Commercial Litigation: Seven Practical Tips

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Business executives who have faced lawsuits as plaintiffs or defendants understand the effect that commercial litigation can have on a business's ability to focus on its goals, objectives and customers. Kean Miller helps companies involved in litigation assess their options and make decisions consistent with their goals. The following article addresses seven important issues that savvy businesses should be aware of in the boardroom and in the courtroom.

COMPETING EMPLOYEES, TRADE SECRETS AND ARBITRATION

1. Noncompete agreements

The Louisiana Legislature recently passed a law overruling the Louisiana Supreme Court decision in *S.W.A.T. 24*. In that action, the Court addressed the meaning of the Louisiana non-compete statute. The statute provides that every contract for which anyone is restrained from exercising a lawful profession, trade or business is null and void, except in certain circumstances. One of the circumstances is a person who is employed as an agent, servant or employee may agree with his employer to refrain from carrying on or engaging in a business similar to that of the employer within specified parishes or municipalities, not to exceed a period of two years. The Supreme Court defined "carrying on or engaging in" to mean that if the employee carries on or engages in his or her own business, a noncompete agreement cannot be enforced against one who is an employee of a competing business. Governor Foster signed Act No. 428 enacting House Bill 1770, which amends the noncompete statute to provide that a person who becomes employed by a competing business, regardless of whether or not that person is an owner or equity interest holder of that competing business, may be deemed to be "carrying on or engaging in" a business similar to that of the party having a contractual right to prevent that person from competing. Thus, the Legislature has overruled *S.W.A.T. 24* and employees can be restricted from not only going into competition as a part of his or her own business, but also from working as an employee of a competing business.

2. Protect your trade secrets

Businesses should be careful in storing and retaining confidential information. In the event the information is misappropriated, the business will want to file for injunctive relief, pursuant to the Uniform Trade Secrets Act. The Act defines a trade secret as information, including a formula, pattern, in compilation, program, device, method, technique, or process that derives independent, economic value, actual or potential, from not being generally known, and not being readily ascertainable by proper means, by other persons who can obtain economic value from its disclosure or use. From a practical standpoint, it is any information that gives a business a competitive edge. Consideration of whether information fits within this definition involves factors such as the extent to which the information may be known outside of the business, the value of information to the business or its competitors, and ease of which the information can be acquired. However, there is a second component of the definition which is often overlooked. To constitute a trade secret, the information must be subject to efforts that are reasonable under the circumstances to maintain its secrecy. Thus, information that may have the intrinsic characteristics of a trade secret can lose this cloaking because of the action of the owner in not securing it. Businesses should implement a corporate trade secret program to keep confidential information in a controlled environment. Businesses should consider such things as restricting access to the physical plant, limiting employee access to documents, using nondisclosure agreements and confidentiality legends, trade secret stamps, and computer passwords. When and if confidential information is misappropriated by a former employee or otherwise, these activities, or the lack thereof, will be the subject of scrutiny by the Court in determining whether a trade secret is at issue.

3. Draft arbitration agreements carefully

Many businesses are electing to include arbitration clauses as part of consumer contracts. As part of the underlying transaction, the parties are agreeing to forego the courtroom and bring any dispute to binding arbitration. However, when a dispute arises, the business will want to be in the position to enforce the contract and require arbitration. This may even include overcoming the consumer's "I didn't know what I was signing defense." In any civil action to compel arbitration, the circumstances surrounding the drafting and execution of the contract

will be at issue and thus should be considered prior to execution.

INSURANCE COVERAGE

4. Understand your insurance policy

Most general liability policies are underwritten on either an "occurrence" or a "claims-made" basis. The occurrence policy applies to accidents that take place during the policy term. Such policies typically require prompt notice of an occurrence, and any delay will not adversely affect coverage in the absence of prejudice to the insurer. Claims-made policies cover a claim made against the insured during the policy term, but may also require notice to the insurer, during the policy term. The failure to provide notice under a claims-made policy may preclude recovery. Not all claims-made policies contain the same notice provisions. Thus, the first reaction to an incident should be to review the terms of all insurance policies, and notice should be promptly given, even if it is not clear that the insurance policy provides coverage.

5. Be alert when buying or renewing insurance

Anyone purchasing insurance is aware of the dramatic increase in the cost of insurance. Many insurance purchasers do not realize that the more expensive insurance generally provides less coverage than policies purchased a few years ago. For example, new insurance policies allow the insurers to reduce their policy limits by including defense costs as amounts that reduce the limits. And, insurers increasingly have eliminated occurrence-based coverage in favor of claims-made coverage. Claims-made coverage allows the insurers to minimize risk by limiting risk to claims occurring and made during the policy period, thus eliminating all future claims. Be sure to negotiate and review new and old insurance policies.

BUSINESS REORGANIZATION, BANKRUPTCY AND CREDITORS' RIGHTS

6. Understand the director's fiduciary duties to creditors

In a solvent corporation, director's fiduciary duties or care and loyalty do not extend to creditors. However, when a corporation is unable to pay its debts, or if the entity's debts are greater than its property at fair valuation, the duties of a director shift. When a shift from solvency to insolvency occurs, the director's fiduciary duties also shift from the shareholders to the creditors. An officer or director of an insolvent corporation has a duty to the corporation's creditors to be loyal and to act solely for the financial benefit of creditors. Directors must act cautiously to safeguard themselves against creditors' claims for breach of fiduciary duty. Directors should maintain board minutes and address the competing concerns among interested parties, providing explanations of all of the steps taken by the Board.

7. Avoid controversy over critical vendor orders

First day orders in a Chapter 11 bankruptcy may seek court authority to pay a portion or all of pre-petition claims of certain pre-petition creditors. These "critical vendors" are paid because the debtor relies on certain vendors for critical products and services. If a debtor is not permitted to pay its pre-petition debts to essential vendors, they would stop supplying the debtor, hampering the chance of a successful reorganization. To the extent possible, a vendor should utilize its leverage to convince the debtor to specifically name it as a critical vendor early in the bankruptcy. Vendors should use an agreement to provide post-petition goods and services on customary terms as an opportunity to extract a promise from the debtor that it will not assert certain preferences and pay some of its pre-petition claim.

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