

NDA's – Significant Business Tool or Simply More Paperwork?

Article

November 23, 2021

In business, many situations require you to share sensitive and confidential information with another individual or company. To ensure the other party respects the confidentiality of this information, a non-disclosure agreement, or NDA, is often used. But when is the right time to utilize an NDA? And why should you consider them as part of your toolkit when generating and maintaining business?

Generally, and simply put, NDAs should be used any time you wish to convey valuable, confidential, proprietary, or sensitive information about your business or idea to another party and want to ensure the other party does not use the information outside the scope of your proposed business relationship. That said, there are three primary reasons to use an NDA: for protective purposes, contractual purposes, and strategic purposes. Let's break these down and discuss a few common business situations wherein an NDA should be considered and implemented.

Protection: The most common reason for entering into an NDA is to ensure there are adequate and binding protections in place with the recipient before sharing your company's confidential information. When entering a new business relationship, it's easy to get caught up in the excitement of possibilities that lie ahead. Ideas begin flowing, conversations evolve, and verbal agreements and handshakes take place. Unfortunately, this excitement and desire to hit the ground running can sometimes lead to putting the cart before the horse. And although we live in a region ripe with "mid-west nice," that alone should not be the basis for a business relationship. Initial conversations and excitement go far in bringing a business deal or relationship to fruition, but before sensitive business information such as financials, customer lists, developmental designs/inventions, business methods, or manufacturing processes are shared, it's crucial to implement a non-disclosure agreement with the other party to ensure your business information is adequately protected and binding protections are in place. It's common for businesses to enter into NDAs as a first step for discussing licensing agreements, vetting mergers and acquisitions, and discussing potential manufacturing, supplier, or distributor agreements. But, as stated earlier, really any situation wherein confidential information is to be shared, an NDA should be considered. Then, as the relationship evolves and begins to take shape, a more

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formal agreement should be executed to formalize the relationship and outline definitive terms and conditions moving forward.

Contractual: Bottom-line, NDAs are legally binding contracts that establish a confidential relationship between the signing parties. It is important to be aware of existing contractual obligations of confidentiality your company may be under from prior NDAs and like agreements to ensure you are not inadvertently breaching existing contracts by sharing protected information with third parties. Perhaps you are an engineering company that has entered into an NDA with a small start-up company to discuss designing a prototype of a new invention, before reaching out to a potential fabrication shop to assist in bringing the prototype to life, consider if the NDA is in place to allow such discussions of confidential information to the fabricator (a third-party), or if an agreement with the fabricator needs to be put in place per the terms of your current agreement with the start-up company. Realistically, the receiving party of confidential information will be liable for third parties to whom it will disclose the confidential information from the NDA, and as such, it is not uncommon for NDAs to include either that the receiving party is jointly and severally liable for any failure of a third party, or that the receiving party is obliged to discuss adequate confidentiality obligations with the third parties that will be involved. That said, before disclosing information received from a third party to subcontractors, business partners, or other vendors, it is crucial to determine your existing obligations to avoid a breach of contract when disseminating information.

Strategic: Lastly, executing an NDA with another party can help gauge whether that party is truly serious about discussions with your company and engaging in a business relationship. If the other party questions why an NDA is needed, consider whether that is a red flag. The other party may not view confidentiality as a significant concern or priority, may not understand the importance of strong confidentiality practices, or unfortunately, may just be trying to get you to reveal confidential information without the protections of an NDA in place. Whether you are looking to contract with a vendor to develop, manufacture, or distribute your company's product or explore potential strategic or exit transactions such as an M&A deal, joint venture, or partnership, an NDA is a great first step to vetting business relationships before locking down a more formalized agreement.

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