



**Non-Disclosure Agreement:**  
An imperative need of the time

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## **1. Introduction:**

This era has witnessed incredible growth in trade and commerce due to globalization and liberalization of markets worldwide. The world over, the governments started the process of economic liberalization, thus provided opportunities to the multinational companies to invest and have access to their markets for mutual benefits. In the last three decades, the business entities witnessed multiple growths in their operations. They garnered substantial market shares for their products & services and transformed themselves as economic powerhouses. Nevertheless, current developments were largely attributable to the unique business ideas/modules, technological developments, trade secrets and other business sensitive information of confidential nature. For example, much of the credit for the success of Coco- Cola, Pepsi, Microsoft and Apple Computers could be accorded to specific business ideas/modules, research & developments and trade secrets and other information of confidential nature.

Thus Confidential Information<sup>1</sup> became essential element in success and failure of the corporate entities. The entrepreneurs recognized the importance of Confidential Information and evolved various physical and legal mechanisms to ensure protection and prevention of Confidential Information from wrongful or inadvertent disclosures.

In the normal course of the business operations, an employee will have access to Confidential Information for discharging his/her regular duties and functions. Further certain information of confidential nature will have to be disclosed by the employer to the employees for specific operational requirements of the business. Hence, the employer would like to ensure that Confidential Information is used for the legitimate purposes related to broader aspects of business operations. And at the same time, employer would also like to ensure that, during the term of employment and thereafter for certain reasonable period, the Confidential Information is not divulged or disclosed wrongfully or inadvertently having detrimental effect on its business interests.

The un-authorized disclosure of Confidential Information by the employee(s) could cause or expose the employer to the irreparable losses/damages in monetary terms as well as damage the reputation and goodwill. For example, if secret mixture of Coca Cola is divulged and made available in public domain, the Coca Cola would certainly loose its substantial business world over. Apart from the substantial financial losses to Coca Cola, the damage to the goodwill and reputation would be significant. Hence every employer would like to put in place all necessary safeguards against the wrongful or inadvertent disclosures of Confidential Information.

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<sup>1</sup> Please see elaborate definition of "Confidential Information" at Point No. 2 of this Article.

Apart from application of various other practical safety measures such as cameras, scrutinises, frisking (through physical or electronic modes) of employees, checking of electronic gadgets and other security measures and procedures etc, the Non-Disclosure Agreement (“NDA”)<sup>2</sup> could play a very vital role in safeguarding the Confidential Information from the un-authorized or inadvertent disclosures during the term of employment of an employee and thereafter for a certain reasonable period. NDA is a legal agreement between the employer and the employees for protection of the Confidential Information and further prevention of the same from wrongful or inadvertent disclosures. NDA also acts as deterrent with the employees against wrongful or inadvertent disclosure of Confidential Information.

This article will briefly discuss about Confidential Information, characteristics and important elements of NDA (negative and positive covenants), importance of NDA and possible threats for not having NDA or not having proper NDA in a business enterprise.

Additionally, the NDA becomes more relevant and essential in the case of software companies, companies engaged in research & development, pharmaceutical & biotechnology companies and other large enterprises where secrecy and confidentiality of data/information is vital for the business operations and stakes in terms of financial proposition and/or loss or damage to goodwill and reputation are substantially high.

## **2. Definition of Confidential Information:**

“**Confidential Information**” means all the information of the employer disclosed or marked to the employee(s) as a information of confidential nature or employee(s) have access to such information in the course of employment whether oral or written and shall include all vital information but shall not be limited to;

- (i) Company’s, business plans, strategies, methods and/or practices;
- (ii) Any information relating to company or its business that is not generally known to the public, including but not limited to information about company’s personnel, products, customers, marketing strategies, accounts, finance, statutory, contractual obligations, services or future business plans;
- (iii) Trade secrets, technical know-how, patents, utility models, formulations, processes/methods of preparation, test data, conducted in house or by/through collaborative/venture efforts, inclusive of any and all improvements, modifications, alterations substantial or otherwise etc.; and

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<sup>2</sup> NDA is also executed with consultants, clients, suppliers and business partners etc, however for brevity; this article will focus on NDA with respect to employees only. NDA is also known as confidentiality agreement.

- (iv) Process Information defined as data/test data/reports/studies in-house or contracted/ quantified steps/ process details whether affixed on paper or transferred by way of oral and/or practical instruction with reference to any product, manufacturing information, procurement specifications, quality control specifications, inspection and test protocols etc.

### **3. Characteristics and important elements of NDA:**

In the usual course of recruitment, an employer issues appointment letters to the employees covering terms and conditions of the employment but often fails to correctly define the rights and obligations of the parties in connection with business sensitive Confidential Information. Therefore, NDA has a role to play in this scenario, which protects the interest of the employers from the unprincipled employees from misusing the Confidential Information, during the term of employment and thereafter, accessed or conveyed to employees for the business objectives. Thus, NDA offers great relief to the entrepreneurs to disclose important business ideas, data, resources, business related sensitive information, technical know-how and trade secrets to the concerned employee for the operational requirements.

NDA is a legally enforceable agreement, executed between the employer and the employees, which prevents the employees from wrongful or inadvertent disclosure of the Confidential Information. The NDA is not required to be very complicated or cumbersome, but it should clearly lay down the terms and conditions creating obligations between the employer and the employees. A lengthy and complex NDA would deter invincible professionals from joining the organization and consequently hamper the businesses in accomplishing their objectives.

The contractual restrictions contained in an NDA will vary according to the nature of the information and the purposes of its disclosure. The NDA should not be one sided favoring to the employers only; such agreement would be held as void in the court of law. The Calcutta High Court in the case of Gopal Paper Mills v. Malhotra held that one sided contract, providing absolute and discretionary powers to one party, shall be void. The NDA should include provisions governing the disclosure of the Confidential Information and shall also describe the conditions, circumstances and actions resulting in disclosure of Confidential Information be deemed as breach of NDA.

NDA can be drafted in different ways depending upon nature of Confidential Information, but NDA, in general, contains positive and negative covenants, conditions and circumstances of breach and remedies available thereon. For the sake of better understanding of the NDA, some of the positive and negative covenants are analysed herein:

**Positive Covenants:**

The employees shall:

- Maintain the highest degree of secrecy for all Confidential Information. This covenant would put onus on the employees to maintain secrecy of all Confidential Information and also operate as a deterrent from wrongful or inadvertent disclosure of Confidential Information;
- Use, discuss or disclose such Confidential Information in a duly authorized manner specific to the business or other authorised purposes in the overall interest of the organization. This covenants would ensure that employees use, discuss or disclose the Confidential Information in a authorized manner for legitimate business purposes;
- Undertake and use the same degree of care in safeguarding the Confidential Information as he/she uses or would use in safeguarding his/her own Confidential Information. The covenant place a reminder in the mindset of an employee to adopt similar approach as he/she would prudently do in respect of personal information of confidential nature; and
- Take all steps necessary to protect the Confidential Information from unauthorized or inadvertent disclosure. It casts obligations on the employees to work as trustees of the Confidential Information entrusted with them and take all essential measures for protection of the same from wrongful or inadvertent disclosure by any employee of the organization.

**Negative Covenants:**

The employees shall not:

- Remove/take away/distribute/forward any Confidential Information without proper authority of the competent official. The covenant ensures that requirement of the removal/ distribution/forwarding of Confidential Information is evaluated by the competent official of the company and if such official is satisfied, with the objects for removal/ distribution/forwarding of Confidential Information, he/she would allow the removal/ distribution/forwarding with or without stipulations or may call for further clarifications from the concerned employee or department.
- Divulge, or allow to be divulged Confidential Information during the term of employment and thereafter for a reasonable period. This matter was settled by the Supreme Court in the case of Niranjan Shankar Golikari v/s Century Spinning<sup>3</sup> that a

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<sup>3</sup> Niranjan Shankar Golikari V/s The Century Spinning And Mfg. Co. Ltd (1967 AIR 1098, 1967 SCR (2) 378), Supreme Court of India.

restriction to disclose the Confidential Information during the term of employment contract and thereafter for a reasonable period is not void and un-enforceable.

- Spread rumors or communicate in relation to the Confidential Information, which causes or may cause disenchantment among the employees or could be detrimental to the interest of the Employer. It has been often seen that disgruntled employees apply a hidden propaganda by spreading the rumours against seniors and/or the management, therefore create a sense of confusion among the concerned employees. The rumours spread like wildfire leading to upsurge in the dissatisfaction level among the related employees and consequently causing veiled losses to the employers due to non proper application/utilization of human resources for the benefits of the organization. This covenants deter the employees from spreading rumours and also from making unwarranted communication/comments with respect to seniors and/or management of the company; and
- At any time, directly or indirectly, communicate with company's customers, suppliers, bankers, competitors or other persons or companies with whom the company does business except as instructed or necessary in the course of performance of duties. In the case of *Bombay Dyeing v/s Mehar Karan Singh*<sup>4</sup>, the Bombay High Court held that sending an e-mail duly attached with a manual of customized software is violation of the negative covenant of the NDA and restrained the defendant from divulging and using the information in any manner. However in the case of *Sanmar Speciality Chemicals Limited v/s Dr. Biswajit Roy*<sup>5</sup>, the plaintiff claimed that defendant is carrying on business which is similar to the business of the applicant by using the confidential information furnished to him by the plaintiff. Further, the plaintiff alleged that the respondent is also soliciting its employees and contacting customers by using the information obtained from it. The Madras High Court refused to grant relief to the plaintiff citing that these information could easily be obtained from some other sources i.e. information is available in the public domain, hence such informations loses the nature of confidentiality and similarly negative covenant of the NDA also loses its enforceability.

Further negative covenants should not be contrary to the section 27 of the Contract Act, 1872. Section 27 provides that every agreement restraining a person from exercising a lawful profession, trade or business of any kind shall to that extent be void. Only exception being sale of goodwill wherein seller agrees to refrain from carrying out similar business within the specified limits, however such limits should be reasonable having regard to the nature of the business. In

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<sup>4</sup> *Bombay Dyeing and Manufacturing Co.Ltd V/s Mehar Karan Singh*, ( Suit No.3313 of 2008), the High Court of judicature at Bombay.

<sup>5</sup> *Sanmar Speciality Chemicals Limited Bangalore V/s Dr. Biswajit Roy*, (AIR2007Mad237) Madras High Court.

the case of *Niranjan Shankar Golikari v/s Century Spinning*<sup>6</sup>, it was held that negative covenants operative during the period of employment when the employee is bound to serve his employer exclusively are not to be regarded as restraint of trade and therefore do not fall under section 27 of the Contract Act. A negative covenant wherein the employee will not engage himself in trade or business or get employed with any other employer and perform similar or substantially similar duties is not a restraint of trade unless the contract is unconscionable or excessively harsh or unreasonable or one-sided.

However, in the case of *Sanmar Speciality Chemicals Limited Bangalore v/s Dr. Biswajit Roy*<sup>7</sup>, the court held that use of Confidential Information by the defendant in his trade or business, which is available in public domain, can not be regarded as contrary to the negative covenants. The negative covenants, restraining a person from exercising trade or business, are contrary to the provisions of Section 27 of the Indian Contract Act and thereby lose their enforceability in law.

#### **4. Importance of NDA**

A unique idea or a specific business module is crucial for success of every business; hence every entrepreneur should give utmost importance for protection of such idea or business module. It is evident that vast majority of breaches relating to Confidential Information are carried out by employees or ex-employees of a company<sup>8</sup>. Therefore, apart from other measures, the execution of NDA between employer and employees is the need of an hour.

Further in the current economic environment, there is a greater need for the employers to protect their Confidential Information to sustain in this fiercely competitive world. Confidential Information can only be protected by keeping it out of the public domain; once the information has reached to the public domain, the essential nature of its confidentiality is lost forever. Accordingly, the role of NDA becomes very critical in providing most effective solutions against wrongful or inadvertent disclosure of Confidential Information.

The under mentioned points highlight the importance of NDA in fulfilling the need of the business entities in protection and prevention of their Confidential Information.

- The employer minimizes the probability of Confidential Information being spread wrongfully or inadvertently by casual/ callous comments of the employees;
- It acts as a deterrent to the employees against wrongful or unwarranted disclosure of Confidential Information; and

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<sup>6</sup> Supra Sl. No. 3

<sup>7</sup> Supra Sl. No.5

<sup>8</sup> UK Insolvency Helpline available at [http://www.insolvencyhelpline.co.uk/business\\_advice/exploit\\_ideas/succeed/nda.php](http://www.insolvencyhelpline.co.uk/business_advice/exploit_ideas/succeed/nda.php)

- If there is any violation of NDA, it will prove to a better tool to contest the matter in the court of law for such breach.

## **5. Threats of not having NDA:**

The involvement of the current and former employees in most of wrongful or inadvertent disclosures or divulging of Confidential Information reflects the magnitude of threats posed by employees and the ex-employees. Further non execution of NDA or execution of inappropriate NDA is one way employer wilfully releasing the employees from their obligations of secrecy and confidentiality during the term of employment and thereafter and therefore these threats continue to loom over perpetually.

NDA vividly describes the rights and obligations of parties and make them conscious of their rights and obligations. NDA enables the employees to know and understand which all information are classified as Confidential Information and also state the authorized/lawful manners for disseminating the Confidential Information to all concerned parties. NDA also describes that what are all circumstances and actions would result in wrongful and inadvertent disclosure of Confidential Information and shall be regarded as breach of terms and conditions of the NDA. As there are numerous advantage for having NDA in place and similarly there are plentiful threats for not having NDA or not having proper NDA. Some of the threats posed due to non execution of NDA or not having proper NDA are stated herein through the illustrations:

### **Illustration-1**

A list for promotion of the employees has been sent from the regional office to the head office and head office is mulling over the objectivity of promotions, cost burden to the company, deployment of promoted employees and impact on other departments/employees etc. In the mean time an employee at the regional office spread rumour/information that because of a particular employee, the promotions of all other employees are being kept in abeyance. Thus create distress among all related employees and the employees become disenchanted with the functioning of the management. This act of an employee leads to reduction in working potency of the effected employees and thereby cause losses/damages to the employer for involuntary under utilisation of human resources. The Employer has to tackle this issue form various angles such as:

- If information spread by an employee at regional office is true, then employer has to plug in the leakage at head office level and also initiate actions against the employee at regional office; and
- If this information happens to be rumour without any truth, then the employee based at regional office has to be bridled for spreading unfounded rumours about Confidential Information.

## **Illustration-2**

The company "X" is planning to acquire company "Y". The company "Y" shall be acquired by acquisition of 100% shareholding at an agreed price. The promoters and employees from both sides will have various meetings to discuss modalities including manner of transfer of shares, payment mechanisms and change of board composition etc. Further, company "X" will carry out financial and legal due diligence of company "Y". In absence of NDA, there will be no restriction on the promoters and employees of either side to refrain from disclosing the highly sensitive and secret information relating to each other and/or the transaction. The illegal or inadvertent disclosure of Confidential Information could be disastrous to the reputation and goodwill of both parties and may also lead to scuttling of the transaction as a whole.

The above illustrations reflect the need of having a NDA in order to deter employees from wrongful or inadvertent disclosure of Confidential Information.

## **6. Remedies for Breach of NDA:**

The employee, by signing the NDA, agrees and acknowledges that any wrongful or inadvertent disclosure of Confidential Information is prohibited. The employees also become conversant that any breach of terms and conditions of NDA may result in irreparable injury and damage to employer and which can not be adequately compensated by the monetary compensation. The NDA provides ample opportunities and remedies to the concerned parties, under the applicable laws or in equity, for protection of their interest.

Some of the remedies available are as:

### **Injunction:**

In case where employer has apprehension that an employee or group of employees possess Confidential Information and may wrongfully or inadvertently disclose the Confidential Information. The employer can approach to the competent court for seeking an injunction against employee(s) in order to restrict them from making such disclosures.

In the case of Bombay Dyeing and Manufacturing Co.Ltd v/s Mehar Karan Singh<sup>9</sup>, the defendant had entered into an NDA with the plaintiff, wherein the defendant had unequivocally agreed not to divulge or disclose to any person the confidential information and knowledge obtained by him during the term of his employment, including information pertaining to the business and affairs of the Plaintiff, trade secrets, list of the plaintiff's customers, suppliers etc., even after he ceases to be in the service of the plaintiff. The Bombay High Court held that sending of an e-mail is violation of NDA and issued injunction against defendant from making any disclosure, divulgement or use of confidential information.

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<sup>9</sup> Supra SI No.4

The grounds for seeking injunction should be comprehensible, definite and fair. Further the plaint should clearly specify about the nature of information which the defendants have gained and what part of information the defendants are attempting to divulge or disclose. The Madras High Court in the case of Polaris Software V/s Suren Khiwadkar<sup>10</sup> refused to grant injunction as the reliefs sought for by the plaintiff company were obscure and unclear.

**Claim for losses or damages:**

Where, due to wrongful or inadvertent disclosure of Confidential Information, employer incurs any cost or made to bear any loss or damage, the employer shall have right to claim such losses and damages against erring employees. The similar rights shall also be bestowed with the employees for protection of their rights against the employers as well.

**Re-imbursalment of legal fees and other costs:**

The parties shall also have right to claim reimbursement of reasonable legal fees and other costs incurred in enforcing their rights against other party.

**7. Conclusion:**

This article has led to the conclusion that execution of NDA between employer and the employee is imperative in the present economic environment. Further, the employers have to revisit their personnel policies and set out the processes wherein employees, depending upon their position in employment, play an important role in safeguarding and preventing the wrongful or inadvertent disclosure of Confidential Information.

Success of the business operation is paramount for any entrepreneur and Confidential Information plays an important tool in accomplishing the business objectives. Hence employer should initiate proactive steps and ensure that NDA are executed, this will not only ensure protection of Confidential Information but also acts as deterrent from wrongful or inadvertent disclosure of Confidential Information. NDA will also eliminate the requirement of contesting costly legal suits in the courts for restraining wrongful or inadvertent disclosure of Confidential Information or claiming compensation for losses/damages/costs caused or incurred due to wrongful or inadvertent disclosure of Confidential Information.

Solution for successfully combating the wrongful or inadvertent disclosure of Confidential Information lies in efficient and effective processes, well defined roles and responsibilities of the employees and carefully drafted NDA between the employer and the employees.

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<sup>10</sup> Polaris Software Lab. Limited V/s Suren Khiwadkar, { (2004) ILLJ 323 Mad, (2003) 3 MLJ 557 } Madras High Court.