

## TRADE SECRETS<sup>1</sup>

Until recently, hydraulic fracturing<sup>2</sup> has been prohibited in North Carolina. The ban on fracking was lifted in 2012.<sup>3</sup> The Department of Environment and Natural Resources (DENR) has been tasked by the legislature to create the rules for regulating and overseeing the future of fracking operations in North Carolina.<sup>4</sup> The Mining and Energy Commission (MEC), previously known as the Mining Commission, was delegated the authority to research and write the proposal for the laws on fracking.<sup>5</sup> One of the most contentious issues, and the focus of this report, is the trade secrets exception to the mandatory disclosure rules that are currently under consideration.

### **I. Fracking**

#### *A. The process*

The process of fracking is a new way of collecting natural gas from shale deposits. This is performed by drilling a vertical well deep enough to reach the shale deposits and then leveling the well path almost horizontally.<sup>6</sup> High volumes of fracking fluid are then injected into the well at high pressure in order to create fissures in the horizontal part of the well.<sup>7</sup> The fissures in the shale deposits create pathways for the gas trapped inside the shale deposits to travel to out. The composition of the fracking fluid is the base, additives and proppants. The base is usually water,

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<sup>1</sup> This report was last updated on August 1, 2013, the information following will only be as current as of that date.

<sup>2</sup> Also referred to as “fracking,” which is the term that will be used throughout this report.

<sup>3</sup> S.B. 76, 2013 Leg., 2013 Sess. (N.C. 2013).

<sup>4</sup> S.B. 820, 2012 Leg., 2012 Sess. (N.C. 2012).

<sup>5</sup> *Ibid.*

<sup>6</sup> George E. King, “Hydraulic Fracturing 101: What Every Representative, Environmentalist, Regulator, Reporter, Investor, University Researcher, Neighbor and Engineer Should Know About Estimating Frac Risk and Improving Frac Performance in Unconventional Gas and Oil Wells” (SPE Hydraulic Fracturing Conference, 2012): 3.

<sup>7</sup> *Ibid.*

although oil or diesel has been used as well. The additives are variations of chemicals that alter the fluid to make it more effective. The formulaic combination of the fracking fluid determines the profit ability of the operation because it can enhance the efficiency of the process. The chemical combination would vary the most from company to company and is the valued component of the operation. The proppants are usually some kind of sand or a synthetic mixture of granular substance (such as ceramic proppants). They prop open and keep open the fissures allowing the gas to escape and be collected. Fracking is different from other methods of obtaining gases because of the depth of its wells, the amount of water and the mixture it utilizes.

### *B. The actors*

There are several steps in the venture of fracking and multiple actors in each. It is important to consider and understand the hierarchy of the industry in order to be able to regulate it effectively. Several of the actors might be combined into one company that is large enough to fulfill several steps on its own, but for the purposes of clear and rigid regulation, they should be categorized uniformly and the multiple-function actors should comply according to their function at the time. The main functions to keep in mind is who is responsible and liable for the possible shortcomings of the operation, how the issuing of permits should be dependent on that, whether it is possible to shift the liability, and who can assert privileges or exceptions within this framework.

Ordinarily, finances and coordinates the entire project. However, it is the involvement of everyone else that has to be considered in order not to obscure or create loopholes for disclosure or liability purposes. The actors would be the drillers of the well, the producers of chemicals (this might be a long chain or combination of actors), the transporters of chemicals, the operators of the well (who would create the appropriate mixture and oversee the operation of the well), and

the cleaning-up operation (which could be delegated to a third party). Throughout all of these steps, there are likely multiple actors involved and it is essential that the liability is clearly defined and communicated to the parties. Specifically for trade secrets, it is important to establish who has the ability to claim the trade secret protection and under what circumstances. It is likely that the manufacturer will be unwilling to disclose that information to the operator. That would be problematic because technically the state would only be dealing with the operator and would not likely acquire authority over the manufacturer to disclose the chemicals used. The state would be limited to the authority it would have over the permit-holder, who would probably be liable for the operation. Mandating disclosures in this case, especially as conditional permitting, would be an unworkable scheme if manufacturers were frequently uncooperative. It would be impossible for the operator to comply with such an order. There has to be a provision that extends the authority of the state in order to acquire the disclosures directly from the source or a rule in place that would help the operator to acquire that information. This is necessary to ensure that trade secrets remain a viable option as a protection.

## **II. Trade secrets**

### *A. Definition*

The accepted definition of a trade secret comes from the Torts Restatement:

A trade secret may consist of any formula, pattern, device or compilation of information which is used in one's business, and which gives him an opportunity to obtain an advantage over competitors who do not know or use it. It may be a formula for a chemical compound, a process of manufacturing, treating or preserving materials, a pattern for a machine or other device, or a list of customers.<sup>8</sup>

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<sup>8</sup> *Restatement of the Law Third, Torts, Liability for Physical and Emotional Harm* (St. Paul, MN: American Law Institute Publishers, 2010): § 757.

A common example is the Coca-Cola formula. It is not patented or copyrighted and is liable to reverse engineering, but it is not commonly known or available. The company protects the secrecy of the formula in order to retain the trade secret protection. Because it is a trade secret, reverse engineering is allowed. Reverse engineering is the process of taking the finished product, in this case that would be the drink, and attempting to figure out the formula by separating it into its components. This is not part of the protection of a trade secret and if someone were to arrive at the formula by this process, it would not be considered as a cause for a suit in damages.

The qualifications for a trade secret are generally separated into three categories: (1) the trade secret qualifies under the broad parameters, (2) it is not commonly known and the possessor takes reasonable steps to keep it secret, and (3) it grants competitive (economic) advantage to the possessor by remaining secret.<sup>9</sup> These three elements have to be proven in order for the trade secret protection to be granted. The evaluation of those criteria rely on six elements: (1) the extent to which the information is known outside the claimant'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 claimant to guard the secrecy of the information, (4) the value of the information to the business and its competitors, (5) the amount of effort or money expended by the business in developing the information, and (6) the ease or difficulty with which the information could be properly acquired or duplicated by others.<sup>10</sup> The six factors are evaluated holistically in determining whether it is a trade secret and should be protected. The first two factors speak to the secrecy of the information overall. Because the trade secret protection is not exclusive, multiple

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<sup>9</sup> Steven N. S. Cheung, "Property Rights in Trade Secrets," (*Economic Inquiry* 20.1, 1982): 42-43.

<sup>10</sup> *Restatement of Torts*, § 757, comment b.

competitors can use the same secret in their process and maintain the secrecy requirement. The number of employees that have access to the knowledge of the secret will partly determine how secret it is and partly reflect the steps that the employer has taken to keep it secret. The third factor speaks to the employer's attempt to guard the information. The last three categories are directly related to the economic benefits of the secret in the cost-benefit analysis from the business point of view. The balance of these considerations will determine whether the trade secret exists and should be protected by law.

*B. Difference between a patent and a trade secret*

The main differences between a trade secret and a patent lie in the kind of material that can be protected and the extent of the protection. The protection of a patent is very specifically limited in scope, extends only for twenty years and the patented material is made public with its grant. Trade secret protection covers a broad range of materials, is indefinite, and remains secret.

The qualifications for a trade secret are described above. The vague definition of a trade secret leaves it very open to what can constitute a trade secret. This will range from something as specific and tangible as a chemical formula to something as broad as a customer list.

The qualifications for a patent are very different. The scope of what is a patent is generally limited to an invention or a manufacturing process – it has to be useful, novel and non-obvious (as the most basic requirements).<sup>11</sup> The patents are protected for twenty years and are made public once patented.<sup>12</sup> Patents were generally instituted and encouraged in order to incentivize research and then public disclosure in order for the researchers and developers not to

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<sup>11</sup> 35 USC. Sec. 112 (2012).

<sup>12</sup> Ibid.

be working on the same product that has already been invented.<sup>13</sup> By making it public and granting monopoly to the inventor, the inventor was incentivized and would receive royalties from the invention once it is public. This is commonly seen and used in the pharmaceutical market, where they get market power for the invention of the drug. Compulsory patenting generally does not happen outside of defense inventions.

Patents are exclusive to the company that holds the patent and any other company wishing to use it will have to negotiate a royalty fee or some kind of payment system. Once the patent is granted, the composition of it becomes public record and reverse engineering is no longer needed or possible. Both of these are not true of trade secrets. Trade secrets are not exclusive within the industry nor are they made public at any point.<sup>14</sup> Partly because of that, reverse engineering is allowed and acceptable in that sphere.

Perhaps the best illustration of the differences is a customer list.<sup>15</sup> It is not patentable, and logically, even if it were, it would lose its value once it is made public despite the patent. The time limit of twenty years would also be useless to the company. As a trade secret, on the other hand, it qualifies under the broad definition, it keeps the protection indefinitely and its usefulness stems from its secrecy. While the other companies are still able to contact the customers from the list and work with them, if the list itself was stolen or improperly sold to a competitor, the company could recover for that breach under the trade secret protection.

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<sup>13</sup> David D. Friedman, William M. Landes and Richard A. Posner, "Some Economics of Trade Secret Law," (*The Journal of Economic Perspectives* 5.1, 1991): 63-64.

<sup>14</sup> John J. Mahon, Jr., "Trade Secrets and Patents Compared," (*Journal of the Patent Office Society* 50.8, 1968): 542-43.

<sup>15</sup> Friedman, "Some Economics of Trade Secret Law," 61.

### *C. Trade Secrets: Status*

Trade secrets are a fluid concept in the sphere of law. They are a vestige of the common law and have not been codified (adapted into law through a statute).<sup>16</sup> The most common usage of a trade secret is an unpublished copyright work or a pending patent invention.<sup>17</sup> Trade secrets are employed for practical and efficient reasons. During the process of research, it is unfeasible to patent every single step along the way nor are all of the ideas patentable. In the process of the application for a patent, the applicant is treading the line of revealing enough information to qualify for a patent without revealing all of the information in order to protect the invention as much as possible. If the applicant is unsuccessful, either due to his stinginess with information or the type of material to be patented, he retains the trade secret protection for that invention.<sup>18</sup>

Generally, the claim for a trade secret protection will come after the secret has been used by another and the suit will be for misappropriation. Misappropriation is the dishonest use of the property of another for one's own benefit.<sup>19</sup> The use of a trade secret is not always considered a misappropriation (and thus an actionable violation) of it. The circumstances will dictate whether a misappropriation occurred. It will generally be granted only in cases where the disclosure was improperly obtained or the person was under the obligation not to disclose the information.

The protection that trade secrets offer partly stems from their status as something between a patent and a copyright. Because they are generally not applied or codified unless they are an exception to mandatory disclosures, they offer a workable structure for companies to both ensure the profitability and protection of their research as well as some control over the actions

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<sup>16</sup> John C. Stedman, "Trade Secret," (*Ohio State Law Journal* 23, 1962): 4.

<sup>17</sup> *Ibid.*

<sup>18</sup> *Ibid.*, 15-16.

<sup>19</sup> Bryan A. Garner, ed., *Black's Law Dictionary* (St. Paul, MN: West Publishing Co., 2009): 1088.

of their employees outside the scope or time of the employment. The trade secret claim is usually an action made for misappropriation of that trade secret. Because of the two most common uses of them (patent-pending work or non-copyrighted, unpublished work), this is usually a contracts or a tort claim.<sup>20</sup> Contracts claims are generally within the scope of the employment and are brought for violation of an employment agreement in this circumstance. A tort claim, generally, is a claim for any kind of harm caused – in this case, it would be financial and the damages sought would be to recover lost profits or potential profits.

### **III. Conceptual framework for fracking**

The current debate over the rules for fracking, at its core, is the balancing of the industry's concerns with the public's. The industry is looking for a profitable, reasonable investment in the project in North Carolina, which the legislature wants to encourage because of the possible economic growth it presents for the state. It also provides an energy source which seems to have a relatively low price. On the other hand, the legislature has to balance this ambition with the negative costs and concerns that fracking brings environmentally and socially. It is the job of the government to protect the public and use the public resources in the most effective way. Because fracking is a relatively new phenomenon, its long-term effects on public health and the environment is unclear and untested.

The industry's concern, besides the profitability of the venture, is the impact of this operation on their overall company. Part of this is highly dependent on trade secret laws in each state. A company operating in several states, with many of the same competitors, has a need for the protection of its methods of production in order to maintain a competitive advantage. Disclosure of a trade secret in one state will not only destroy it in that realm, it will allow the

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<sup>20</sup> Cheung, "Property Rights in Trade Secrets," 46.



competitors to gain access to it and will likely destroy the status of the trade secret protection that it enjoyed in other states. This is a substantial loss for the company overall. Because of the amount of resources and research that went into developing the correct formula, the company may choose not to pursue an otherwise profitable operation because of the possibility of disclosure. Furthermore, the availability of other, more favorable, forums for the same kind of operation will encourage them to forego the state altogether. On the other hand, lacking trade secret protection might perversely incentivize the companies to use older, less safe methods or mixtures during fracking in order to protect their latest innovations.

The public's concern is the impact of fracking on their daily lives and the repercussions of the operation once it is complete. One of the primary concerns is the contamination of their drinking water. This could occur in two ways: either through the contamination of groundwater or through spillover to surface water. The contamination of the underground water would occur because the wells are drilled through a water table and if improperly constructed or poorly designed, the fracking fluid could percolate into the water. Similarly, if the operation is not properly monitored, chemicals can spill over into the water sources in the area. Contamination of the soil could happen through either of those occurrences, but is even more likely through leftover chemicals, waste pit contents buried on site, or leaking waste tanks after the operation has been completed. The chemicals could be left in the ground or may have seeped into the ground throughout the fracking process and will permanently remain there. A concern of spills during transportation and prior to fracking should be addressed as well. Because of the variety of ways that the fracking fluid can impact the neighborhood, the public has a need to know the chemicals used in the process in order to be able to counteract and treat the possible effects.

Nor are the chemicals in the fracking fluid the only concern. There is mounting evidence that not all of the gas released in the operation is properly collected and contained. Some of the gas, i.e. methane, has been shown to escape during the drilling process and migrate into drinking water. Hydraulic fracturing is different from the previous drilling operations because of the amount of water it needs – several millions of gallons per operation. This is problematic because such use of the water changes it so that it cannot be distilled back into potable water. Using water in such amounts will put a strain on the regions that are already prone to droughts and have limited water resources.

The practical impacts of fracking on the community as a whole extend farther than just the contamination concerns. Fracking operations are highly industrial, and intensive in the amount of work and involvement. Having a fracking well in the neighborhood will increase truck traffic for the delivery of the necessary materials, which would increase the levels of air and noise pollution. The fracking operations are work-intensive and the drilling occurs almost constantly throughout further adding to noise pollution and general disruption of the neighborhood.

One of the groups that will be uniquely affected is the owners or tenants of split estates. The term “split estates” refers to the possibility of having separate interests in the surface and the subsurface (such as mineral) rights. In cases of split estates, the subsurface rights owner can consent to the extraction of oil and gas without consulting others affected. This is problematic because the surface landowner will be the one who is the most vulnerable and forced to endure the drilling proceedings on or under his land without any input on that decision.

Compulsory pooling is a similar legal issue, with comparable results. Under the current laws in North Carolina, which the MEC is proposing to apply, compulsory pooling will be

allowed. The current law<sup>21</sup> has not been updated since 1945 and was originally created for vertical oil and gas wells, which flow freely. It was meant to protect the landowner from having his minerals usurped from under him by the sharing of the common “pool” of minerals with a neighbor. This would also optimize the process of obtaining the minerals because the drilling of several wells would be more expensive and lower the pressure of the pool, decreasing the total recoverable amount of the mineral sought. Prior to passing this law, there was an incentive to drill first and frequently to obtain the minerals first. This was a perverse incentive for waste and inefficiency. When applied in this context, however, the law will likely achieve the opposite goal of the original intention. Within a designated area, the drilling as a joint unit may be ordered by the Commission upon a hearing.<sup>22</sup> This would dictate the reluctant owners to submit to the decision. The owners will either be compensated for the land/minerals used and obtained within that process or be allowed to invest and share in the profits of the venture. This is especially troubling when the owners do not want to develop their resources, for any reason.

The environmental concerns are immediate in terms of whether fracking actually works or is worthwhile, whether the process is damaging in terms of chemicals injected or fissures created, and whether there will be repercussions past the ones present during the operation. The disposal of the waste fluids from the operation is another issue for concern. Because of the chemical additives in the fluid, it needs to be disposed of in a deliberate and careful manner. However, it is unclear if all the liquid and chemicals used could be removed nor what is the appropriate way to neutralize this waste.

The rules currently being discussed by the MEC are supposed to address and balance those concerns and to provide for the possible contingencies that come with it. However,

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<sup>21</sup> *Oil and Gas Conservation*. N.C. Gen. Stat. Sec. 113-393 (2012).

<sup>22</sup> *Ibid.*

industry needs appear to be a major concern at this time, which is not often congruent with public health and the environment.

#### **IV. Background of trade secrets**

##### *A. Uniform Trade Secrets Act*

In 1979 (amended in 1985), the Uniform Law Commission undertook to write the Uniform Trade Secrets Act (UTSA) in order to promote an industry standard for trade secrets. It has since been adopted and followed by 47 states.<sup>23</sup> The states are not mandated to adapt the UTSA in its entirety and amend it as suited to their purpose, but the general framework remains the same. The UTSA echoes the definition and concerns of the Torts Restatement<sup>24</sup>. In order to maintain an action under the trade secret protection, it must fulfill the following requirements: (1) the subject matter involved must qualify for trade secret protection; it must be the type of information trade secret was intended to protect, and it must not be generally known, (2) the holder of the trade secret must establish that reasonable precautions were taken to prevent disclosure of the secret information and (3) the trade secret holder must prove that the information was wrongfully acquired by another; that the information was misappropriated.<sup>25</sup> UTSA defines misappropriation more broadly than the Restatement and relies on whether the party that disclosed the trade secret knew or should have known that it was a trade secret.<sup>26</sup> It further provides both injunctive relief and damages for misappropriation, officially granting the authority that was previously at the court's discretion.<sup>27</sup> UTSA also includes a statute of

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<sup>23</sup>The National Conference of Commissioners on Uniform State Laws, *Enactment Status Map*.

<sup>24</sup> As discussed above in II.A.

<sup>25</sup> The National Conference of Commissioners on Uniform State Laws, *Trade Secrets Act*.

<sup>26</sup> Ramon A. Klitzke, "The Uniform Trade Secrets Act," (*Marquette Law Review* 64.2, 1980): 285.

<sup>27</sup> Klitzke, "The Uniform Trade Secrets Act," 301-06.

limitations on when the action can be brought (within three years) and when the timing starts,<sup>28</sup> which previously varied greatly.

### *B. Federal*

The federal regulations similarly follow the pattern of defining what a trade secret it and provide for misappropriation of the trade secrets. In 1996, the federal government criminalized acts of economic espionage, including the definition of trade secrets as a protected class of information.<sup>29</sup> The term is defined more expansively in the statute<sup>30</sup> than in the Restatement, but both would cover the same scope of information. The statute reiterates that in order to maintain the protection: “(A) the owner thereof has taken reasonable measures to keep such information secret, and (B) the information derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable through proper means by, the public.”<sup>31</sup>

### *C. The status of trade secrets in North Carolina*

North Carolina is one of the few states that have not enacted the UTSA. The current protection that North Carolina offers for trade secrets stems from the Trade Secrets Protection Act.<sup>32</sup> The requirements for protection track the language of both UTSA and the federal regulation. Section 152 defines trade secret as “business or technical information, including but not limited to a formula, pattern, program, device, compilation of information, method,

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<sup>28</sup> *Uniform Trade Secrets Act*, Sec. 6.

<sup>29</sup> 18 USC. Sec. 1839 (2012).

<sup>30</sup> *Ibid.* (3) “the term ‘trade secret’ means all forms and types of financial, business, scientific, technical, economic, or engineering information, including patterns, plans, compilations, program devices, formulas, designs, prototypes, methods, techniques, processes, procedures, programs, or codes, whether tangible or intangible, and whether or how stored, compiled, or memorialized physically, electronically, graphically, photographically, or in writing.”

<sup>31</sup> *Ibid.*

<sup>32</sup> *Trade Secrets Protection Act*. N.C. Gen. Stat. Secs. 66-152 to -157 (1992).

technique, or process” provided that it “derives independent actual or potential commercial value from not being generally known or readily ascertainable through independent development or reverse engineering by persons who can obtain economic value from its disclosure or use” and “is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.”<sup>33</sup> Having uniform parameters and a generally accepted framework for trade secrets is a useful starting point for this process. It will be likely that most of the interpretations would be applicable to the issue at hand. However, the trade secret designation is usually given retroactively, remedied with injunctions and monetary compensation. The most appropriate way is to preemptively create the framework for justifying a trade secret.

#### **V. Trade secrets in fracking**

The definition of trade secrets is relatively standard and well accepted. The problem is that it is broad and vague, thus its application can vary widely. Because fracking regulation is a recent development, trade secret exceptions are new and undeveloped concepts. The process for claiming and receiving trade secret protection is the focal point of the issue. Unlike the previous use of trade secrets, this would be an exception to mandatory disclosures, granting them a legal recognition prior to the possible misappropriation claim. The establishing of trade secret status has to occur prior to the violation of the trade secret. Justifying it as a trade secret has to happen in some form that would still maintain its secrecy to the extent it would be without the mandatory disclosures.

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<sup>33</sup> *Trade Secrets Protection Act*. N.C. Gen. Stat. Sec. 66-152.

### A. Overview of different states' disclosure rules

Currently 29 states have confirmed fracking operations within their borders.<sup>34</sup> Only fifteen<sup>35</sup> of the states have mandatory disclosure rules for chemicals used in fracking.<sup>36</sup> The rest of the states have no disclosure rules specific to fracking. Twelve of the states with mandatory disclosure rules have a trade secret exception.<sup>37</sup> The two main approaches used in claiming trade secret protection are: (1) a determination made by the claimant with some form of justification (which is not always required), or (2) an application process that is evaluated by some authority other than the claimant. Most states that have the exception apply the first approach with some variation in the process. The majority of the states in that category will allow the companies not to disclose trade secrets once the claimant makes such designation.<sup>38</sup> The justifications accompanying that designation are rarely reviewed or evaluated further. A minority of the states require some form of further disclosure even after the recognition of the claim of trade secrets. Three of the states require a disclosure of the chemical type or chemical family of the trade secrets, sometimes in the form of a master list.<sup>39</sup> Some will require a further disclosure of concentration of the chemical: either exact, as a range or a maximum used. Only two of the states that follow the first approach require the disclosure of trade secret information to the government agency despite the claim of trade secrets.<sup>40</sup> The agency requires all the information with proper labeling and will then hold the trade secrets information confidential. The first approach is efficient and convenient. The industry is comfortable with determining how much of their

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<sup>34</sup> Matthew McFeeley, "State Hydraulic Fracturing Disclosure Rules and Enforcement: A Comparison" *Natural Resources Defense Council* (2012): 4.

<sup>35</sup> Interstate Oil and Gas Compact Commission. *State Statutes*.

<sup>36</sup> *Ibid.*

<sup>37</sup> *Ibid.*

<sup>38</sup> *Ibid.*

<sup>39</sup> *Ibid.*

<sup>40</sup> *Ibid.*

information they must expose and the government agencies do not have to deal with a designation of highly technical information.

The only state that currently uses the second approach is Arkansas.<sup>41</sup> In this case, the company submits an application for trade secret protection to the designated Board and the Board determines whether the protection should be granted. This approach allows for a more objective and uniform standard. The determination is made by the same Board every time and is consistent. The Board should be less biased in reviewing the material than a company who has a pecuniary interest in keeping as much information undisclosed as possible. Furthermore, over time with the variety of the information, the Board would be familiar with what is known and used in the industry and better able to make the determination of what actually is and is not secret, which the individual company is less likely to be able to do because of the lack of access to the information from other companies.

## **VI. The process**

Once it is established whether the trade secret exception should be granted, the process by which it is established is important to consider. The main concerns are the timing and the method of obtaining the trade secret protection. In considering how that process should be developed, the needs of the public and access of information in case of emergency should be the driving forces behind the considerations.

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<sup>41</sup> Ibid.



### *A. Timing*

The timing of the disclosure is important. Firstly, since any operation will be permitted prior to any actions on the part of the operator,<sup>42</sup> it is not logistically a problem to require disclosure at the earliest possible stage. Because spills and accidents can occur even during the transportation phase of the operation, it is essential to have the information available as early as possible. The broad guidelines of disclosure would be: at the time of the filing of the permit, before transportation, prior to drilling, after the drilling, or after the completion of the entire process. These timings do not have to be mutually exclusive. Requiring early disclosure and mandating updates throughout the process is the best way to have accurate information in a timely manner. The early disclosures might be vague and tentative because the operator might not have selected the exact combination for the process yet, but frequent updates should make it more accurate and easier for the operator to comply with.

### *B. Method*

There are two questions to consider what is being released from trade secrets to the state, and what will be publicly available.<sup>43</sup> If the trade secrets are not fully disclosed to an overseeing agency or a third party,<sup>44</sup> what portion, if any, should be disclosed?

There are several methods of disclosure that other states have adopted.<sup>45</sup> There are two considerations that could be addressed separately: the composition of the trade secret chemical and the concentration of it used in the compound. The composition of the chemical can be disclosed through different levels of specificity: starting from the general group that the

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<sup>42</sup> For uniformity, in the remainder of the report, “operator” will be used as the placeholder word for whoever is deemed liable and holds the trade secret at the time. As discussed above in I.B, this is a distinction that should not be taken lightly.

<sup>43</sup> Discussion of public access to the information is below in section H.

<sup>44</sup> Who should hold the trade secrets is discussed below in section C.

<sup>45</sup> See Section V.A.

compound belongs to by what it does (i.e., acid), going down to the family group, family name or even the exact compound without the specific qualifications or molecular formula of it. The concentration can similarly be distilled by the level of specificity required during disclosure. This range is from something as vague as the total possible amount used or a range of the amounts possibly used to the exact concentrations of the compound within the entire mixture and more importantly, the highest possible concentration to be used. This strikes a balance between the protection of the secret from the company's standpoint, and the state's awareness of what is being put into the ground and how to deal with it.

### *C. To whom*

If it is decided that the trade secrets should be disclosed in some form and placed in safekeeping, there are two options of who should receive and retain them: a government agency or a third party.<sup>46</sup> A government agency would be any division or department of the government, which would be answerable to the public. A third party would be a private agent that is not affiliated with the government and is not held liable to the public. The government agency holding the secrets would have immediate access to the information in case of an emergency and could validate that it is complete and appropriately labeled. The most efficient way would be for the company to submit a complete disclosure, which would be sealed, and a redacted copy that would be available for general use and to the public. There is some concern about the protection and ability of a government agency to keep the trade secrets safe from disclosure and public access.<sup>47</sup> A third party holding the trade secrets is more secure from the viewpoint of the company because it is not answerable to the public under any freedom of information act. A third

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<sup>46</sup> If the company holds on to the trade secrets, this would be classified as non-disclosure for the purposes of this report.

<sup>47</sup> Public access to trade secrets and within a government agency is discussed more fully in Section H.

party will also be shielded from litigation because they are mere holders of information and are not authorized to disclose it. The litigation would then be aimed either at the company who might be improperly claiming a trade secret, or at the agency that would allow that claim to stand. On the other hand, access to the information would be more difficult in case of an emergency than from a government agency, but that could be addressed through proper agreements for the third party to have that information. It is also likely more reliable to get the information from a third party in an emergency, when those conditions have been specifically stipulated, than attempting to contact the company and force a disclosure which could result in delay.

The MEC recently proposed that DENR should hold the trade secrets.<sup>48</sup> DENR has vehemently opposed this idea on the grounds that it would lead to extensive litigation, which they do not have the resources for or wish to deal with. This is controversial as DENR currently holds other trade secrets and there is no data to show that there has been a large amount of litigation in that sphere.

#### *D. For how long*

Currently, trade secret protection is provided indefinitely – as long as the information is protected and kept secret: it qualifies as a trade secret. This has generally been the case and stems back to the unannounced and unknown status of trade secrets prior to the suit for misappropriation. In this case, where the status would be conferred at some point while the trade secret protection is still available and will remain available, it is a question to ask, how long that protection will or should last. The MEC has brought up the issue of temporal limits on trade

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<sup>48</sup> Mining and Energy Commission: Trade Secrets Study Group, (June 28, 2013. Raleigh, NC).

secret protection, if granted.<sup>49</sup> This is problematic on some levels. It will fundamentally change the status and idea of what trade secrets are. This might set a dangerous, and perhaps inconsistent, precedent for trade secret protection in other fields. It is also counterintuitive to have the trade secret protection expire after its conferral because the qualifications for trade secret protection in and of themselves require secrecy and protection of that information. Most disclosure language will specifically state that the transfer of the secret to the agency that holds the trade secrets or the emergency personnel will not be construed to compromise the “secrecy” part of the trade secret. This might also cancel out the protection the companies enjoy in other states, which would circle back to the idea of companies being comfortable with disclosing trade secrets at all.

#### *E. Appeals*

In the process of granting or denying a trade secret to the companies, there has to be some oversight and balancing authority from the company as well. As a precaution, every decision made by the overseeing body regarding the status of trade secrets should have at least one chance of appeal to a higher authority by the company. This process once again needs to be timely and efficient, keep the protection of the trade secret and determine the proper forum in keeping with those ideas.

#### *F. Challenges*

In order to ensure impartiality of the overseeing body granting the status of trade secrets, there should be some way to challenge the decision on the other side as well. In this case, it is likely the public (or some subset within it) or the government that would make the challenge and bring the case. As above, the challenge of the correct forum and the legal hierarchy would be a

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<sup>49</sup> Mining and Energy Commission Meeting (June 28, 2013, Raleigh, NC).

question, but it is even more important to delineate and establish standing – what party would have the right to challenge the determination.

This is where the concern of split estates is especially relevant. The standing could be drawn narrowly to landowners or very broadly to the entire public. If standing is limited to some group of people, it has to be clear as to what group that is and who belongs to it. Whether renters, split estate owners or those affected by the operation belong in that group and how can they establish standing is vitally important to make this a workable scheme for challenges.

As to the forum, the first challenge would most likely and favorably be an in-camera review by the appropriate court, as designated by the rules established. This would need to be a court that could function quickly and efficiently, have the authority to override the decision of the governing body and the right expertise in the field. Another concern with the choice of court is whether the choice would be prohibitive monetarily for an individual who would have standing to bring a claim: for example, the filing fees. The appeals going beyond that are likely, for reasons of ease and predictability, be then fed back into the court system at the appropriate step – probably with the following appeal going up to the Court of Appeals.

#### *G. Emergency Exceptions*

There is a need for emergency personnel and/or first responders to have specific information about the operation in order to be able to plan accordingly for contingencies. Sometimes, this needs to extend to trade secrets. In addition, generally in an emergency, a full and complete disclosure needs to occur, at least to the first responders who would be dealing with the chemicals and the medical practitioners who would be treating the people affected. In this case, depending on the prior disclosure procedures, the trade secret information would have to be disclosed from either the primary party claiming the privilege (such as the manufacturer), a

secondary agent (such as the operator) who holds or has access to the trade secret, or the third party to whom the disclosure was made, including the trade secret information (which could be the government agency or an independent actor). These procedures have to be in place prior to the emergency, communicated, and worked out at the time of the grant of the permit or the disclosure.

Because accidents can happen prior to the drilling or fracking, the timing of disclosure has to account for that possibility. The disclosure rules have to recognize the need for contingency plans and dictate the safekeeping of the trade secret information accordingly. In case of an emergency, first responders and medical personnel will need to be able to acquire that information. How quickly someone could obtain information in case of an emergency should be a central concern in determining who holds the trade secrets because time is of the essence. If the company is allowed to retain their trade secrets with emergency stipulations, such as an appointed person who has to release the information within for example two hours, how will that be enforced? What will be the alternative in an emergency when that information is not provided in a timely manner?

This similarly applies to how specifically a trade secret will be disclosed at the time of the granting of the trade secret status. Whether there will be another alternative for obtaining more accurate information and from who is necessary to consider when the chemical formula and concentration of the compound affect the treatment given.

Frequently, with the release of trade secrets in an emergency, the medical personnel or first responder have to provide a justification for the release of information – the timing and thoroughness of that justification should be established prior to the emergency and the company should be monitored for compliance. The timing should be such as is reasonable in an emergency

situation – perhaps the emergency can be sanctioned by a government official, in which case the justification can be written at a later date.

Generally, disclosure in case of an emergency does not alter the trade secret status and the people who have the information will be required to sign a non-disclosure agreement. The signing of the non-disclosure agreement, while enforced, could not and should not be conditioned prior to the release of information. The timing should not be detrimental to the treatment in case of emergency.

#### *H. Public Access*

##### *1. What information?*

The public has a wish and a right to know what goes into the ground that they are living on and will continue to be next to after the operation is done. This is problematic with trade secrets because they are not meant to be disclosed to the public. In that case, the public's right to know is counterweighed by the company's need to protect their secrets. The type of the process in place for granting trade secret protection will determine the access public will have to the information.

Depending who holds the trade secret information, it might be liable to disclosure under the Public Records Act.<sup>50</sup> Although there is a specific caveat for that protection, there is some room for argument of whether that could be upheld within the confines of government-held information. The industry's concern is with mistakes and wrongly disseminated information, but this should not be a stopping point for determining the proper repository of trade secrets. A proper process and redacted duplicates should address that concern sufficiently.

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<sup>50</sup> *Public Records Law*. N.C. Gen. Stat. Sec. 132-1 (1993).

An interesting question is whether the concentration and family names that are revealed abstractly about the trade secrets, for emergency planning, should be made available to the public. On the one hand, it is a concession of protected information for emergencies. However, it is information that is disclosed to a public agency, which could be liable under the Public Records Act. It is a concern that should be discussed and addressed.

## *2. What forum?*

Access to information by the public is vitally important for transparency and legitimacy. The medium and the ease of access will demonstrate how committed policy makers are to an open process. Digital access, accurate and timely information and searchable options should be a high priority; every extra hurdle of a request, application or obtaining paper copies seems unnecessary and probably more expensive. However, whatever agency or individual is responsible for collecting the data should maintain hard copies of the information as a fail-safe mechanism.

In terms of the digital options, there is a FracFocus.org website or the maintenance of a separate website by the state/agency. FracFocus.org is somewhat useful because it is already established, used by other states, and companies can submit the information there directly, but it has limitations as well. The maintenance of an independent website would require investment of resources, uploading of the information and design , but it can be controlled and regulated by the agency.

FracFocus.org is a website that managed by the Ground Water Protection Council and the Interstate Oil and Gas Compact Commission in order to compile the records and disclosures from the fracking companies nation-wide. It is currently used by eleven states, with some of



them using it exclusively.<sup>51</sup> It is known and accessible to the public. It is searchable and has been available since 2011. Because it is a nationwide website – the specifications for the disclosure, which vary from state to state, are uniform, thus missing information or places to input the required disclosures. There are some problems with its workability and accessibility in terms of accessibility. The website is an independent entity and cannot be regulated or controlled by the government – including altering the disclosure forms. The website can also go down without notice and permanently. The state should prepare for that possibility and account for it – especially in case the informational input is lost. There is a lag in when the information is processed and posted, which is problematic – both for the state if that is their only source of information, and for the public. A new version of FracFocus.org has been recently released and some or all of these shortcomings might have been addressed. Currently, there is no cost to the state or the public for using the service, but it is unclear how long it will stay that way.

The agency's own website will be completely regulated by the agency. It can be designed with the specific state and its rule in mind. It can accommodate and evolve with the state's rules and needs. State has a lot more oversight and flexibility with it, which might justify the extra cost of compiling and maintaining the website instead of using an available one.

## **VII. Currently in North Carolina**

The MEC is currently considering the rules for disclosure and fracking for North Carolina. They are addressing some of the concerns discussed above. However, they might not be as liberal in their considerations as they wish: the North Carolina Legislature has recently been active in this sphere as well. Although the MEC has been tasked with writing the disclosure

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<sup>51</sup> Kate Konschnik, Margaret Holden and Alexa Shasteen, "Legal Fractures in Chemical Disclosure Laws," *Harvard Law School: Policy Initiative Report* (2013): 3.

rules, some of the proposed legislation<sup>52</sup> suggested bypassing the MEC and/or limiting their authority and ability to write the rules. This is problematic for reasons of transparency and legitimacy of both the rules and the process. The MEC is makes their meetings and minutes available to the public. The legislature's attempts to circumvent that are dangerous and troubling. Furthermore, the MEC has put in time, effort and expertise in learning and discussing the issues. Because this is such a controversial and complicated matter, and it is the charge and mission of the MEC to develop rules to regulate the gas industry, the Legislature's meddling is out of place.

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<sup>52</sup> Specifically, H.B. 74, 2013 Leg., 2013 Sess. (N.C. 2013) and H.B. 94, 2013 Leg., 2013 Sess. (N.C. 2013).

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