liable since the employer/employee relationship is based on agency. *See Foodcomm International v. Barry*, 328 F.3d 300 (7th Cir. 2003) (employees held to be fiduciaries because they were compensated based on the company’s net profits, held purchasing power, and had significant autonomy and discretion). An agent must act solely for the principal in all matters related to the agency and refrain from competing against the principal. 328 F.3d at 304 (employees breach fiduciary duties when they exploit their positions within the company for their own benefit, fail to inform employer of plans to form rival company, and use company resources to plan their new business); *Dvorak v. Mostardi-Platt Associates, Inc.*, No. 97 C 8461, 1998 U.S. Dist. LEXIS 12666 (N.D.Ill. Aug. 4, 1998) (rejecting argument that non-officer employee who is not bound by restrictive covenant has no fiduciary duty to employer). An employee owes an employer a duty of fidelity and undivided loyalty and is prohibited from acting in a manner

inconsistent with the interests of the employer. The employee's duty is not exclusive, but is an obligation to act solely for the benefit of the employer in all matters connected to the employment. *Riad v. 520 South Michigan Avenue Associates Ltd.*, No. 97 C 2488, 2000 U.S. Dist. LEXIS 7646 (N.D.Ill. May 22, 2000) (stating moonlighting or holding second job may be permissible if it does not interfere with principal's interests).

However, there is an exception to an employee's fiduciary duty. Illinois courts have held that the "preliminary stages" doctrine allows an employee to engage in setting up a competitive corporation while still working for the employer so long as the employee does not commence competition. *Id.* An employee does not violate any fiduciary duty in forming a rival corporation and outfitting it for business while still employed with the future competitor; however, an employee does breach the fiduciary duty to an employer when he or she commences business as a rival while still employed.

B. [12.34] Shareholders of Closely Held Corporations

Due to the intimate nature of closely held corporations, Illinois courts have analogized them to joint ventures and partnerships and have held that shareholders in closely held corporations, unlike those in public companies, owe fiduciary duties to each other. *Hagshenas v. Gaylord*, 199 Ill.App.3d 60, 557 N.E.2d 316, 322 (2d Dist. 1990). In *Hagshenas*, the court concluded that a 50-percent shareholder in a closely held corporation had a fiduciary duty to the other shareholders, as well as the corporation. 557 N.E.2d at 323.

More specifically, shareholders of closely held corporations owe fiduciary duties of full disclosure, utmost good faith, and undivided loyalty to other shareholders, regardless of whether they are active participants in the business or remain as officers or directors. *Id.* However, contrary to the vast amount of case law, *Daley v. Chang (In re Joy Recovery Technology Corp.)*, 257 B.R. 253, 273 (Bankr. N.D.Ill. 2001), determined that "[a] stockholder does not stand in any fiduciary relation to the corporation or its directors; rather, the directors and officers of a corporation occupy a fiduciary or quasi-fiduciary relation to the corporation and its stockholders." The court went on to find that although the majority shareholders may owe a fiduciary duty to minority shareholders, the mere ownership of stock does not create this duty. The court did conclude, however, that if a shareholder exercises control or direction over the management of the corporation, a fiduciary duty is imposed.

No cases within the Seventh Circuit have followed *Joy Recovery Technology* for the proposition stated above, and in fact, many courts have held that even a frozen out minority shareholder of a close corporation, who has no influence or control over corporate affairs, owes fiduciary duties to the corporation. *See Rexford Rand Corp. v. Ancel*, 58 F.3d 1215 (7th Cir. 1995). However, other courts have held that if the shareholder has no influence or control over the corporation, there is no duty to the corporation. *Dowell v. Bitner*, 273 Ill.App.3d 681, 652 N.E.2d 1372, 210 Ill.Dec. 396 (4th Dist. 1995) (23-percent owner of close corporation could not hinder, influence, or control corporation, and therefore defendant had no fiduciary duty as shareholder to corporation after he was removed as director and left employment). Thus, a fiduciary may be restricted in his or her ability to compete, solicit, or use "confidential" information as a result of the fiduciary relationship between the parties in a close corporation.

C. [12.35] Members and Managers of Limited Liability Companies

Limited liability companies, or LLCs, are composed of members and sometimes managers, and may be member-managed or manager-managed. The fiduciary duties of the members and managers vary according to the management structure of the company. In both cases, however, Illinois' LLC statutory scheme provides guidance. See Limited Liability Company Act, 805 ILCS 180/1-1, *et seq.*

In a member-managed LLC, a member owes the duty of loyalty and duty of care to the company and to its other members. 805 ILCS 180/15-3. These duties include (1) accounting to the company for any property, profit, or benefit derived by the member in the conduct of the company's business; (2) acting fairly when a member deals with the company in the conduct or winding up of the business as or on behalf of a party having adverse interests; and (3) refraining from competing with the company in the conduct of the company's business. 805 ILCS 180/15-3(b). *See also Anest v. Audino*, 332 Ill.App.3d 468, 773 N.E.2d 202, 210, 265 Ill.Dec. 840 (2d Dist. 2002).

In a manager-managed company, by comparison, a member "owes no duties to the company or to the other members solely by reason of being a member." 805 ILCS 180/15-3(g)(1). However, in a manager-managed company, a manager owes the same duties as the member of a member-managed company, as set forth above. 805 ILCS 180/15-3(g)(2). While no Illinois cases have yet addressed this issue, *see, e.g., Credentials Plus, LLC v. Calderone*, 230 F.Supp.2d 890, 899 (N.D.Ind. 2002) (finding that because LLCs impose common law fiduciary duty on their officers and members, the sole officer of LLC owed fiduciary duties to company and its other members); *VGS, Inc. v. Castiel*, No. 17995, 2000 Del.Ch. LEXIS 122 at *12 – 15 (Del.Ct.Ch. Aug. 31, 2000) (holding that managers of a manager-managed LLC owe duty of loyalty to other managers as well as to company and its investors).

Like fiduciaries of corporations, members and managers of LLCs may not divert company opportunities. *Anest, supra*, 773 N.E.2d at 210 (member-managed company). "When a corporate fiduciary wants to take advantage of a business opportunity that is within the company's line of business, the fiduciary must first disclose and tender the opportunity to the corporation before he or she takes advantage of it, notwithstanding the fiduciary's belief that the corporation is legally or financially incapable of taking advantage of the opportunity." 773 N.E.2d at 211. When corporate assets are used to develop an opportunity, the resulting opportunity belongs to the corporation, even if it was not feasible for the corporation to pursue the opportunity or it had no expectancy in the project. *Id.* (citing *Graham v. Mimms*, 111 Ill.App.3d 751, 444 N.E.2d 549, 67 Ill.Dec. 313 (1st Dist. 1982)). In *Anest*, the court held that even though the LLC was incapable of taking advantage of a business opportunity, the LLC's member did not have a right to take the opportunity for himself, particularly in light of the fact that the LLC's assets were used to develop the opportunity. *Id.*

D. [12.36] General and Limited Partners of Limited Partnerships

A limited partnership is a partnership composed of one or more general partners who control the business and who are personally liable for the partnership's debts, and one or more limited

partners who contribute capital and share profits, but who cannot manage the business and are liable only for the amount of their contribution. General partners owe limited partners a fiduciary duty “which necessarily encompasses the duty of exercising good faith, honesty, and fairness in his dealings with them and the funds of the partnership.” *Labovitz v. Dolan*, 189 Ill.App.3d 403, 545 N.E.2d 304, 310, 136 Ill.Dec. 780 (1st Dist 1989). When one partner is a senior or managing partner, he or she has a heightened duty to deal fairly and openly and to make complete disclosures. See *Cronin v. McCarthy*, 264 Ill.App.3d 514, 637 N.E.2d 668, 675, 202 Ill.Dec. 129 (1st Dist 1994). Furthermore, if any partner takes responsibility for all financial aspects of the partnership, that partner has a duty to maintain regular and accurate records and to account for partnership transactions. *Beerman v. Graff*, 250 Ill.App.3d 632, 621 N.E.2d 173, 178, 190 Ill.Dec. 304 (1st Dist 1993).

Generally, “limited partners do not per se owe a fiduciary duty to the partnership or to the other partners.” *Herzog v. Leighton Holdings, Ltd. (In re Kids Creek Partners, L.P.)*, 212 B.R. 898, 937 (Bankr. N.D.Ill. 1997). Limited partners do not owe fiduciary duties to the other partners because they are not typically involved in managing the partnership. *Id.* Just as a corporate fiduciary duty “develops only when the stockholder takes a role in corporate management and acts to dominate, interfere with or mislead other stockholders in exercising their rights,” a limited partner’s fiduciary responsibility develops only when he or she is “so involved with the partnership as to create fiduciary duties.” *Id.* For example, a limited partner may owe fiduciary duties if he or she has access to confidential information, is an insider, or is in control of the partnership. *Id.*

Under Illinois partnership law, “it is well established that ‘[a] general partner may be held to have breached his fiduciary duty by personally appropriating a business opportunity which he should have seized for the partnership.’” *Gault v. Foster*, No. 83 C 1688, 1989 U.S. Dist. LEXIS 5714 at *12 – 13 (N.D.Ill. May 17, 1989) (quoting 59 AM.JUR.2d *Partnership* §1342). Illinois courts hold that a partner must not misappropriate a business opportunity that has been developed using partnership assets. 1989 U.S. Dist. LEXIS 5714 at *13. Furthermore, a Maryland court held that a general partner must not appropriate opportunities that are of “critical importance” to the interests of the limited partnership. *Dixon v. Trinity Joint Venture*, 49 Md.App. 379, 431 A.2d 1364 (1981).

Partners can circumvent the duty to disclose partnership opportunities in two ways. First, the partners may end the limited partnership. Once the partnership has terminated, the “fiduciary relationship ceases and the remaining partner is free to do business on his own.” *Langer v. Becker*, 240 Ill.App.3d 823, 608 N.E.2d 468, 470, 181 Ill.Dec. 395 (1st Dist. 1992). Second, the partnership may create a partnership agreement that gives the partners a right to develop and pursue other business opportunities, even in the same line of business that the partnership pursues. See *Gault, supra*, 1989 U.S. Dist. LEXIS 5714 at *13. If a limited partnership has a clause in its partnership agreement that authorizes competition, thus putting the partnership on notice that the partners intend to compete with the partnership, it cannot expect to be informed of all relevant opportunities. See *id.*; *Kahn v. Icahn*, No. 15916, 1998 Del.Ch. LEXIS 223 at *12 (Del.Ch.Ct. Nov. 12, 1998). See also *U.S. West, Inc. v. Time Warner, Inc.*, No. 14555, 1996 Del.Ch. LEXIS 55 at *69 (Del.Ct.Ch. June 6, 1996) (emphasizing that “partnerships are amenable to greater freedom contractually to shape the set of legal relationships that constitute the partnership than are corporations, and this freedom may include clear contracting with respect to ‘fiduciary duties.’”). Accordingly, the language of the partnership agreement is key.

E. Effects of Fiduciary Relationship on Attorney-Client Relationship: Recent Developments in Illinois Law

1. [12.37] Fiduciary Exception to Attorney-Client Privilege

Under the fiduciary exception to the attorney-client privilege, “a communication between a client and its attorney is not privileged from those to whom the client owes a fiduciary duty.” *Monfardini v. Quinlan*, 2004 U.S. Dist. LEXIS 4054 at *9 (N.D.Ill. Mar. 11, 2004). While this exception is not new, an Illinois district court recently expanded the exception to apply to pre-litigation discussions between minority shareholders of a closely held corporation and their counsel.

In *Monfardini*, plaintiff Monfardini was a former shareholder of defendant Vico Associates, Inc. (Vico) as well as President and Chief Operating Officer of United Group, Inc. (United), one of Vico’s primary customers, positions to which the shareholders of Vico had assigned him. The case arose when Monfardini entered into a stock purchase agreement with defendants Quinlan and Siech to sell his shares of Vico stock, and the defendants defaulted on payments. Quinlan and Siech counterclaimed that Monfardini had breached his fiduciary duties to Vico and engaged in fraudulent conduct by selling the Vico stock with full knowledge that its value was going to drop because United was going to terminate its business relationship with Vico. In fact, the defendants alleged that Monfardini had engaged in a plan to dilute the United stock in order to acquire majority ownership, to terminate United’s relationship with Vico, and ultimately to defraud Quinlan and Siech as well as breach his duties to Vico. To substantiate these allegations, the defendants requested documents from a pre-litigation shareholders’ meeting between United’s attorneys and its shareholders. United’s counsel claimed that the documents were protected under attorney-client privilege.

The district court held that the documents were discoverable because they fell under the fiduciary exception to the attorney-client privilege. It acknowledged that both Vico and United were closely held corporations, and that minority shareholders of a closely held corporation have a duty “not to damage the corporate interests.” 2004 U.S. Dist. LEXIS 4054 at *15. They “may also owe a fiduciary duty to the corporation when their interests are controlling on a particular issue” and any time that they have the ability to “hinder, influence, or control the corporation.” 2004 U.S. Dist. LEXIS 4054 at *15 – 16. Here, Vico had assigned Monfardini to the COO position at United with the understanding that he would act with Vico’s best interests in mind, and that he in no way would hinder Vico. Accordingly, Monfardini owed a fiduciary duty to Vico because he had an ability to hinder or influence Vico through his actions as a director of United.

The court also held that Monfardini’s fiduciary duties to Vico were sufficient enough to cause an exception to the attorney-client privilege. The communications that occurred at a United shareholders’ meeting regarding the issuance of stock as it related to Vico fell under the exception because of Monfardini’s duty to Vico. The court also found good cause because Vico might need such information to defend itself, the information was not otherwise available, the information related only to past communications, and the information did not reveal other confidential information. Furthermore, it found that requested post-termination documents were discoverable because an employee’s duty of loyalty continues even after termination as long as the employee retains the ability to hinder or influence the corporation.

2. [12.38] Settlement Agreements Between Fiduciaries

Another recent decision, *Thornwood Inc. v. Jenner & Block*, 344 Ill.App.3d 15, 799 N.E.2d 756, 278 Ill.Dec. 891 (1st Dist. 2003), has significant ramifications for settlement agreements between fiduciaries as well as a lawyer's minimum obligations prescribed by the Rules of Professional Conduct. This case appears to create a viable cause of action for a party to a settlement agreement between fiduciaries. It also provides that a disgruntled former fiduciary may sue the opposing party's law firm that prepared the settlement agreement, even though no fiduciary or attorney-client relationship existed between them.

Thornwood arose upon termination of the fiduciary relationship between Thornton and Follensbee, partners in a joint venture to develop a PGA-quality golf course. When the PGA first declined involvement with the venture, Thornton decided to sell his interest in the partnership. Unbeknownst to Thornton, however, Follensbee had continued to negotiate with the PGA. The partners ultimately executed a settlement agreement through which Follensbee would purchase Thornton's interest in the partnership. The settlement agreement contained a release of Follensbee and a concurrent release of Follensbee's attorneys, Jenner & Block (Jenner). Years later, when Thornton learned that Follensbee had secured PGA involvement, he brought suit against Jenner for aiding and abetting a breach of fiduciary duty, aiding and abetting a scheme to defraud, and abetting a scheme of fraudulent inducement.

The court acknowledged that the settlement agreement contained a specific release of the claims Thornton pursued against Jenner, but held the entire settlement agreement, including the release of Jenner, invalid because Follensbee and Jenner had intentionally concealed material facts surrounding Follensbee's negotiations with the PGA. It concluded that Thornton had pled a cause of action by alleging that Follensbee, as one of the parties to the settlement agreement, owed him a fiduciary duty to disclose his negotiations with the PGA, and Jenner aided Follensbee (its client) in concealing his negotiations from Thornton.

VII. [12.39] EMERGENCY INJUNCTIVE RELIEF AND APPEALS THEREFROM

A party who is threatened with possible harm to its business through breach of restrictive covenants may seek emergency injunctive relief. Typical pleadings in Illinois state court to obtain emergency injunctive relief are set forth below:

- a. verified complaint;
- b. motion for temporary restraining order;
- c. memorandum in support of motion for temporary restraining order;
- d. affidavits of supporting witnesses that conform to S.Ct. Rule 191;
- e. motion for "turnover order" (may be subsumed in temporary restraining order motion and depends on the nature of the action);

- f. motion for order to file pleadings under seal; and
- g. motion for expedited discovery.

New employers and former employees may also consider filing an action for declaratory relief. *See, e.g., Bergstein v. Technology Solutions Co.*, 274 Ill.App.3d 689, 654 N.E.2d 479, 211 Ill.Dec. 17 (1st Dist. 1995) (former employee obtains declaration of invalidity of restrictive covenant).

VIII. [12.40] POSSIBLE RELATED CLAIMS

Sections 12.41 – 12.53 discuss possible claims related to trade secret misappropriation and unfair competition.

A. [12.41] Uniform Deceptive Trade Practices Act

The Uniform Deceptive Trade Practices Act (UDTPA), 815 ILCS 510/1, *et seq.*, is violated when a person acting in the course of business or occupation: (1) “passes off” goods or services as those of another; or (2) causes the likelihood of confusion or misunderstanding as to the source, sponsorship, approval, or certification of goods or services. *Phillips v. Cox*, 261 Ill.App.3d 78, 632 N.E.2d 668, 198 Ill.Dec. 338 (5th Dist. 1994) (setting forth elements of UDTPA claim). *See also Logan Graphic Products, Inc. v. Textus USA, Inc.*, No. 02 C 1823, 2002 U.S. Dist. LEXIS 21801 (N.D.Ill. Nov. 7, 2002) (party bringing UDTPA claim must show that opposing party publicized untrue or misleading statements that disparaged its goods or services); *Egnell, Inc. v. Weniger*, 94 Ill.App.3d 325, 418 N.E.2d 915, 49 Ill.Dec. 895 (1st Dist. 1981) (employer brought action to enjoin former employee who was subject to covenant not to compete from selling product in violation of UDTPA; appellate court reversed trial court holding that there was insufficient evidence to establish likelihood of confusion).

B. [12.42] Common Law Unfair Competition

Subject to the preemption provisions of the ITSA, the common law tort of unfair competition prohibits the adoption or use of a name by a party in a manner likely to cause confusion in the trade as to the source of products or services. *Chapman Performance Products, Inc. v. Producers Sales, Inc.*, 16 Ill.App.3d 459, 306 N.E.2d 615 (1st Dist. 1973). *See also Higher Gear Group, Inc. v. Rockenbach Chevrolet Sales, Inc.*, 223 F.Supp.2d 953, 959 (N.D.Ill. 2002) (“claim of unfair competition exists when a defendant misappropriates the labor and expenditures of a plaintiff and reaps the profits of the plaintiff’s work”); *Microsoft Corp. v. Logical Choice Computers, Inc.*, No. 99 C 1300, 2001 U.S. Dist. LEXIS 479 at *31 (N.D.Ill. Jan. 19, 2001) (holding that it need not address common law claim of unfair competition separately from UDTPA claim, as both have same liability standard).

C. [12.43] Tortious Interference with Contractual Relations

The elements of tortious interference with contractual relations are (1) the existence of a valid and enforceable contract; (2) the defendant’s awareness of this contractual relationship; (3) an

unjustified and intentional inducement of a breach of contract that causes a subsequent breach by the other; and (4) damages. *Ocean Atlantic Development Corp. v. Willow Tree Farm, L.L.C.*, No. 01 C 5014, 2004 U.S. Dist. LEXIS 4152 at *33 – 34 (N.D.Ill. Mar. 17, 2004); *Lawson Products, Inc. v. Chromate Industrial Corp.*, 158 F.Supp.2d 860 (N.D.Ill. 2001); *Dames & Moore v. Baxter & Woodman, Inc.*, 21 F.Supp.2d 817 (N.D.Ill. 1998).

D. [12.44] Tortious Interference with Prospective Economic Advantage

The requirements of tortious interference with prospective economic advantage are (1) reasonable expectancy of entering into a valid business relationship; (2) the defendant's knowledge of the expectancy; (3) an intentional and unjustified interference by the defendant that induced or caused a termination of the expectancy; and (4) resulting damage. *Menasha Corp. v. News America Marketing In-Store, Inc.*, 238 F.Supp.2d 1024, 1035 (N.D.Ill. 2003) (“[t]he theory underlying this tort is that some conduct is so odious that it goes beyond the bounds of legitimate competitive practices”); *Doherty v. Kahn*, 289 Ill.App.3d 544, 682 N.E.2d 163, 224 Ill.Dec. 602 (1st Dist. 1997); *Taimoorazy v. Bloomington Anesthesiology Service, Ltd.*, 122 F.Supp.2d 967 (C.D.Ill. 2000).

E. [12.45] False Representation of Material Fact

The elements of this claim are the false representation of material fact made by the defendant who knew that the representation was false, and reliance on the representation by the plaintiff. *Callahan v. Balfour*, 179 Ill.App.3d 372, 534 N.E.2d 565, 128 Ill.Dec. 383 (1st Dist. 1989). See also *Man Roland, Inc. v. Quantum Color Corp.*, 57 F.Supp.2d 576 (N.D.Ill. 1999) (discussing similar elements of fraudulent misrepresentation).

F. [12.46] Malicious Prosecution

What is the purpose of the lawsuit? Elements of malicious prosecution are (1) malicious intent and lack of probable cause; (2) a former action terminated in the defendant-now-plaintiff's favor; and (3) a special injury or special damage beyond the usual expense, time, or annoyance in defending a lawsuit. *Cult Awareness Network v. Church of Scientology International*, 177 Ill.2d 267, 685 N.E.2d 1347, 226 Ill.Dec. 604 (1997); *Thomas v. Hileman*, 333 Ill.App.3d 132, 775 N.E.2d 231, 266 Ill.Dec. 669 (4th Dist. 2002). See also *Wade v. American Airlines, Inc.*, No. 01 C 3521, 2003 U.S. Dist. LEXIS 15300 (N.D.Ill. Aug. 29, 2003).

G. [12.47] Antitrust Violations

Would requested relief improperly restrict competition in the marketplace? Federal and state antitrust laws may apply. See *Menasha Corp. v. News America Marketing In-Store, Inc.*, 238 F.Supp.2d 1024 (N.D.Ill. 2003); *A & A Disposal & Recycling, Inc. v. Browning-Ferris Industries of Illinois, Inc.*, 279 Ill.App.3d 337, 664 N.E.2d 351, 215 Ill.Dec. 954 (2d Dist. 1996); *MBL (USA) Corp. v. Diekman*, 137 Ill.App.3d 238, 484 N.E.2d 371, 91 Ill.Dec. 812 (1st Dist. 1985) (former employer brought action seeking enforcement of restrictive covenant against employee and employee counterclaimed alleging conspiracy by plaintiffs to monopolize urethane market in violation of antitrust laws; appellate court reversed trial court decision dismissing counterclaim, holding that defendant properly alleged antitrust violation).

H. [12.48] Patent and Trademark Infringement

Has the defendant also violated any patent or trademark laws? *See, e.g., Cullen Electric Co. v. Cullen*, 218 Ill.App.3d 726, 578 N.E.2d 1058, 161 Ill.Dec. 412 (1st Dist. 1991).

I. [12.49] False or Misleading Statements

Is the defendant advertising or otherwise acting in a manner that is (1) false or misleading; (2) actually or likely to deceive a substantial segment of the audience; (3) material to an individual's purchasing decisions; (4) related to interstate commerce; and (5) actually causing or likely to cause injury to the plaintiff? *Logan Graphic Products, Inc. v. Textus USA, Inc.*, No. 02 C 1823, 2002 U.S. Dist. LEXIS 21801 (N.D.Ill. Nov. 7, 2002) (finding that defendant sufficiently pled elements of false advertising under §43(a) of Lanham Act); *Truck Components, Inc. v. K-H Corp.*, 776 F.Supp. 405 (N.D.Ill. 1991) (discussion of Lanham Act).

J. [12.50] Defamation

What is being said to others by the former employee, the former employer, or the new employer? *Logan Graphic Products, Inc. v. Textus USA, Inc.*, No. 02 C 1823, 2002 U.S. Dist. LEXIS 21801 (N.D.Ill. Nov. 7, 2002); *Doherty v. Kahn*, 289 Ill.App.3d 544, 682 N.E.2d 163, 224 Ill.Dec. 602 (1st Dist. 1997); *Tyler Enterprises of Elwood, Inc. v. Shafer*, 214 Ill.App.3d 145, 573 N.E.2d 863, 158 Ill.Dec. 50 (3d Dist. 1991) (employer sought injunction and damages from former employees alleging inter alia breach of restrictive covenant and defamation).

K. [12.51] Conversion

Has the defendant converted company property? To state a claim for conversion, a party must show that (1) it has a right to the property; (2) it has an absolute and unconditional right to the immediate possession of the property; (3) it made a demand for possession; and (4) the defendant wrongfully assumed control over its property. *Morris Silverman Management Corp. v. Western Union Financial Services, Inc.*, 284 F.Supp.2d 964 (N.D.Ill. 2003); *Stathis v. Geldermann, Inc.*, 258 Ill.App.3d 690, 630 N.E.2d 926, 196 Ill.Dec. 761 (1st Dist. 1994). *See also Combined Metals of Chicago Limited Partnership v. Airtek, Inc.*, 985 F.Supp. 827 (N.D.Ill. 1997) (plaintiff could maintain claim for violation of ITSA and claim for conversion of trade secrets).

L. [12.52] Conspiracy

Are two or more people acting together to harm the plaintiff? *ABC Trans National Transport, Inc. v. Aeronautics Forwarders, Inc.*, 90 Ill.App.3d 817, 413 N.E.2d 1299, 46 Ill.Dec. 186 (1st Dist. 1980); *Dames & Moore v. Baxter & Woodman, Inc.*, 21 F.Supp.2d 817 (N.D.Ill. 1998) (plaintiff/former employer alleged sufficient facts against former employee and competitor supporting finding of alleged agreement to solicit clients away from plaintiff/former employer). *See also Higher Gear Group, Inc. v. Rockenbach Chevrolet Sales, Inc.*, 223 F.Supp.2d 953, 959 (N.D.Ill. 2002) (conspiracy claim may be preempted by ITSA).

M. [12.53] Racketeer Influenced and Corrupt Organizations Act

For a discussion of the Racketeer Influenced and Corrupt Organizations Act (RICO), 18 U.S.C. §1961, *et seq.*, see *Rockwell Graphic Systems, Inc. v. DEV Industries, Inc.*, 925 F.2d 174 (7th Cir. 1991) (manufacturer brought action against competitor for violation of ITSA and RICO based on conspiracy to misappropriate trade secrets; Seventh Circuit reversed district court decision dismissing claims, finding that material fact issues existed as to whether manufacturer took reasonable precautions to protect trade secrets). See also *Sears Roebuck & Co. v. Emerson Electric Co.*, No. 02 C 5771, 2003 U.S. Dist. LEXIS 332 (N.D.Ill. Jan. 7, 2003); *Goss Graphics Systems, Inc. v. DEV Industries, Inc.*, 267 F.3d 624 (7th Cir. 2001) (reinstating actions against former employees and competitors for violation of ITSA and for violation of RICO based on conspiracy to misappropriate trade secrets).

IX. [12.54] RECOMMENDED READING

The following are recommended reading:

Convery, James J. and Thomas S. Bradley, *Restrictive Covenants & Confidentiality Restrictions Under Illinois Law*, 13 CBA Rec., No. 1, 58 (Jan. 1999).

COVENANTS NOT TO COMPETE: A STATE-BY-STATE SURVEY (Brian M. Malsberger ed., 3d ed. 2002).

EMPLOYEE DUTY OF LOYALTY: A STATE-BY-STATE SURVEY (Brian M. Malsberger ed., 2d ed. 1999).

Felton, Amy Muran, *I've Got a Trade Secret: Keeping Customer Information Secret in Illinois*, 16 CBA Rec., No. 8, 40 (Nov. 2002).

Gabel, Joan T.A. and Nancy R. Mansfield, *The Information Revolution and Its Impact on the Employment Relationship: An Analysis of the Cyberspace Workplace*, 40 Am.Bus.L.J. 301 (2003).

Gimbel, Stuart and Miles J. Zaremski, *Medical Restrictive Covenants in Illinois: At the Crossroads of Carter-Shields and Prairie Eye Center*, 12 Ann. Health L. 1 (2003).

Levinson, Michael R., *Inevitable Disclosure: Inquiring Into the Minds of Former Employees*, 16 CBA Rec., No. 4, 34 (May 2002).

Quinlan, William R. and John F. Kennedy, *The Rights and Remedies of Shareholders in Closely Held Corporations Under Illinois Law*, 29 Loy.U.Chi.L.J. 585 (1998).

Schaller, William Lynch, *Competing After Leaving: Fiduciary Duties of Closely Held Corporation Shareholders After Hagshenas v. Gaylord*, 84 Ill.B.J. 354 (1996).

Schaller, William Lynch, *Some Preliminary Thoughts About Preliminary Injunctions*, 85 Ill.B.J. 12 (1997).

Stevens, William M., *Restrictive Covenants Forbidden in Law Firm Employment Agreements*, 86 Ill.B.J. 316 (1998).

TRADE SECRETS: A STATE-BY-STATE SURVEY (Brian M. Malsberger ed., 2d ed. 1997, Supp. 2003).

Weiss, Steven A. and Gayle M. McMurry, *Modification of Employment Restrictive Covenants: A Call for Equitable Analysis*, 82 Ill.B.J. 256 (1994).

Vanko, Kenneth J., “*You’re Fired! And Don’t Forget Your Non-Compete . . .*”: *The Enforceability of Restrictive Covenants in Involuntary Discharge Cases*, 1 DePaul Bus. & Comm.L.J. 1 (2002).