Ed Nowogroski Insurance, Inc. v. Rucker: Is the Memory Rule Just a Thing of the Past

Rhonda DeVincent
Suffolk University Law School

Follow this and additional works at: https://dc.suffolk.edu/jtaa-suffolk

Part of the Litigation Commons

Recommended Citation
ED NOWOGROSKI INSURANCE, INC. V. RUCKER: IS THE MEMORY RULE JUST A THING OF THE PAST?

I. INTRODUCTION

As a general rule, an employee who has not signed an agreement not to compete is free to engage in competitive business upon leaving employment. The former employee may freely use general knowledge, skills, and experience acquired under his or her former employer in his new employment. Even without an enforceable covenant not to compete, however, the employee remains under a duty not to use or disclose trade secrets acquired in the course of previous employment to the detriment of the former employer. Many businesses invest a great deal of time and money in developing extensive customer lists, which are essentially compilations of market data to be used to gain a competitive advantage over other businesses. Businesses who make large investments in their trade secrets desire to protect their confidential information and will take the appropriate steps to pursue former employees who misappropriate valuable trade secrets.

There are contradictory social and economic policy considerations to consider in analyzing a trade secrets issue. On one hand, a business that has spent considerable amounts of money and time to develop trade secret

---

1 137 Wash. 2d 427, 437 (1999).
2 See id. at 437. The existence of a contract protecting trade secrets does not preclude separate cause of action in tort under provisions defining trade secrets. Id. Terms of a contract may be relevant, however, to such issues as existence of protectable trade secret or creation of a duty of confidence. Id.
3 Id.; see also RESTATEMENT OF TORTS, § 757 (b) (1939) (stating general matters of public knowledge or general industry knowledge cannot be appropriated as secret).
4 See RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 42 (1995); see also ROBERT P. MERGES ET AL., INTELLECTUAL PROPERTY IN THE NEW TECHNOLOGICAL AGE 107 (Aspen Law & Business 2000) (1997). To qualify for trade secret protection, information must not be generally known, must be valuable, and must not be disclosed. Id.
5 Henry J. Silberberg & Eric G. Lardiere, Eroding Protection of Customer Lists and Customer Information Under the Uniform Trade Secrets Act, 42 BUS. LAW 487, 487 (1987) (mentioning especially true in industries that depend on salespersons or customer contact to conduct business). Id.
6 See id. (stating massive volume of litigation concerning protection of customer information exists.)
advantages over its competitors should receive protection against the misappropriation of the information by a former employee who obtained the information while in a position of confidence and trust.\textsuperscript{8} On the other hand, an individual should be entitled to pursue the particular occupation that he or she chooses in a free society, even if the occupation is in the same industry as that of his or her former employer.\textsuperscript{9} This Note will address the trade secret protection that is afforded to customer lists and, more specifically, whether a customer list that is retained in an employee’s memory qualifies as a trade secret. The Note will focus on the recent decision in \textit{Ed Nowogrowki Insurance, Inc. v. Rucker},\textsuperscript{10} where the court rejected the “memory rule” of agency law and stated that it was inconsistent with promoting commercial ethics and fair dealing.\textsuperscript{11}

\section{II. ARE CUSTOMER LISTS PROTECTABLE AS TRADE SECRETS?}

A customer list can qualify as a protected trade secret if it meets the criteria of the Uniform Trade Secrets Act (“UTSA”).\textsuperscript{12} Forty-one states and the District of Columbia have adopted the UTSA.\textsuperscript{13} The UTSA was intended to “codify[y] the basic principles of common law trade secret protection.”\textsuperscript{14} After the UTSA was initially enacted in 1985, there was some uncertainty as to whether customer lists would continue to be trade secrets under the law because the definition of a trade secret did not specifically include customer lists.\textsuperscript{15} The case of \textit{American Paper &
Packaging Products v. Kirgan\(^\text{16}\) eliminated this concern, however, when the court held that customer lists could be considered a “compilation” and, therefore, a trade secret as defined by the UTSA.\(^\text{17}\)

Generally, any confidential information that gives one’s business a competitive advantage may constitute a legally protectable trade secret.\(^\text{18}\) Whether a customer list is protected as a trade secret depends on whether the information is not known or readily ascertainable and whether the information derives value from reasonable secrecy efforts.\(^\text{19}\) More particularly, courts consider the following factors in determining whether information constitutes a protectable trade secret: (1) the extent to which the information is known outside of the employer’s business; (2) the extent to which it is known by employees and others involved in the business; (3) the extent of measures taken by the employer to guard the secrecy of the information; (4) the value of the information to the employer and its competitors; (5) the amount of effort or money expended by the employer in developing the information; and (6) the ease or difficulty with which the information could be properly acquired or duplicated by others.\(^\text{20}\) No one factor is necessarily more determinative than the others, but if an employer cannot prove substantial investment in his or her compilation of customer information, he or she is not likely to prevail on a claim of trade secret misappropriation.\(^\text{21}\)

Trade secret protection does not generally extend to customer lists where the information is readily ascertainable.\(^\text{22}\) Whether customer information is generally known or readily ascertainable is a question of fact.\(^\text{23}\) An employee’s general familiarity with the information relating to

---

\(^{16}\) 183 Cal. App. 3d 1318 (1986).
\(^{17}\) Id. See also supra note 13 and accompanying text.
\(^{19}\) Nowogroski, 137 Wash. 2d at 435 (citing RCW 19.108.010 (4) (a), (b)).
\(^{20}\) RESTATEMENT (FIRST) OF TORTS, Comment (b) § 757 (1939).
\(^{22}\) Nowogroski, 137 Wash. 2d at 441 (citing Boeing, 108 Wash. 2d at 49-50); National Sch. Studios, Inc. v. Superior Photo Serv., Inc., 40 Wash.2d 263, 273 (1952) (stating no trade secret where customer’s identity well known or readily ascertainable); Jewett-Gorrie Ins. Agency, Inc. v. Visser, 12 Wash. App. 707 (1975) (permitting employee to solicit customers if readily ascertainable even if knowledge acquired working for ex-employer). See also Zoecon Industries v. American Stockman Tag Co., 713 F.2d 1174, 1179 (5th Cir. 1983) (stating customer lists of readily ascertainable names and addresses not protected as trade secrets); American Paper & Packaging Products, Inc. v. Kirgan, 183 Cal. App. 3d 1318, 1326 (1986) (concluding customer list not trade secret because comprised of information readily ascertainable to others in trade or business)
"the former employer's costs, prices, productivity, revenues, profits, products, customers, and suppliers" is typically classified as a matter which is generally known to a person involved with a business.\textsuperscript{24} Therefore, if prospective customers for a particular product or service are readily identifiable, their identities do not constitute a trade secret.\textsuperscript{25}

In contrast, specialized customer information that cannot be easily duplicated may be sufficiently valuable and secret to qualify as a trade secret.\textsuperscript{26} For example, in \textit{NCH Corporation v. Broyles},\textsuperscript{27} the plaintiff corporation produced route books to facilitate solicitation of orders for its employees.\textsuperscript{28} Each page of the route books was marked "confidential" and contained not only the customers' names and addresses but also the "identity of the person to be contacted at each customer's location, a detailed sales history revealing products purchased, the quantities purchased, the container sizes, the prices paid, and the frequency of purchases."\textsuperscript{29} The United States Court of Appeals for the Fifth Circuit held that the evidence supported the conclusion that the information was more extensive than what is "generally known or readily ascertainable," even though some of the information contained in the route books could be acquired from other sources.\textsuperscript{30}

III. HISTORY OF THE "MEMORY RULE" AND RECENT DEVELOPMENTS

The Second Restatement of Agency states, in pertinent part, "the agent is entitled to use general information concerning the method of business of the principal and the names of the customers retained in his memory, if not acquired in violation of his duty as agent."\textsuperscript{31} This is the so-called "memory rule."\textsuperscript{32} This rule implies that although an agent cannot use copies of written memoranda concerning the employer's customers in subsequent employment, he or she is not precluded from using the names of customers retained in his memory.\textsuperscript{33} Courts are more likely to conclude

\textsuperscript{24} Randall Scott Hetrick, \textit{Employee "Head Knowledge" and the Alabama Trade Secrets Act}, 47 ALA. L. REV. 513, 535 (1996); see also Stampede Tool Warehouse, Inc. v. May, 272 III. App. 3d 580, 587 (concluding employee's general knowledge not trade secret).

\textsuperscript{25} \textit{RESTATEMENT (THIRD) OF UNFAIR COMPETITION} §42 (f) (1995).

\textsuperscript{26} \textit{RESTATEMENT (THIRD) OF UNFAIR COMPETITION} §42 (f) (1995).

\textsuperscript{27} 749 F.2d 247, 247 (5th Cir. 1985).

\textsuperscript{28} \textit{Id.} at 249.

\textsuperscript{29} \textit{Id.} at 252.

\textsuperscript{30} \textit{Id.} (concluding former employee under duty not to use route book).

\textsuperscript{31} \textit{RESTATEMENT (SECOND) OF AGENCY} § 396(b) (1958).

\textsuperscript{32} See \textit{id.}

\textsuperscript{33} See \textit{id.} The Restatement refines its position by stating that it is unfair conduct to secure a position primarily for the purpose of ascertaining business methods of the
that particular information is a trade secret if the employee misappropriates some physical form of the information such as written blueprints, plans, or lists of customers. Although information retained in the employee’s memory may be less likely to be regarded as a trade secret absent evidence of intentional memorization, the inference is not conclusive.

Many courts have wrestled with the issue of whether a former employee who used memorized information misappropriated his former employer’s trade secrets. In Peace v. Conway, former employees of a hair replacement business used their memories to recreate employer’s customer lists and to solicit business from those customers. The employees did not take any documents or use property that belonged to the employer for contacting customers and non-compete covenants had not been executed. The Supreme Court of Virginia ruled that the employees did not use “improper methods” of interfering with their former employer’s hair replacement contracts. The court concluded that, “it is not unusual in the business world for an employee to leave his or her employment and to start a competing business”, and “inevitably customers of the former employer will desire to continue to deal with the former employee in the new business”.

Conversely, in Allen v. Johar, Inc., the Supreme Court of Arkansas ruled that a former employee’s solicitation of the customers of his former employer was prohibited under Arkansas Trade Secrets Law, even though the employee did not sign a written non-competition agreement and used only his memory to contact the customers.

employer for a competitor’s use or for the purpose of memorizing names, not as incidental to the employment, but primarily for later competition. Id.

See Restatement (Third) of Unfair Competition § 42 (1995) (stating that systematic attempts to memorize information will not insulate former employees from liability).

Id.

See supra notes 30-33.


Id.

Id.

Id. at 281.

Id. at 282.


See id. at 50. "Whether the customer information used was written down or memorized is immaterial, and the proper issue is whether information can be protected as a trade secret." Id. The court also stated, “customer lists that have been obtained through use of a business effort and the expenditure of time and money that are not readily ascertainable and are kept confidential are given protection as a trade secret.” Id. at 49. The dissenting justices held that a customer list should not be protected unless it is reduced to a writing. Id. at 52. The dissent also felt that the only practical step the employer can make to protect a list not in written form is to enter into a confidentiality agreement with the employee. Id.
Recent decisions indicate that courts are affording more trade secret protection to employers than they have in the past regarding a prior employee’s ability to solicit to former customers with which they have personal contacts.\textsuperscript{44} In \textit{Moss, Adams & Co. v. Shilling},\textsuperscript{45} a 1986 California case, the California Court of Appeals held that as a matter of law, employees of an accounting firm did not engage in unfair competition by using a company rolodex to acquire the addresses of clients of the firm for whom they had provided services, in order to mail those clients an announcement of the opening of their new firm.\textsuperscript{46} The court held that a former employee was permitted to do business with his or her former employer’s customers with whom he or she became personally acquainted and developed a business relationship while formerly employed.\textsuperscript{47} The court stated that the defendants could not be compelled to “wipe clean the slate of their memories.”\textsuperscript{48} The court’s reasoning in the \textit{Moss} case was subsequently questioned in \textit{Morlife, Inc. v. Perry},\textsuperscript{49} where the Court of Appeals stated that:

\textit{[t]here is no legitimate reason for characterizing differently the conduct of a former employee who uses customer information personally developed for the employer during the period of employment from the use of the very same information developed by a coworker who had no customer contact. Creating an artificial distinction between the conduct of these two employees under the rubric of commercial impracticality in not being able to “wipe clean” one former employee’s memory constitutes an unjustified abandonment of legitimate regulation of competitive activity, and ignores the paramount interest in protecting information meeting the definitional criteria of a trade secret.}\textsuperscript{50}

\textsuperscript{44} See NCH Corp. v. Broyles, 749 F.2d 247, 247 (5th Cir. 1985); see also American Credit Indemnity Co. v. Sacks, 213 Cal. App. 3d 622, 626-31 (1989) (holding former employee’s letter and subsequent phone calls announcing new employment a went beyond professional announcement and amounted to solicitation).

\textsuperscript{45} 179 Cal. App. 3d 124 (1986).

\textsuperscript{46} Id. at 126.

\textsuperscript{47} Id. at 129. See also Avocado Sales Co. v. Wyse, 122 Cal. App. 627, 634 (1932) (stating lawful for salesman to sell avocados to retail customers whom salesman had serviced for former employer); Theodore v. Williams, 44 Cal. App. 3d 34, 37-9 (1919) (stating lawful for driver to announce new employer by driving along old route in truck marked with his name and new employer’s name). \textit{But see Klamath-Orleans Lumber, Inc. v. Miller, 87 Cal. App. 3d 458, 462-66, (1978) (stating use by memory of extensive customer list to permit selective solicitation held unfair competition).}

\textsuperscript{48} Moss, 179 Cal. App. 3d at 124 (1986).

\textsuperscript{49} 55 Cal. App. 4th 1514, 1514 (1997).

\textsuperscript{50} Id. at 1526.
IV. ED NOWOGROSKI INSURANCE, INC. V. RUCKER

In *Ed Nowogroski Insurance, Inc. v. Rucker*, the Supreme Court of Washington considered the issue of whether information that meets the UTSA definition of a trade secret loses its protection because it has been memorized rather than taken in written form. Ed Nowogroski Insurance, Inc. accused its former employees Rucker, Rieck, and Kiser of misappropriating the company's trade secrets by keeping and using confidential client lists and other information. Rieck testified that he was familiar enough with his top fifty clients that he did not need summaries or other aids to solicit business because he had memorized the customers' personal information. The plaintiff argued that the form of information was irrelevant and that the defendant employee should be liable for misappropriation of the customer lists whether written or memorized. The trial court found that Reick, Kiser, and Rucker violated the UTSA because they misappropriated their employer's trade secrets either by taking or refusing to return summaries of insurance, company records, and other confidential information. The court, however, concluded that the plaintiff would not recover additional damages for the memorized information because an employee does not violate the UTSA by using information from his head to solicit business from his former employer. The Washington Court of Appeals held that there was no legal distinction between written and memorized information under the Washington UTSA, and said that the Act focuses on the nature of the information and not the form in which it exists. The defendants appealed.

The Washington Supreme Court noted that there is a split of authority among the jurisdictions on the issue but stressed that the trend seems to be that it is the character of the information—not the manner of its appropriation—that determines whether the customer list is a trade secret. In reversing the trial court's decision, the Washington Supreme Court cited Callman's treatise on unfair competition, in which the author cited cases

---

51 *Nowogroski*, 137 Wash. 2d at 436 (stating question of law dependent on interpretation of statute and, thus, subject to de novo review).
52 *See id.* at 429.
53 *See id.* at 433.
54 *See id.* at 434.
55 *Id.* at 432-34.
56 *See Nowogroski*, 137 Wash.2d at 435.
57 *See id.* at 941.
58 *See id.*
60 Callman, Rudolf, *The Law of Unfair Competition, Trademarks, & Monopolies*, 4th
holding that the modern trend is to eliminate the distinction between written and memorized information. Rudolf Callman recognized that many older cases drew a distinction between written customer lists and those committed to memory but stated that the distinction between written and memorized information should not be encouraged. The Washington Supreme Court concluded that the form of information, whether written or memorized, is immaterial under the UTSA.

V. DAMAGES FOR TRADE SECRET MISAPPROPRIATION

Injunctive relief is one form of damages that employers often seek when alleging that a former employee has misappropriated their trade secret. Generally an injunction should only last as long as is necessary to eliminate the commercial advantage that an ex-employee would obtain through trade secret misappropriation. An injunction should terminate when the trade secret becomes known to competitors. Therefore, an injunction should not be issued if the trade secret is no longer truly a secret and is known by competitors. The Uniform Trade Secrets Act also provides for damages for trade secret misappropriation and for attorneys' fees if bad faith can be proven.

---

61 Nowogroski, 137 Wash.2d at 448.
62 Id. (stating form of information and manner in which obtained unimportant). The nature of the relationship and the employee’s conduct should be determinative factors. Id.
63 Id. at 449. The court stated, “whether the information is on a CD, a blueprint, a film, a recording, a hard paper copy or memorized by the employee, the inquiry is whether it meets the definition of a trade secret under the Act and whether it was misappropriated.” Id.
66 Id.
67 Id.
68 Uniform Trade Secrets Act, § 3-4. Damages can include both the actual loss caused by misappropriation and the unjust enrichment caused by misappropriation that is not taken into account in computing actual loss. Id. If willful and malicious misappropriation exists, the court may award exemplary damages in an amount not exceeding twice any award made under subsection (a). U.T.S.A. § 3. If (i) a claim of misappropriation is made in bad faith, (ii) a motion to terminate an injunction is made or resisted in bad faith, or (iii) willful and malicious misappropriation exists, the court may award reasonable attorney's fees to the prevailing party. U.T.S.A. § 4.
VI. CONCLUSION

The requirement that a former employee misappropriate a physical object before there can be the misappropriation of a customer list is becoming obsolete. Recent court decisions clearly indicate that the trend is to eliminate the distinction between a customer list committed to memory and one that is physically taken. Using memorization to rebuild a trade secret does not transform that trade secret from confidential information into non-confidential information. It should not make a difference whether the employee has possession of a physical list or has committed the list to memory because the result is the same: trade secret misappropriation. The “memory rule” may truly become just a memory, and the courts should adhere to the logical conclusion that it is possible for a customer list to be misappropriated through memorization alone.

Rhonda DeVincenct

---


70 See e.g. Nowogroski, 137 Wash.2d at 448 (explaining that Uniform Trade Secrets Act does not distinguish between written and memorized information); Allen, 308 Ark. 45, (1992) (holding immaterial distinction between written and memorized customer information), Morlife, 56 Cal. App. 4th at 1526 (1997) (holding view that former employee should not be compelled to wipe clean slate of memory not legitimate). Id.

71 See Stampede, 272 Ill.App.3d at 590 (physical appropriation not required for misappropriation of customer list). Id.