



Protecting Trade Secrets and IP in Toll Manufacturing Agreements Checklist

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A Checklist identifying key practical and contractual considerations a company should consider for a toll manufacturing agreement to protect its trade secret and other intellectual property (IP), particularly in Brazil, Russia, India and China (BRIC) countries.

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CONSIDER PRELIMINARY ISSUES

Before entering into a toll manufacturing arrangement, designate specific company employees who are responsible for:

- Conducting a thorough due diligence process to vet and select the prospective manufacturer.
- Determining the transaction structure that will best protect the company's trade secrets and other IP.
- Negotiating the toll manufacturing agreement.
- Managing the toll manufacturing transaction and relationship with the manufacturer.

Conduct Thorough Due Diligence

- Undertake a thorough due diligence investigation of the manufacturer, which may include:
 - background checks of the manufacturer's principal officers and directors;
 - audits of the prospective manufacturer's financial statements;
 - inspections of the manufacturer's facilities; and
 - investigations of manufacturer's supply chain and trading partners.
- Require the prospective manufacturer to submit:
 - business references from past and current clients.;
 - references and credentials for key employees;
 - an overview of its complete organizational structure, as well as beneficial ownership documentation; and
 - a list of all current clients.
- Include in the agreement representations and warranties from the toll manufacturer confirming the due diligence results.

IMPLEMENT PRACTICES AND PROVISIONS TO PROTECT TRADE SECRETS AND IP

Require specific commitments and obligations from the toll manufacturer designed to protect the company's trade secrets and other IP, including:

- Acknowledgements by the toll manufacturer of:
 - the existence of the company's trade secrets;
 - their confidential nature; and
 - their value as derived from their secrecy.
- A transaction structure separating the manufacturing process and including limits on the use and disclosure of specific sensitive information. The structure may define certain types of information and specific scopes of use for:
 - the company versus the contracting toll manufacturer;
 - the contracting toll manufacturer versus other service providers;
 - separate designated facilities of the toll manufacturer; and
 - isolated teams of the toll manufacturer.
- An obligation for the manufacturer to maintain a designated facility for all work involving the transaction.
- Frequent audit rights for the company, which if possible, extend throughout the manufacturer's enterprise.
- The company's right to appoint delegates to oversee the toll manufacturer's operations, with sufficient access rights for these individuals.
- An obligation to limit the use and disclosure of confidential information to specific, identified individuals to the extent they need to know the information. The company's written consent should also be required to substitute the named individuals.
- The toll manufacturer's agreement to provide copies of employment contracts for all employees who have access to confidential information. In addition, the agreements should be modified to include:
 - confidentiality and non-compete obligations; and

- obligations to disclose and assign all developed IP to the company or alternatively to the toll manufacturer, who should be obligated to assign the rights to the company.
- The toll manufacturer's liability to the company for breach by its employees of the specified obligations. Alternatively, or in addition, the company can consider executing agreements itself with the applicable employees for direct enforcement.
- The toll manufacturer's agreement to train its employees to protect confidential information.
- If the agreement permits the toll manufacturer to use independent contractors and consultants, the toll manufacturer's agreement:
 - to be responsible for the actions of such individuals and obligations; and
 - ensure that confidentiality protections at least as protective as those used with its employees apply to such individuals.
- The obligation to mark confidential documents as "Confidential" and encrypt electronic files.
- The toll manufacturer's obligation to maintain electronic firewalls within its computer systems.
- Procedures for transmitting confidential information through secure channels, with established protocols for communication through such channels.
- The toll manufacturer's obligation to segregate confidential information in secure areas and isolate it from:
 - computer networks;
 - communication devices; and
 - any computer that provides access to the internet.
- The toll manufacturer's commitment to maintain physical security for its facilities, including through:
 - security guards;
 - access restrictions and sign-in and sign-out logs for secure areas;
 - surveillance devices;
 - access restrictions for visitors; and
 - restrictions on removal of confidential materials.
- Protocols for the toll manufacturer to terminate employees to prevent trade secret misappropriation.
- The toll manufacturer's obligation to expunge confidential information after use and certify the same to the company.
- Procedures that define the parties' obligations for:
 - presentations;
 - press releases; or
 - other public disclosures
- An obligation for the toll manufacturer to prominently display the company's brand in connection with the products and services and maintain appropriate quality control.

CONSIDER LOCAL LAW

Consult local counsel to help determine the most effective means to protect the company's IP under local law. The laws of a particular jurisdiction will define:

- What constitutes a trade secret in the jurisdiction.
- The protective measures that owners must undertake to be eligible for legal remedies for misappropriation.

ACCOUNT FOR TERM, TERMINATION AND TRANSITION

Require contract provisions that anticipate the company's dissolution of its relationship with the toll manufacturer, including:

- A flexible term for the company, including one or more of the following:
 - a short initial term of the agreement, with renewal terms at the company's discretion;
 - the company's ability to terminate for convenience; and
 - readily exercisable termination triggers for the company and short cure periods for breach.
- Extensive transition services by the manufacturer for the company post-termination, including transferring to the company key:
 - equipment;
 - materials;
 - facilities; and
 - employees.
- The potential right for the company to acquire the manufacturer's facility or designated facilities relating to the transaction after termination or expiration.
- Restrictions on the assignment of the agreement by the manufacturer or the manufacturer's change of control.

INCLUDE DISPUTE RESOLUTION AND ARBITRATION

Incorporate into the toll manufacturing agreement:

- Formal escalation procedures.
- Neutral governing law.
- Unless the court system of the BRIC country provides an effective remedy, binding arbitration of disputes if the dispute cannot otherwise be settled, with venue in an appropriate forum that offers:
 - established procedures; and
 - many potential arbitrators who are fluent in English and have experience with toll manufacturing transactions.

For the links to the documents referenced in this note, please visit our online version at <http://us.practicallaw.com/8-520-6049>



CONSIDER ADDITIONAL PROVISIONS TO PREVENT OR MITIGATE MANUFACTURER BREACH

Consider including certain additional provisions in the agreement to prevent, or at least mitigate the effects of, the manufacturer's breach. For example, requiring the toll manufacturer to:

- Post a bond in escrow.
- Purchase insurance.
- Maintain a letter of credit.
- Grant the company a lien on certain assets, with the company's rights triggered by the manufacturer's breach under certain conditions.

For a discussion of other key toll manufacturing provisions, see *Practice Note, Toll Manufacturing Transactions: Trade Secret and IP Protection, Toll Manufacturing Provisions*.

For more information, search for the following resources on our website.

Topics

- Commercial
(<http://us.practicallaw.com/topic3-500-0084>)
- Confidentiality
(<http://us.practicallaw.com/topic7-103-1304>)
- General IP
(<http://us.practicallaw.com/topic0-103-2076>)
- Supply of Goods and Services
(<http://us.practicallaw.com/topic0-103-1128>)
- Trade Secrets
(<http://us.practicallaw.com/topic3-506-0474>)

Practice Note: Overview

- Joint Ventures: Overview
(<http://us.practicallaw.com/1-107-3580>)

Practice Note

- Toll Manufacturing Transactions: Trade Secret and IP Protection
(<http://us.practicallaw.com/8-525-5209>)

Standard Document

- Confidentiality Agreement: International Joint Ventures
(<http://us.practicallaw.com/2-500-4898>)

Checklist

- Confidentiality and Nondisclosure Agreements Checklist
(<http://us.practicallaw.com/6-501-7380>)

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