Safeguarding Confidentiality in Investor Relations: Start-ups Edition

In the dynamic realm of investor relations, safeguarding confidential information is paramount for both start-ups and investors. In today's business environment, start-ups and investors commonly engage in transactions where conducting due diligence is recognized as the crucial first step whereby the confidential business information is shared with the investors/venture capitalists. Apart from this, start-ups also create presentations through investor decks having multiple initial rounds of discussion to pitch and generate enough interest in their business model. Start-ups today fear the breach of their confidential and proprietary information they provide to the investors/venture capitalists during this process of due diligence. They often find it difficult to protect their sensitive business information and secure their competitive edge from the investors. However, while the process of soliciting investments is the ultimate need for start-ups, they often overlook the crucial role of an NDA and what is actually protects. It is essential to understand that an NDA is not a blanket agreement for all the information shared by the start-ups; rather it's only a reflection of a core promise. It is one of the initial key documents that one as a start-up must sign when disclosing confidential information about their company such as their product(s), business performance, funding round, valuation expectations etc. Understanding the specific scope and limitations of an NDA is of utmost importance for effectively safeguarding a start-up's sensitive information during the investment process. An NDA is signed with the primary purpose of protecting the confidential information against unauthorized use; however, it typically by default carves an exception for professional disclosures. Consequently, the level of binding obligation under an NDA to maintain confidentiality in not truly tested in a court of law. In fact, very seldom, do start-ups have the ability to sue potential investors. Therefore, NDAs neither should be taken lightly nor it should be taken as a standard document by start-ups. It is the foundation stone of what the start-up is planning to do and in the event of investor solicitation, all start-ups must pre prepare their own NDAs or review them beyond standard formats.

Moreover, even with a well-drafted NDA, enforcing it in case of a breach can be challenging as it must align with the legal principles, especially the one outlined in Section 27 of Indian Contract Act, 1872. This section aims to prevent agreements that excessively restrict an individual's ability to engage in their profession or business. Even though there are no judgments on it being imposed between any investor and a company, however, there are a plethora of judgments pertaining to employment agreements whereby the various courts have tried to clarify the scope of what constitutes confidentiality in terms of an agreement. Some being ***Navigators Logistics Ltd. v. Kashif Qureshi and Ors.***, 2018 SCC OnLine Del 11321, ***Star India Pvt. Ltd. v. Laxmiraj Seetharam Nayak,*** 2003 SCC OnLine Bom 27, ***Ambiance India (Private) Ltd. v. Naveen Jain***, 2005 SCC OnLine Del 367 and ***American Express Bank Ltd. v. Priya Puri*** 2006 SCC OnLine Del 638, wherein it was held that not every customer/client list would qualify as confidential information or trade secret unless the confidentiality about it is of economic/business/commercial value. It has been held that in any employment, every employee would get to know some information without any special effort. All such persons cannot be said to be in knowledge of trade secrets or confidential information and every knowledge of such facts cannot be labelled as trade secret or confidential information. Furthermore, it was also adjudicated upon that any information which is available in public domain shall not constitute a trade secret or confidential information. On the other hand, what can constitute a trade secret has also been defined in one of the cases to be a formula, technical know-how or a peculiar mode or method of business adopted by an employer which is unknown to others.

In the light of the above, when we look at the process of due diligence being conducted between start-up companies and investors, an extensive assessment is conducted by the investors and confidential information like financial statements of the company is shared for the same, however, now as per the scope of confidentiality, the same cannot be protected as a trade secret if it is available in the public domain. Hence, it is imperative for start-up companies to craft NDA(s) reasonably and practically to protect legitimate interests while avoiding undue restrictions that might render them void under Section 27 and must be careful about the extent to which they share confidential information. It is suggestive that while pitching the business to the investors, the start-up companies should share what the business is about without showing how it is done. By adhering to these principles and best practices, start-ups and investors can safeguard their sensitive information and foster a successful investment process. Accordingly, it can be inferred that notwithstanding the fact, the courts have been consistently trying to protect the trade secrets and the confidential information, there is still a need to arrive at an established position pertaining to the same.

Authors: Ms. Akriti Anand, Associate – Corporate Practice Division