Global Strategic Collaboration: Trade Secrets and Firm Value

Evan A. Peterson¹

¹ Department of Management, University of Detroit Mercy, Detroit, USA

Correspondence: Evan A. Peterson, Department of Management, University of Detroit Mercy, 4001 W. McNichols Road, Detroit, MI 48221, USA. E-mail: evan.peterson4545@yahoo.com

Received: May 7, 2012   Accepted: May 29, 2012   Online Published: June 4, 2012

doi:10.5539/jms.v2n2p178   URL: http://dx.doi.org/10.5539/jms.v2n2p178

Abstract

Intellectual property is gaining increased recognition as one of the most important organizational assets in the highly competitive global marketplace. As companies struggle to seize value from intellectual property, technological advances have prompted the formation of strategic partnerships between companies seeking to exploit unique intellectual assets. However, scholars have paid relatively little attention to the risks involved with intellectual property collaboration, given that relationships may be formed with organizations based in countries that have traditionally ignored intellectual property laws. Despite past advancements protecting intellectual property rights across the globe, the continued lack of effective enforcement remains cause for concern for organizations doing business abroad. Consequently, my primary motivation is to highlight the significance and severity of this issue, in order to guide future research and practice on the capacities necessary to develop effective collaborative relationships on a global scale. Based on emerging legal trends, I propose that U.S. organizations can reduce the anxieties associated with sharing intellectual property abroad by lobbying for increased extraterritorial application of domestic trade secret laws, employing contractual agreements with heightened protections, and championing the importance of intellectual property protections to overseas strategic partners.

Keywords: collaboration, competitive advantage, intellectual property, law, trade secrets

1. Introduction

As modern organizations face an increasingly convoluted and global business environment, there is increasing acknowledgment that intellectual property is one of the most valuable organizational assets (Rivette and Kline, 2000). Paralleling the rise in importance of technological assets, as a result of widespread global infringement, the business community is also witnessing dramatic increases in the amount of litigation (Daly, 2010), particularly in the arena of trade secret disputes and piracy concerns (Almeling et al., 2010; Almeling et al., 2011). For example, estimates indicate that annual losses to the U.S. motion picture industry from global piracy are nearly $20.5 billion (Siwek, 2006). Similarly, Proctor and Gamble estimates that 10–15% of its annual revenue in China is lost to counterfeit products (Economist, 2003). In the wake of globalization, organizations are faced with the increasingly arduous task of delivering innovation while keeping that innovation safe from competitors.

The critical role of trade secrets in shaping organizational capabilities and competitiveness has been documented by strategic researchers for years. Bird and Jain (2008) and Schwarts and Weil (2010) revealed that trade secrets encompass nearly 75% of the value of intellectual assets. Similarly, Prahalad and Ramaswamy (2000) argued that modern value is derived from experience networks created by companies working in unison, and is no longer determined by the efforts of any single firm. Moreover, scholars have argued that greater organizational success can be attained by fashioning collaborative relationships with market participants that strategically pool and exploit unique intellectual assets (Prahalad and Krishnan, 2008; Phelps and Kline, 2009; Siedel and Haapio, 2010). Given the fundamental responsibility played by innovation in overall growth and sustainability, intellectual property collaboration has been identified as a necessary factor in seizing value from innovation (Pisano and Teece, 2007).

However, scholars have paid relatively little theoretical attention to how intellectual collaboration is affected by the pervasive levels of infringement and piracy found in certain parts of the developing world. Consequently, my primary motivation is to conduct a comprehensive analysis that may guide future research and practice on the
capacities necessary to develop effective collaborative relationships on a global scale. An understanding of the unique circumstances surrounding trade secret protections within an overall collaborative strategic framework will help pinpoint what measures can be taken to protect trade secret confidentiality on an international scale, while fostering the spirit of collaboration that is emerging as a new route to competitive advantage.

2. Literature Review

2.1 Trade Secrets

Trade secret laws are designed to protect valuable and sensitive information from unfair competition and industrial espionage (Halan, 2004; Hannah, 2007; Jameson, 2011). Under the Uniform Trade Secrets Act (UTSA) of 1985, a trade secret is defined as information, including a formula, pattern, compilation, program device, method, technique, or process, that satisfies two requirements. First, it must derive independent economic value from not being generally known, or readily ascertainable by proper means, to other persons who can obtain economic value from its disclosure or use. Second, it must be the subject of efforts that are reasonable under the circumstances to maintain its secrecy. This definition has been widely enacted in practice within the United States (Frankel, 2012) and is analogous to definitions employed at the international level (World Trade Organization, 1994).

Under this broad designation, virtually any information that may have value to an organization can qualify as a trade secret (Levine, 2007; Frankel, 2012). For example, customer lists (American Family, 2007), pricing, distribution and marketing plans, market analysis information and sales data (Johnson Controls, 2004), drawings, specifications, and chemical formulas (Ctr. for Auto Safety, 2000) are all protectable trade secrets. Even negative information, such as information about failed experiments, products, or procedures, can qualify as a trade secret (Morton, 1993; Bar-Gill and Parchomovsky, 2009). However, as noted above, in order to qualify as a trade secret, confidential information must also derive value from its secrecy (Holmes, 2011; Frankel, 2012), either by enhancing the trade secret owner’s competitive position or by diminishing the capacity of other firms to compete effectively against the information holder (Halligan and Weynand, 2006).

A key vulnerability of trade secrets is that organizations must take appropriate measures to preserve their secrecy (Hannah, 2005). The determination of whether the owners of trade secrets have taken reasonable efforts to maintain secrecy turns on a case-by-case examination (Frankel, 2012). Organizations frequently implement a variety of measures designed to protect their trade secrets, such as storing trade secrets in rooms protected by special locks and alarm systems, restricting access to individuals with a need to know, and informing individuals who work with trade secrets that the information that must be kept confidential. Additionally, employees and third parties that have access to trade secrets are alerted to the confidential nature through personnel manuals, confidentiality stamps, and posted warnings. Moreover, organizational policies and informational sessions continuously emphasize company policies prohibiting the disclosure of trade secret information through display, publication, and advertising (Halligan and Weynand, 2006; Schwartsand Weil, 2010).

However, recent surges in communications technology, along with increased employee mobility and market globalization, have forced companies to reevaluate the effectiveness of these and other protective measures (Gabel and Mansfield, 2003; Halligan and Weynand, 2006). As noted above, once trade secrets become public, their protected status vanishes permanently and cannot be regained (Frankel, 2012). In the next section, I will outline these developments and their resulting effects in greater detail.

2.2 Trade Secrets in the Technology Age

While organizations have always faced the possible disclosure of confidential information, today’s business environment increases that risk dramatically (Matwyshyn, 2004), as technology can facilitate the complete and utter ruin of priceless trade secrets in a matter of moments (Rowe, 2007). For example, with over fifty percent of all households connected to the internet (Park, 2004), it has become an integral part of daily life, connecting over 800 million people to a global information network (Nguyen and Maine, 2004). As of June 2011, Google ranked Facebook as the most commonly visited website on the internet (Google, 2011), with over 900 million active users (Facebook, 2012). Similarly, LinkedIn boasts more than 120 million worldwide users (LinkedIn, 2011). As social media is increasingly being used to network with professionals, recruit new employees, and stimulate consumer purchasing (Meister and Willyerd, 2010), social media can have a profound effect on the safeguarding of trade secretsand the coverage of non-compete agreements (Warren and Pedowitz, 2011).

The rise in social media has accompanied a veritable migration of personal and professional information from virtual obscurity to the public light. Company insiders now find themselves with the capability to disseminate confidential information, on subjects ranging from new product development and internal sales figures to
upcoming layoffs and court litigation strategies (Warren and Pedowitz, 2011), to limitless amounts of people. While employees may not necessarily use social media to overtly post confidential information, having contact lists easily accessible on social networking sites could lead to the unwitting disclosure of sensitive customer information and the erosion of trade secrets (Warren and Pedowitz, 2011).

Reflecting on this shifting nature of technology, courts have voiced their concerns that internet users can instantaneously extinguish valuable intellectual property rights by posting them online (Religious Technology Center, 1995). As a result, there have been significant governmental efforts in numerous jurisdictions to modify trade secret and other technology sensitive laws (Milligan, 2012). For example, at the national level, the federal government is devoting amplified resources to forestalling trade secret theft, including the establishment of advisory committees and the formation of an Intellectual Property Task Force (Holmes, 2011). Organizations are cautioned that previous devices used to preserve confidentiality may no longer be sustainable. As technological advances have changed the way the law examines trade secret protections, increased efforts are being made to move towards intellectual property collaboration.

2.3 Toward a Collaborative View of Trade Secrets

Technological development raises important questions and concerns regarding how organizations can deliver value in the dynamic context of the modern global economy (Teece, 2010). While some champion innovation as they key to growth and sustainability, there is no assurance that innovators will be able to reap the fruits of their labors (Pisano and Teece, 2007). The benefits of innovation can be siphoned off by imitators or suppliers of complementary products. In addition, innovators must also be mindful of the trade barriers posed by legal protections and the investments in complementary assets made by their competitors (Pisano and Teece, 2007). Value is no longer individually determined by any lone organization. Instead, it is shaped by associations of firms working together to create experience networks (Prahalad and Ramaswamy, 2000). As noted by Pisano and Teece (2007), the test is “not just creating value from innovation, but capturing that value as well.”

A comprehensive understanding of the principles of intellectual property law and practical knowledge surrounding its business applications is paramount for organizations wishing to achieve a sustained competitive advantage. Such wisdom assists organizations in pursuing strategic decision-making and prevents the inadvertent transgression upon the intangible assets of competing organizations (Siedel and Haapio, 2010). Based on its fundamental contribution to competitive effectiveness and overall profitability (Bird and Jain, 2008), intellectual property occupies a key role in the heart of organizational strategic development (Blaxill and Eckardt, 2009; Siedel and Haapio, 2010). However, based on the diversity, complexity, and sheer dimensions of today’s global marketplace, few organizations remain capable of amassing all the necessary resources and business competencies essential to long-term survival. As a result, increased momentum is building behind the concept that companies can achieve greater success by using their intellectual assets to build collaborative relationships with other key market participants (Prahalad and Krishnan, 2008; Phelps and Kline, 2009; Siedel and Haapio, 2010).

The design and collaborative application of intellectual property is a key force behind the innovation process. Collaboration facilitates rapid and comprehensive market distribution, delivers guidelines for pursuing joint projects with other market leaders, streamlines market entry, and generates revenue through intellectual property licensing (Phelps and Kline, 2009). Organizations that strengthen and develop their intellectual resources through coordinated, cross-departmental efforts can generate profits by licensing intellectual property and forming joint ventures with other organizations, thereby maximizing intellectual property value creation (Siedel and Haapio, 2010).

2.4 Global Issues and Trade Secret Valuation

As trade secrets can be a source of competitive advantage only if they are unknown outside the organizations that own them (Dorr and Munch, 1995; Hannah, 2005), the secrecy component of trade secrets diminishes their practical value (Bar-Gill and Parchomovsky, 2009). The economic value of a discovered trade secret is zero, as companies risk forfeiture of trade secret rights and the associated capital investment when competitors acquire access to the protected information and legally appropriate it for their own ends (Hannah, 2005; Halligan and Weynand, 2006). Concerns posed by potential trade secret disclosure are further intensified when business relationships transcend national boundaries. As noted by the World Intellectual Property Organization, existing trade secret protection measures are relatively weak in certain parts of the world. There are indications that apathy towards infringement and piracy of trade secrets, patents, and copyrights is pervasive outside of the world’s developed economies (Petherbridge, 2001; Pisano and Teece, 2007).
Conventions and treaties at the international level set forth guidelines for the uniform protection of intellectual property rights (August, Mayer, and Bixby, 2009). For example, the Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS), the most prominent and important international accord in the area of intellectual property (Reichman, 1996), is binding on all members of the World Trade Organization (WTO) and enforceable through WTO dispute settlement procedures. Although TRIPS works to diminish impediments to international trade through suitable protection of intellectual property rights, it affords states great flexibility in designing their own domestic protection regimes (Segal, 2006).

While the international community endlessly works towards establishing international norms for the protection of intellectual property, mixed results indicate that the road remains a difficult one (August, Mayer, and Bixby, 2009). For example, China, a country notorious for intellectual property infringement, has made substantial efforts in recent years to strengthen domestic laws that facilitate the protection of technological assets (Weinstein, 2009). For example, China, a country notorious for intellectual property infringement, has made substantial efforts in recent years to strengthen domestic laws that facilitate the protection of technological assets (Weinstein, 2009). While some scholars and policymakers are encouraged by such efforts (Yu, 2000; Yu, 2006), critics accuse the Chinese government of continuing to lag behind in the enforcement of these legal measures (WTO, 2009). Concerned by this lack of effective implementation, U.S. Trade Representatives have stated that China will remain on the Priority Watch List, subject to continual monitoring (Beane, 2000).

3. The Effectiveness of Collaborative Strategy

As existing literature indicates, scholars are taking an increased interest in the collaborative use of intellectual property as a central driver of innovation. However, despite the potential engendered by this movement, trade secrets, unlike other forms of intellectual property, present unique challenges for a collaborative strategy. As trade secrets derive their value from secrecy, it’s necessary to consider how they can effectively fit into the overall scheme of marshaling resources to exploit intellectual property examined by Prahalad and Krishnan (2008), Siedel and Haapio (2010), and other scholars. Given the global nature of modern business, U.S. organizations are forced to execute collaborative strategies that include alliances with companies based in parts of the world that have traditionally failed to respect intellectual property rights. As evidenced by the above discussion, efforts to rectify this deficiency have met with mixed results. The question becomes what can U.S. companies do to adequately protect trade secret confidentiality on an international scale, while fostering the spirit of collaboration that is emerging as the new route to competitive advantage?

Despite all the advancements to protect intellectual assets in other parts of the world, the continued lack of effective enforcement continues to trouble U.S. organizations doing business abroad. However, there are steps that can be taken to mitigate the risks associated with pursuing a collaborative strategy. The following recommendations are designed to help companies manage trade secret disclosure risk as well as to pave the way for increased cooperation regarding the protection of trade secrets across the globe.

3.1 Extraterrestrial Application of U.S. Trade Secret Law

The International Trade Commission (ITC) is a quasi-judicial Federal agency with authority to scrutinize and adjudicate disputes concerning imports that allegedly disregard intellectual property rights (USITC, 2012). Under Section 337 of the Tariff Act of 1930, the ITC has the ability to investigate allegations of trade secret misappropriation involving goods imported into the U.S. (19 USC sec 1337(a)(1)(A)). Out of respect for the sovereignty of foreign states, American courts have traditionally neglected to exercise jurisdiction over foreign defendants, except in very limited cases where the conduct at issue occurred within the U.S. (Morrison, 2008). As such, federal courts have traditionally not addressed whether Section 337 authorizes the ITC to apply domestic law in situations where trade secrets, misappropriated abroad, become connected to goods that are later imported into the U.S. (Strapp, 2011). However, the recent decision in TianRui Group Company v. International Trade Commission (2011 WL 4793148 (Fed Cir)) significantly expanded ITC authority to protect domestic industries by establishing that Section 337 does apply to instances where the misappropriation occurs overseas (Strapp, 2011).

The ruling enhances the negotiating position of organizations wishing to share trade secrets abroad (Strapp, 2011), as foreign defendants accused of impropriety can now more easily find themselves before U.S. courts. TianRui may be the long awaited catalyst that can pave the way for increased efforts by the U.S. government to better protect the intellectual property rights of its domestic industries overseas. Influence oriented strategies are characterized by attempts to proactively influence the consumer public, legislators, and administrative agencies responsible for shaping industry regulatory structures (Watkins, Edwards, and Thakrar 2001; Gardner, 2003) by proposing favorable rules, lobbying, and engaging in other strategic-minded activities (Hillman and Hitt 1999;
U.S. firms may now find greater receptivity in their lobbying efforts urging the government to:

- Extraterritorially apply more laws that directly or indirectly support the protection of U.S. intellectual property interests.
- Reduce the legal threshold necessary to bring foreign defendants before U.S. courts.
- Broaden the scope of liability to more readily include host governments that turn a blind eye toward violations.

3.2 Increased Potency of Contractual Agreements

Common measures employed to protect trade secrets include confidentiality, non-disclosure, and non-compete agreements. Non-disclosure agreements forbid employees from divulging proprietary secrets outside of the company, and are generally enforced by the courts (Sherwood, 2008). Likewise, non-compete agreements, which limit the ability of former employees to work for a company’s competitors, are being implemented with increased frequency (Nicandri, 2011). These agreements habitually include choice-of-law provisions that solidify the application of U.S. law and the jurisdiction of U.S. courts in the event of a legal dispute between parties residing in different countries.

Despite recent legal developments, such as TianRui, that make it easier to haul foreign defendants before U.S. courts, injured firms may choose to avoid jurisdictional problems and seek their remedies directly in foreign courts. Traditionally, attempts by domestic organizations to bring suit in foreign courts have met with limited success. However, in recent years developed nations have activated diverse strategies linking the reform of intellectual property rights directly to international trade policy (Gadbaw, 1989). For example, section 301 of the U.S. Omnibus Trade and Competitiveness Act of 1988 (“Special 301” or “Super 301”), grants the U.S. government the ability to impose tariffs and trade sanctions against countries that refuse to control violations of intellectual property laws (Sykes, 1990; Lopez-Velarde, 1994; Sell, 2003). As a result, U.S. firms can lobby the government to exercise its powers under Section 301 to:

- Request foreign governments promote a greater respect for intellectual property rights and contracts upholding their protection.
- Pressure foreign courts to allow easier access to overseas plaintiffs.
- Condition foreign aid on the success rate of efforts by foreign governments to control and prevent violations of intellectual property rights.
- Imposes greater trade sanctions and tariffs on foreign governments that fail to take efforts to protect intellectual property rights.

3.3 Improved Recognition of the Value of Intellectual Property

Segments of the academic and legal communities assert that the lack of respect for intellectual property rights in certain parts of the world is fundamentally based on an insufficient understanding of the rights’ importance to the business community (Segal, 2006). Innovators may more easily capture value from innovation by advocating for the importance of increased intellectual property protection on a global scale (Pisano and Teece, 2007). Recent examples have demonstrated that the domestic economies of countries that respect intellectual property rights are healthier than the domestic economies of countries that do not respect such rights. For instance, Japan has traditionally disregarded intellectual property rights (Beane, 2000; Tessensohn, 2007). However, after domestic industries suffered due to surges in counterfeit products from China and other Asian countries during the late 1990s (Asahi, 2004), the Japanese government dramatically altered its view (Arai, 2004), in an effort to turn Japan into an “intellectual-property based nation” (Tessensohn, 2007). As the foundation of these successful reforms was based in no small measure on the lobbying efforts of Japanese industries (Asahi, 2004), this example illustrates the potential power of company pressures on legislative action (Bullock, 2000). As such, U.S. organizations can:

- Urge key overseas strategic partners to lobby their own governments for reform of intellectual property laws.
- Maintain business relationships only with companies that have demonstrated a longstanding commitment to the respect of intellectual property.
4. Conclusion

Modern organizations continue to face difficulties in safeguarding and seizing the value from intellectual property assets. As technological advances and globalization continue to transform the business environment, increased efforts are being devoted towards researching intellectual property collaboration. Specifically, scholars are investigating how value creation can be attained through fashioning collaborative relationships with key market participants that strategically combine and exploit unique intellectual assets. However, relatively little focus has gone into examining how such strategies are influenced and affected by apathetic views towards intellectual property laws. Given trade secret value is derived from secrecy, there are legitimate concerns that partnerships with companies in parts of the world that ignore intellectual property rights may be a recipe for disaster. Despite numerous advancements protecting such rights across the globe, including those in countries known for past violations, the continued lack of effective enforcement continues to distress organizations doing business abroad. Consequently, my primary motivation was to conduct further analysis and examination into this issue, in order to guide future research and practice on the capacities necessary to develop effective collaborative relationships on a global scale. Based on emerging legal trends, U.S. organizations can reduce the anxieties associated with sharing intellectual property abroad by lobbying for increased extraterritorial application of domestic trade secret laws, employing contractual agreements with heightened protections, and championing the importance of intellectual property protections to overseas strategic partners.

References


Uniform Trade Secrets Act (UTSA) of 1985.


