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No. 64408-4

IN THE COURT OF APPEALS
OF THE STATE OF WASHINGTON, DIVISION I

FLUKE CORPORATION and DANAHER CORPORATION,
Appellants and Cross Respondents,

v.

JONATHAN MORROW, EVANS NGUYEN and
MILWAUKEE ELECTRIC TOOL CORPORATION,
Respondents and Cross Appellants.

RESPONDENTS' BRIEF

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I. INTRODUCTION

The trial court dismissed Fluke's's[1] claims on summary judgment because the undisputed evidence conclusively refutes its hyperbolic rhetoric. Fluke's contract claims against Nguyen are based on an employee nonsolicitation provision presented to Nguyen for signature years after he began employment with Fluke, which is unenforceable because Fluke gave no independent consideration for that provision, and because it is an unreasonable restraint on trade. The trial court dismissed Fluke's contract claims against Morrow because this court's prior decision established as the law of the case that Fluke had no rights under an agreement between Morrow and the Jacobs Chuck Company (an unrelated Danaher subsidiary), and because the evidence failed to satisfy Fluke's burden of proving an "equitable assignment" by clear and specific evidence.

The trial court also properly dismissed Fluke's trade secret claims as a matter of law. Throughout the case, Fluke refused to specify the trade secrets at issue, thus revealing them for what they were: a tactical ploy to obtain far-reaching discovery of a new competitor using undefined and ever shifting trade secret claims. Ultimately, Fluke's claims failed as a matter of law because it could not meet its burden of proof regarding the

[1] Appellants are Plaintiffs Fluke Corporation ("Fluke") and its parent, Danaher Corporation ("Danaher"). Respondents are Defendants Jon Morrow, Evans Nguyen and the Milwaukee Electric Tool Corporation ("MET").

existence of a trade secret, actual misappropriation, or damages.

On cross-appeal, the court should hold that the trial court erred in denying Respondents prevailing party attorneys' fees based on RCW 4.84.330 (requiring an award of fees in regard to claims based on contracts with unilateral fee provisions), various equitable grounds, and under RCW 19.108.040 (allowing an award of fees in regard to trade secret claims maintained in bad faith).

II. RESTATEMENT OF ISSUES PERTAINING TO ASSIGNMENTS OF ERROR

1. May a trade secrets plaintiff survive summary judgment in the absence of evidence of an enforceable trade secret, or that its competitor misappropriated or otherwise used the trade secrets or other confidential information to the plaintiff's detriment?

2. Is this court's previous holdings on interlocutory appeal – i.e., that Fluke could not enforce the Jacobs Chuck Agreement as a matter of law because Fluke was not a party to the JCA, because those terms expired in 2005, and because the evidence offered was insufficient to prove an equitable assignment of the JCA by "clear and specific evidence" – binding on Fluke as the law of the case?

3. May a contract imposing upon the employee a broad obligation not to solicit other employees to terminate their employment enforced in the absence of consideration under *Labriola v. Pollard Group, Inc.*, 152 Wn.2d 828, 100 P.3d 791 (2004), and even if so, does such an agreement violate Washington's public policy prohibiting restraints of trade?

4. Does a trial court abuse its discretion in denying a plaintiff's motion for a continuance under CR 56(f) where the plaintiff fails to articulate additional discovery that would establish a genuine issue of fact for trial on the issues before the court on summary judgment?

5. Does a trial court abuse its discretion by denying a motion for leave to amend, filed on the eve of oral argument on summary judgment and the close of discovery, and in the absence of any allegations that could support additional claims for relief?

III. RESTATEMENT OF THE CASE

A. Nguyen's and Morrow's Employment at Fluke.

Nguyen and Morrow were two of several thousand employees of Fluke, which manufactures high-end electronic test and measurement ("T&M") equipment for the "premium" T&M market segment. CP 29, 3505, 6661. Fluke is one of more than 600 subsidiaries of Danaher, a multinational company that in its most recent 10K boasted of $20 billion in assets and more than $1 billion in annual profits.[2]

1. Fluke Presents Nguyen With an Employee Nonsolicitation Agreement Four Years After His Hire.

In 2000, Fluke hired Evans Nguyen as a manufacturing engineer. CP 1338-55. In May 2004, nearly four years later, Fluke's Human Resources department distributed a form entitled "Danaher Standard Terms and Conditions of Employment" ("Standard Agreement") to Nguyen and everyone else in his department, which Nguyen signed at the direction of Human Resources. CP 1339.

The Standard Agreement contained, among other terms, an employee nonsolicitation clause broadly prohibiting the employee from soliciting any employee to end his or her employment with Fluke, Danaher or Danaher's subsidiaries. CP 1346 (Section 2). It recites that this

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[2] The Court may take judicial notice of facts which are capable of verification by competent authoritative sources. *Rogstad v. Rogstad*, 74 Wn.2d 736, 446 P.2d 340 (1968); *cf. Kramer v. Time Warner, Inc.*, 937 F.2d 767 (2d Cir. 1991) (court may take notice of statements in securities filing as public record).

obligation "is supported by the Associate's eligibility to be considered for recommendation of annual option grants." CP 1349. But when Nguyen signed the Standard Agreement, he had been eligible for stock options for some time, and had actually received stock options in 2003. CP 1338, 1567. Fluke awarded Nguyen no stock options after 2003, nor did he receive any bonus, raise, promotion, promise of severance pay, or other compensation for signing the Standard Agreement. CP 1338, 1567.[3]

2. Morrow Signs a Noncompetition Agreement with Jacobs Chuck, But Signs No Agreement with Fluke Upon Transfer.

a. The Jacobs Chuck Agreement.

In 2002, Morrow accepted a marketing position at Jacobs Chuck, another Danaher subsidiary in South Carolina that does not compete in the T&M industry. In 2004, Morrow signed the JCA, an agreement utilizing Danaher's Noncompetition Agreement form, which contained noncompetition and employee nonsolicitation clauses. CP 15-24 ("JCA").

Several provisions defined how, *if Morrow agreed*, he could be obliged not to compete with another Danaher subsidiary *after* leaving Jacobs Chuck. In the only provision addressing transfers between Danaher subsidiaries, Jacobs Chuck was allowed to terminate the JCA *only if* the new employer offered a new agreement with substantially

[3] By way of contrast, other employees of Danaher subsidiaries who signed a different Danaher form ("Noncompetition Agreement") were granted "significant post-termination payments and enhanced severance benefits." CP 50.

similar terms. JCA ¶ 12(b). The JCA also stated that Jacobs Chuck "may" assign its rights and obligations "to Danaher and/or any other subsidiary or subsidiaries of Danaher." JCA ¶ 14. Thus, assignment was also permissive, not automatic. Finally, the JCA could not be amended except in writing signed by Morrow. JCA ¶ 13.

b. Transfer to Fluke.

Morrow resigned from Jacobs Chuck in 2004 to accept a position as a marketing manager with Fluke. Fluke did not offer Morrow a new agreement upon transfer. A non-competition agreement was not discussed during interviews, nor was Fluke's offer to Morrow conditioned upon signing a noncompete agreement. No assignment of or amendment to the JCA was signed by any party.[4] After several years, Morrow became a business unit manager for Fluke's recently-acquired Amprobe product line. Amprobe was a strong brand in the "value" T&M market segment that Fluke acquired in 2006 to give its customers a lower cost alternative that would not dilute Fluke's "premium" brand, and to defend against encroachment on the "Fluke" brand by lower cost competitors. CP 29, 4532, 4550, 6387, 6773, 6779. Unlike Fluke, most Amprobe products were outsourced to original equipment manufacturers ("OEMs") in Asia. CP 30, 4542 (Allen Dep., pp. 87-88); *see also* CP 339-40.

Three aspects of Morrow's work related to Amprobe are relevant.

[4] Ex. 31 at pp. FLUKE 000069-70; RP 5/21/2008 at 828-29, 5/22/2008 at 971.

First, in late 2007, the Amprobe unit was considering whether to add an ultrasonic distance finder to its product line. Morrow spent a few hours trying out competitors' ultrasonic distance finders, to evaluate whether well known limitations of ultrasonic technology (as compared to laser technology) were so significant that Amprobe should not offer an ultrasonic product. He did not consider that work or his conclusions to be a trade secret. Others clearly reached the same conclusion, given the number of available ultrasonic products. CP 1745-46.

Second, in December 2007, a co-worker sent Morrow an email attaching a copy of a Fluke marketing plan relating to laser distance finders. Morrow does not remember receiving or reviewing it. At that time, his focus was on ultrasonic technology, and he knew nothing of MET's plans to enter the T&M market. CP 1745.

Third, also in December 2007, Morrow visited a number of sales representatives who sold Amprobe products in the electrical distribution channel, and summarized the trip in a memo captioned "Amprobe Rep Performance Market Research Report." Ex. 16; CP 3963-75. Using public sources, Morrow also compiled a Cross Market Analysis of products available in the "value" T&M market segment, to identify where Amprobe might add new products to its already extensive line. CP 7472-7533; Supp. CP _____.

B. <u>MET Decides To Enter the "Premium" T&M Market Segment, and Recruits Nguyen and Morrow</u>.

MET is a leading manufacturer of heavy duty power tools. CP 337. It has strong distribution channels with professionals in the electrical, HVAC and plumbing markets. Looking to expand its product line, MET established a T&M division in 2007, headed by Mike Jones, a former Fluke employee. MET planned to leverage its brand (with its "Nothing But Heavy Duty" motto) to sell to the high end "premium" T&M market segment. CP 330-31, 337, 7555.

In November 2007, MET offered Nguyen a job as Engineering Manager in its newly formed T&M division, which Nguyen accepted. CP 1339. In his resignation letter, Nguyen told Fluke that he was accepting a position with MET which would involve "product overlap" with Fluke. CP 1352. In February 2008, Morrow accepted a job with MET. The evidence conclusively rebuts Fluke's allegation that Morrow misappropriated Fluke confidential or proprietary information:

The PST file and SIM card. Fluke hypothesizes that Morrow copied a PST file containing emails and files from his Fluke computer onto a thumb drive, and then deleted it from his Fluke computer to hide his tracks. There is no evidence to support this theory. Morrow candidly admitted *accidentally* deleting the PST file from the computer when deleting personal photos and music. CP 1749-54. He hid nothing; indeed, he immediately informed Fluke's IT department so that it could recover the file. CP 3615-22; RP 5/22/2008 at 967-68. Forensic analysis confirms that Morrow copied only personal photos and music onto the thumb drive. CP 1749-54. Fluke did not examine the thumb drive forensically, and offered no evidence contrary to Morrow's explanation. CP 3588, 3680. The SIM card from Morrow's phone, which was for a personal phone number, contained no customer or supplier contacts. RP 5/22/2008 at 1007-09.

"Actionable Distributor Data"/"Low Hanging Fruit." Morrow spent his first weeks at MET analyzing its existing presence within the electrical distribution channel, using public information from the distributors and internal MET data regarding sales of MET's existing – i.e., non T&M – products through each distributor. Morrow identified several existing MET distributors where MET's sales seemed low, which opportunities he characterized in emails as "actionable distributor data" that MET was "uniquely positioned to take advantage" and as "low hanging fruit." CP 1747, 3606-14, 3628-32, 3635-38.

"I know stuff." MET decided even before Morrow was hired that its initial T&M product offering would be the same "bread and butter" products offered by every T&M competitor, *e.g.*, clamps, forks, digital multimeters, etc. CP 1747, 3623-27. Morrow learned in an email from Mike Jones that MET was also considering whether to repackage a distance finder offered by a European affiliate for release in the U.S. under the MET brand. Morrow told Jones to speak with Morrow because he "knew stuff," referring to his impression of ultrasonic technology. CP 1745-46. [5] As it turned out, the European product was a laser distance finder, so ultrasonic technology was not an issue. Morrow did not discuss his work at Fluke with ultrasonic technology, and MET made no decision regarding the product until June 2009, well after Amprobe and Fluke had released their distance finder products. CP 1746.

C. Procedural History.

1. The Trial Court Denies Injunctive Relief Based on Trade Secret Claims and Orders Fluke To Identify the Trade Secrets at Issue With Particularity.

a. The TRO and Addition of Nguyen Claims.

With no evidence of misappropriation by Morrow, and lacking a noncompetition agreement naming Fluke as "the Company," Fluke and Danaher nonetheless sued Morrow three weeks after he resigned, on March 10, 2008. Fluke alleged breach of the noncompetition clause of the JCA (and related tortious interference claims against MET) not based on an equitable assignment – that theory developed later – but rather on the premise that the express terms of the JCA precluded Morrow from working "in any capacity" for any company "in competition with Danaher or its subsidiaries." Ex. 62 at 1; CP 6-7, 240-41. Fluke also alleged misappropriation of unspecified trade secrets and common law claims for

[5] Undisputed evidence refutes Fluke's suggestion that Morrow sent this email while "still a Fluke employee." (App. Br. at 12) Morrow resigned from Fluke on February 19, 2008. CP 338. The "I know stuff" email exchange did not occur until February 22, 2008. CP 3493.

breach of confidentiality and fiduciary duty.

Fluke immediately obtained a TRO precluding Morrow from using or revealing any Fluke confidential information or trade secrets (CP 121-24) and moved for a preliminary injunction to enjoin Morrow from working for MET's T&M division. CP 49, 74, 125-27. A week later, Fluke amended its complaint to add claims against MET and Evans Nguyen. CP 237-67. Although Fluke's TRO pleadings expressly referred to Nguyen's work with and knowledge of OEMs (CP 44-48), it sued Nguyen only for breach of the employee nonsolicitation clause.

b. Fluke Fails To Identify Trade Secrets at Issue.

As Fluke's complaint was silent as to the particular trade secrets that Morrow allegedly misappropriated, Morrow asked Fluke to "[i]dentify with specificity" the trade secrets at issue, and to produce documents related to all elements of Fluke's trade secret claims. Supp. CP ______ (Interrogatory No. 5 and RFPs 19-25 and 41). Fluke first stated only that Morrow "had broad access to a variety of Fluke's confidential and trade secret information" and that it would produce "representative examples" of such information. CP 4660-61. Subsequently, Fluke recited only generic categories of trade secrets and the Bates numbers of documents, but did not identify any specific trade secrets in those documents. CP 4663-76. Its responses made no reference to OEMs.

Based on ample authority that a plaintiff must identify the trade secrets at issue with particularity *before* being allowed discovery of a competitor's internal documents – failure to specify trade secrets at issue is recognized as a deliberate strategy to gain tactical advantage[6] – MET objected to producing competitively sensitive information until Fluke specified the trade secrets at issue. CP 526-40. Morrow and MET moved to compel Fluke to identify the trade secrets at issue with particularity. CP 4500-17. The trial court denied that motion, and Fluke's cross motion to compel, without prejudice for purposes of the injunction hearing. CP 636-41.

c. <u>The Trial Court Twice Holds Fluke's Trade Secret Disclosures To Be Inadequate.</u>

Fluke sought an injunction based both on the JCA and its trade secret claims against Morrow. Fluke contended that it had no adequate remedy at law and would suffer irreparable harm absent an injunction because it could not prove the damages caused by Morrow's conduct. CP 4-11, 237-44 Fluke argued that "[i]t is difficult even to imagine how one could track and measure the impact Morrow's threatened breach and misappropriation would have on Fluke and its business." CP 109. Ken Konopa (VP of Fluke's Industrial group) testified that Fluke would not be

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[6] Charles T. Graves and Brian D. Range, IDENTIFICATION OF TRADE SECRET CLAIMS IN LITIGATION: SOLUTIONS FOR A UBIQUITOUS DISPUTE, 5 Nw. J. Tech. & Intellectual Prop. 68 (2006) (CP 6928-962). An initial and particularized disclosure of the trade secrets at issue serves to guide a court in determining the scope of appropriate discovery, and thus prevent a plaintiff from defining trade secrets based on discovery from the defendant rather than its own internal documents, as well as to prevent abuse of trade secrets claims as a means of obtaining competitive intelligence. *See generally id. at* 68-86.

able to determine what portion of lost sales was caused by Morrow's alleged misconduct. RP 5/20/2008 at 310.

The trial court granted Fluke's request for a preliminary injunction, based on its construction of the JCA (RP 6/3/2008 at 1-15; CP 837-49) and accepting Fluke's factual contention that it could not prove causal damages. CP 846 (Conclusion of Law No. 7). But having seen and considered the documents that Fluke claimed to contain trade secrets and the testimony of Fluke's witnesses,[7] the trial court denied injunctive relief on the trade secrets claims, finding that "[t]he case is not about trade secrets" and that Fluke must first identify the trade secrets at issue before being allowed discovery from MET. RP 6/3/2009 at 3.

Fluke nonetheless continued to press its trade secrets claims as the predicate for overarching discovery of competitively sensitive documents. But when Fluke's *fourth* response to trade secrets discovery was as flawed as its first (CP 4648-51), the trial court ordered Fluke to "identify with particularity the trade secrets at issue on or before September 8, 2008." CP 985-87. It ordered that MET would not have to produce documents until two weeks *after* Fluke made its mandated disclosures. CP 977-80.

d. **The Grant of Injunctive Relief Is Reversed, and Claims Based on the JCA Are Dismissed.**

This court granted discretionary review of the injunction ruling on

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[7] The trial court denied Morrow's motion to exclude trade secret evidence at the hearing based on lack of discovery. RP 5/19/2008 at 2-13.

August 18, 2008, the same day as the trial court granted the cross motions to compel. On February 17, 2009, only two days before the preliminary injunction was to expire by its terms, this court reversed, holding as a matter of law that "the Company" referred only to Jacobs Chuck, and thus that "Fluke [had] no legal rights under the [Jacobs Chuck] Agreement." COA Opinion at 12. This court also rejected Fluke's contention that the trial court had accepted Fluke's "equitable assignment" theory,[8] reviewed the evidence, and noting Fluke's heightened "clear and specific evidence" burden of proof, rejected "equitable assignment" on the merits. *Id.*

Morrow and MET moved to dismiss Fluke's claims related to the JCA based on this court's law of the case. CP 1051-70, 1090-104. The trial court ruled that the evidence offered by Fluke – declarations from Fluke and Jacobs Chuck employees echoing testimony offered at the evidentiary hearing (CP 1071-89) – was insufficient to meet Fluke's heightened burden of proving equitable assignment by "clear and specific evidence," as this court held, and dismissed Fluke's claims based on the JCA. CP 1149-51.

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[8] *Id.* Indeed, after the trial court's oral ruling, Fluke revised its proposed findings of fact and conclusions of law to omit extensive findings and conclusions in support of its "equitable assignment" theory that had been in previously proposed findings and conclusions. Compare Supp. CP _____ (Findings of Fact 5-6 (Supp. CP _____) and Conclusion of Law 3 (Supp. CP _____)) with Supp. CP _____.

2. **The Trial Court Dismisses Fluke's Remaining Claims Against Nguyen and Morrow.**

Fluke did not supplement its response to trade secret discovery until May 7, 2009 (Supp. CP____), again reciting only categories of trade secrets and documents by Bates number, and again making no reference to OEMs.[9] Respondents moved for summary judgment. Nguyen moved to dismiss the only claim pled against him – breach of contract – and the derivative tortious interference claim against MET. CP 1313-34. Separately, Morrow moved to dismiss the remaining claims against him for misappropriation of trade secrets and breach of common law duties, and the derivative claims against MET. CP 1366-92.

Fluke devoted much of its opposition to Morrow's motion to an entirely new and previously undisclosed trade secrets theory that *Nguyen* had misappropriated trade secrets related to OEMs, based on the fact that MET was working with several OEMs with which Nguyen had worked years earlier while at Fluke. CP 1577-78; RP 9/18/2009 at 44-51. As to Morrow, however, Fluke offered into evidence only a few of thousands of pages of documents previously cited in discovery as containing unspecified trade secrets. CP 3936-41, 3963-79, 4002-05. Fluke offered no evidence regarding damages, and moved for additional time and

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[9] A graphic comparison of Fluke's fourth and fifth responses is set forth in briefing (CP 5076-77) and in the Appendix to this brief. The only substantive change was to specify smaller portions of Fluke's 2008 Strategic Plan. Morrow and MET moved to exclude such evidence as a discovery sanction for Fluke's refusal to comply with the trial court's prior orders, but the trial court declined to impose that sanction. CP 5070-81, 1555-57.

discovery under CR 56(f). CP 1586-87. On the afternoon before oral argument, and two days before discovery closed, Fluke moved to amend to add trade secrets claims against Nguyen. CP 1863-1964, 2148-52, 4036-061.

During argument, the trial court made clear that in previously declining to sanction Fluke for failing to disclose the trade secrets at issue with particularity, it had not deemed Fluke's latest disclosure to be adequate. RP 9/18/2009 at 63. On September 21 and 22, 2009, the trial court dismissed all remaining claims in the case, and denied Fluke's CR 56(f) motion. CP 1977–81, 2142-44. On October 12, 2009, the trial court denied Fluke's motion to amend and on October 21, denied the bulk of Respondents' requests for attorney fees. CP 2389-93, 6018-23.

IV. ARGUMENT

A. The Trial Court Correctly Dismissed Fluke's Contract Claims Against Nguyen, and Exercised Its Discretion in Denying Fluke's CR 56(f) Motion and Motion To Amend.

The trial court properly dismissed Fluke's breach of contract claim against Nguyen and the related tortious interference claim against MET, and was well within its discretion in denying Fluke's procedural motions.

1. Nguyen's Employee Nonsolicitation Provision Is Unenforceable as a Matter of Law Because It Lacks Consideration.

Fluke's claims against Nguyen were based on his alleged assistance in recruiting several other Fluke employees to work at MET. Fluke claimed that this conduct breached the Standard Agreement's employee nonsolicitation clause. This extraordinarily broad clause prohibits acts in solicitation of any person employed full or part time by or working as an independent contractor for "Danaher or any of its subsidiaries" (including Fluke). CP 1346. It purports to prohibit Nguyen from soliciting *any* employee of Danaher or *any* of its hundreds of subsidiaries, regardless of whether Nguyen knew them previously, or whether that employee was subject to a non-competition agreement, or was being hired to work in a capacity that implied the possible use or disclosure of confidential information. As drafted, it forbids the most modest recommendation, and cuts off one of the best sources of career opportunity – contacts with former colleagues.

The trial court correctly rejected Fluke's flawed attempt to enforce this clause because it is void for lack of consideration. In *Labriola v. Pollard Group, Inc.*, 152 Wn.2d 828, 100 P.3d 791 (2004), a unanimous Supreme Court held that "independent, additional consideration" is required when an employee enters into a subsequent contract with its employer. Fluke's narrow and attenuated reading of *Labriola* contravenes well-established contract law and public policy disfavoring restrictive covenants.

a. **Contracts Must Be Supported by Consideration To Be Enforceable.**

Every contract must be supported by consideration to be enforceable. 25 WASH. PRAC., CONTRACT LAW & PRAC. § 2:23. A subsequent agreement, or modification to an original agreement, must have separate consideration to be valid. *See Dragt v. Dragt/DeTray, LLC*, 139 Wn. App. 560, 571, 161 P.3d 473 (2007). The sufficiency of consideration is reviewed as a question of law, and is often a summary judgment issue. 25 WASH. PRAC., CONTRACT LAW & PRAC. § 2:23.

In *Labriola*, the Supreme Court rejected an employer's claim that continued employment and training served as sufficient consideration for the formation of a binding restrictive covenant signed by an employee five years after his initial hire. *Labriola*, 152 Wn.2d at 834. The Court held that "independent, additional consideration" is required where an employee enters into a subsequent contract with its employer. *Labriola*, 152 Wn.2d at 834.[10] The *Labriola* Court's reasoning applies equally to *any* bilateral agreement entered into by an employee after the initial hire, including the employee nonsolicitation provision imposed four years after Nguyen's hire.[11]

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[10] Other states similarly require independent consideration for an employee's agreement to enter into a restrictive covenant after his or her initial hire. *See, e.g., Nat'l Risk Mgmt., Inc. v. Bramwell*, 819 F.Supp. 417, 429 (E.D. Pa. 1993); *Lucht's Concrete Pumping, Inc. v. Horner*, 224 P.3d 355, 358 (Colo. App. 2009) *cert. granted*, No. 09SC627, 2010 WL 341383 (Colo. Feb. 1, 2010); *Poole v. Incentives Unlimited, Inc.*, 548 S.E.2d 207, 209 (S.C. 2001); *Hejl v. Hood, Hargett & Assocs., Inc.*, 674 S.E.2d 425, 428-429 (N.C. App. 2009).

[11] Appellant's "baseline rule" that an employer may unilaterally modify contract terms applies to unilateral contracts, such as a compensation plan, employee handbook or employee policy. *See* App. Br. at 42 citing *Duncan v. Alaska USA Fed. Credit Union, Inc.*, 148 Wn. App. 52, 77, 199 P.3d 991 (2008) (holding employment agreement "was properly modified because the agreement was a unilateral contract, which was terminable at will"). Here, the employee nonsolicitation agreement is a bilateral agreement entered into by the employee and the employer. It is not a unilateral promise to provide certain benefits.

Fluke argues that consideration is not required here because, unlike a noncompetition provision, an employee nonsolicitation clause does not threaten a person's livelihood. App. Br. at 43-44. This argument is misplaced. Whether a subsequent employee nonsolicitation agreement requires consideration is a question of contract law distinct from the policy question of whether such an agreement, which directly affects the livelihood and freedom of employment of the employees being solicited, is a reasonable restraint of trade. *See* Section IV.A.2 *infra*. Moreover, Fluke's agreement expressly recites the purported consideration given, and in so doing, tacitly recognizes the necessity of consideration. CP 1349.

b. **Fluke's Promise To Make Nguyen (Re)Eligible for Option Grants Is Illusory.**

Fluke's alternative argument that the employee nonsolicitation clause was supported by consideration also fails as a matter of law. To determine the sufficiency of consideration, the court compares the status of the parties before and after the restrictive covenant. *Labriola,* 152 Wn.2d at 836. A grant of unvested shares of stock, which merely gives an expectation of rights in the future and no enforceable rights in stock, is illusory. *MSC Indus. Direct Co. v. Steele*, No. COA08-418, 2009 WL 2501762, at **4-5 (N.C. App. Aug. 18, 2009). Likewise, granting eligibility for a discretionary bonus cannot constitute consideration because it is too indefinite to be considered an enforceable promise. *See, e.g.*, *Heuser v. Kephart*, 215 F.3d 1186, 1192 (10th Cir. 2000) ("[W]here the purported promise to perform actually leaves it to the discretion of the promisor, the alleged promise is illusory and not consideration as a matter of law."); *Wilmar, Inc. v. Liles*, 185 S.E.2d 278, 282-83 (N.C. App. 1971) (rejecting as consideration a profit sharing plan where the amount given under the plan was subject to the employer's discretionary amendment). Because Nguyen was already eligible for future grants of stock options, granting him eligibility for future awards was not legal consideration for the employee nonsolicitation obligation.

Moreover, the Standard Agreement's plain language describes the consideration as "the Associate's *eligibility* to be *considered* for *recommendation* of annual option grants." CP 1349 (emphasis added). This is not a promise of "future stock option awards." *See* App. Br. at 44. It does not obligate Fluke to award stock options to Nguyen, or even to consider Nguyen for an award of stock options. It is merely a highly indefinite "promise" to possibly consider someone for a *recommendation* of *discretionary* benefits. The provision imposes no obligation (let alone a new obligation) on Fluke, nor confers any benefit on Nguyen. It is no more consideration than continued employment of an at-will employee, which the *Labriola* court held to be inadequate consideration to support such an agreement.

2. <u>The Employee Nonsolicitation Provision Is Also Unenforceable As an Unlawful Restraint of Trade.</u>

This court should affirm the dismissal of Fluke's contract claim against Nguyen as a matter of law for the alternative and independent reason that the employee nonsolicitation clause is unreasonably broad and violates Washington's public policy prohibiting contracts in restraint of trade. *See* RCW 19.86.030 ("Every contract, combination, in the form of trust or otherwise, or conspiracy in restraint of trade or commerce is hereby declared unlawful."); *see also Island Air, Inc. v. La Bar*, 18 Wn. App. 129, 139, 566 P.2d 972 (1977) ("[C]ontracts in general restraint of trade are void and unenforceable. . . ."). Contracts that "partially" restrain trade are disfavored and are enforceable only if reasonable. *Island Air*, 18 Wn. App. at 139; *see also Organon, Inc. v. Hepler*, 23 Wn. App. 432, 436, 595 P.2d 1314 (1979). A covenant not to compete or solicit is a restraint of trade, and may be enforced only if reasonable. *See Wood v. May*, 73 Wn.2d. 307, 309, 438 P.2d 587 (1968); *Copier Specialists, Inc. v. Gillen*, 76 Wn. App. 771, 773, 887 P.2d 919 (1995) (citing *Sheppard v. Blackstock Lumber Co.*, 85 Wn.2d 929, 931, 540 P.2d 1373 (1975)).

Whether a covenant is reasonable depends on three factors: (1) whether restraint is necessary for the protection of legitimate business interests of the employer, (2) whether it imposes upon the employee any greater restraint than is reasonably necessary to secure the employer's business or goodwill and (3) whether the degree of injury to the public is such loss of the service or skill of the employee as to warrant non-enforcement of the covenant. *Copier Specialists*, 76 Wn. App. at 773. As the material facts of this case are undisputed, the employee nonsolicitation covenant is unenforceable as a matter of law. *See Knight, Vale & Gregory v. McDaniel*, 37 Wn. App. 366, 368, 680 P.2d 448 (1984) (summary dismissal proper where facts regarding contract and violation are undisputed).

a. <u>Maintaining Continuity of Workforce Is Not a Legitimately Protected Interest.</u>

The vast weight of authority holds that an employer's business interest in the continuity of an at-will workforce is not sufficient to justify a restrictive covenant. *See, e.g., Lazer, Inc. v. Kesselring*, 823 N.Y.S.2d 834, 839 (2005); *Unisource Worldwide, Inc. v. Carrara*, 244 F. Supp. 2d 977, 983 (C.D. Ill. 2003) (only two business interests are legitimately protected by restrictive covenants: "near permanent" relationships with customers and confidential information or trade secrets). Fluke cites one Illinois case for the proposition that employers have a legitimate interest in maintaining a stable workforce. App. Br. at 43 (citing *Automated Concepts, Inc. v. Weaver*, No. 99 C 7599, 2000 WL 1134541, at *4 (N.D. Ill. Aug. 9, 2000)). But Washington disfavors covenants in restraint of competition. *Organon, Inc.*, 23 Wn. App. at 436 (covenant not to compete is in restraint of trade and is disfavored).

As Justice Madsen stated in her concurring opinion in *Labriola*, "[n]on-compete agreements designed to stabilize a company's current workforce through unreasonable restraints are similarly unenforceable." *Labriola*, 152 Wn.2d at 847 (Madsen, J., concurring). Justice Madsen found persuasive *Schmersahl, Treloar & Co. v. McHugh*, 28 S.W.3d 345, 350 (Mo. App. 2000), where the Missouri Court of Appeals held a covenant not to solicit employees unenforceable because "an employer does not have a propriety interest in its employees at will or in their skills." *Id*;[12] *see also Woody v. Stapp,* 146 Wn. App. 16, 23, 189 P.3d 807 (2008) (no legitimate business expectancy in continued employment of at will employee). Here, Fluke has no legitimate interest justifying the employee nonsolicitation clause that is the linchpin of its claim against Nguyen and companion claim against MET.

b. The Restraint Imposed by the Employee Nonsolicitation Clause Is Greater Than Is Reasonably Necessary.

Fluke's employee nonsolicitation provision is also unenforceable because it is grossly overbroad. Public policy requires courts to examine restrictive covenants carefully to ensure that they are no greater in scope than necessary to protect a legitimately protected employer interest. *Knight*, 37 Wn. App. at 370 (limiting enforcement of covenant to clients with whom employee had contact as a direct result of employment); *see also Alexander & Alexander, Inc. v. Wohlman*, 19 Wn. App. 670, 687-688, 578 P.2d 530 (1978) (limiting geographic and temporal scope of restrictive covenant not to compete).

[12] In 2001, the holding in *Schemersahl* was legislatively overruled in part, but courts have continued to adopt its reasoning. *See, e.g., Lazer, Inc.* 823 N.Y.S.2d at 839; *Unisource Worldwide*, 244 F. Supp. 2d at 983.

The scope of Fluke's employee nonsolicitation clause is extraordinary. It prohibits Nguyen from soliciting any and all employees and independent contractors not just of Fluke, but also of Danaher and its hundreds of subsidiaries, in any position – e.g., even clerical and janitorial staff. CP 1346-50. It prohibits Nguyen even from talking to a Fluke employee who was independently considering moving to MET. CP 1346-50. The employee nonsolicitation clause is far broader than necessary to protect any legitimate Fluke interests.

Furthermore, an employer's ability to protect its interests by drafting more narrowly tailored, alternative restrictions is relevant in reviewing the reasonableness of the covenant. *See Kitsap County v. Mattress Outlet v. Gould*, 153 Wn.2d 506, 515, 104 P.3d 1280 (2005). In holding an employee nonsolicitation agreement unenforceable, the Missouri appellate court noted that an employer could protect itself from competition from employees by entering into valid covenants to prevent the solicitation of customers or the disclosure of trade secrets. *Schmersahl*, 28 S.W.3d at 351.

The same is true here. Fluke can and did (except in cases of employees transferring from other Danaher subsidiaries) protect its trade secrets or confidential information through a confidentiality clause. Fluke can protect its relationships with customers through a noncompetition agreement or a narrowly tailored clause directed at solicitation of customers, not fellow employees. An overbroad employee nonsolicitation clause is simply unnecessary to protect Fluke's *legitimate* interests.

c. <u>**Injury to the Public's Interest in a Mobile Workforce and Fair Competition Also Warrant Non-Enforcement.**</u>

Washington has long been an "at-will" employment state. Absent a contract prohibition, an employee has "the absolute right to abandon his or her employment at-will." *Ford v. Trendwest Resorts*, 146 Wn.2d 146, 152 , 43 P.3d 1223 (2002); *Lasser v. Grunbaum Bros. Furniture Co.*, 46 Wn.2d. 408, 410-411, 281 P.2d 832 (1955). This basic freedom is an important part of the healthy competition inherent and necessary to our employment system:

> Nobody has ever thought, so far as we can find, that in the absence of some monopolistic purpose every one has not the right to offer better terms to another's employe, so long as the latter is free to leave. The result of the contrary would be intolerable, both to such employers as could use the employe more effectively and to such employes as might receive added pay. It would put an end to any kind of competition.

Triangle Film Corp. v. Artcraft Pictures Corp., 250 F. 981, 982 (2d Cir. 1918) (Learned Hand, J.); *accord, Knight*, 37 Wn. App. at 370 (public policy requires careful examination of restrictive covenants, even when legitimate business interest exists, because of equally competing concerns of freedom of employment and public access to professional services).

Enforcement of the employee nonsolicitation clause at issue here would unreasonably threaten, and overly restrict, freedom of employment. It interferes with competition between employers for the best use of this state's workforce, and inhibits the workforce from receiving the best pay and benefits for its desired services. Fluke's asserted interests do not outweigh these important concerns. Fluke's restrictive covenant is not reasonable and is unenforceable as a matter of law.

3. The Trial Court Acted Well Within Its Discretion in Denying Appellants' Rule 56(f) Motion.

The trial court, which presided over the parties' discovery disputes for many months, properly exercised its discretion in denying Fluke's request to continue the summary judgment hearing. *See Bldg. Indus. Ass'n of Wash. v. McCarthy*, 152 Wn. App. 720, 742-43, 218 P.3d 196 (2009) (denial of CR 56(f) continuance reviewed for abuse of discretion). "The trial court may deny a [CR 56(f)] motion when (1) the requesting party does not have a good reason for the delay in obtaining the evidence, (2) the requesting party does not indicate what evidence would be established by further discovery, or (3) the new evidence would not raise a genuine issue of fact." *Id.* Mere lack of discovery is insufficient to warrant a continuance of a summary judgment motion under CR 56(f).[13] The discovery must be *necessary* to oppose summary judgment. *Tellevik v. Real Property Known as 31641 W. Rutherford St.*, 120 Wn.2d. 68, 91,

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[13] Respondents deny Appellants' accusations regarding discovery obstruction. MET consistently and properly objected to Fluke's discovery requests to the extent they broadly seek proprietary or confidential Milwaukee Tool information without first identifying with particularity the nature of the trade secrets allegedly misappropriated. *See, e.g., SmithKline Beecham Pharms. Co. v. Merck & Co.* 766 A.2d 442 (Del. Super. 2000). Fluke was ordered to identify its trade secrets with particularity first, but Fluke never did so. From the outset, Fluke's failure to comply with its own discovery obligations was the source of any discovery "obstruction" in the case.

838 P.2d 111 (1992).

Fluke failed to identify what discovery was necessary to oppose Nguyen's motion for summary judgment, which challenged enforcement of the employee nonsolicitation provision on the legal grounds that it was unenforceable for lack of consideration and was an unenforceable restraint of trade. Fluke's request for factual discovery of other "examples of Nguyen actively recruiting Fluke's employees" had no bearing on these legal issues. CP 1313-14, 1656-68. Fluke had all relevant documents, and no additional production would change the standards of law by which its claims failed. *See* CP 1633-40, 1641-52. The trial court's denial of Fluke's CR 56(f) motion was well within the trial court's sound discretion.

4. <u>The Trial Court Properly Exercised Its Discretion in Denying Fluke's Belated Motion for Leave To Amend.</u>

The trial court also had ample discretion to refuse leave to amend, after granting summary judgment of dismissal. *See In re Disciplinary Proceedings Against Bonet*, 144 Wn.2d 502, 510, 29 P.3d 1242 (2001) (grant or denial of motion for leave to amend is a discretionary act). Under this standard, the denial of a motion to amend may be reversed only when no reasonable person would take the view adopted by the trial court. *Id.*

In particular, a trial court may deny a motion to amend after the trial court has granted summary judgment dismissing all claims with prejudice, and where the movant fails to establish that the "new" legal claims could have been made in advance of summary judgment, had he exercised due diligence. *See Kwiatkowski v. Drews*, 142 Wn. App. 463, 497-98, 176 P.3d 510(2008). Denying a motion for leave to amend where the amended claim is futile is not an abuse of discretion. *Nakata v. Blue Bird, Inc.*, 146 Wn. App. 267, 278, 191 P.3d 900 (2008).

Here, Fluke moved for leave to amend to add entirely new claims <u>after</u> summary judgment briefing had closed, on the eve of oral argument and the close of discovery.[14] Briefing on Fluke's motion concluded after the court had dismissed Fluke's claims. Its proposed amendments alleged trade secrets misappropriation and common law claims against Nguyen (and derivative claims against MET) arising from Nguyen's knowledge of "good" OEM suppliers in Asia. CP 1863-78. But Fluke was on notice of these claims since the early stages of the case. CP 5659-71, 7537-647. Yet in numerous prior amendments to pleadings and discovery responses, Fluke never once articulated a trade secrets claim based on the identity of "good" OEM suppliers.

In denying the motion to amend as futile, the trial court expressly noted that Fluke witnesses testified that knowledge of "good" OEM suppliers is not a trade secret. CP 2389. The trial court properly considered the futility of the amended claims and the prejudice to

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[14] Fluke's motion was filed Thursday afternoon, September 18, 2009. Summary judgment argument was set for the next morning, on September 19, and discovery was set to close on the next business day, on Monday, September 22.

defendants that would accrue by reopening discovery to allow them to defend against the amended claim. *Id.* ("[T]he amendments appear to be futile in light of testimony of Fluke witnesses that undermine its claims.") The trial court's order denying Fluke's motion to amend was soundly within its discretion, and should not be disturbed on appeal.

B. The Trial Court Properly Dismissed Fluke's Trade Secret and Related Common Law Claims Against Morrow and MET.

1. Fluke's Evidence Was Insufficient To Establish a Genuine Issue of Material Fact on All Elements of Its Trade Secret Claims.

A trade secret plaintiff must demonstrate: (1) the existence of a trade secret; (2) the misappropriation by the defendant; and (3) resultant damages. *See* RCW § 19.108.010; *Ed Nowogroski Ins., Inc. v. Rucker*, 137 Wn.2d 427, 971 P.2d 936 (1999). Summary judgment was proper because Fluke failed to present sufficient evidence to create an issue of fact that would justify a trial on several elements of its trade secrets claims. *See Young v. Key Pharms.*, 112 Wn.2d 216, 225-27, 770 P.2d 182 (1989) (defendant may carry its initial burden on summary judgment by asserting that no competent evidence supports the elements of plaintiff's claims).

a. Fluke's Evidence Does Not Establish a Question of Fact of the Existence of Trade Secrets.

It is Fluke's burden to prove that legally protectable secrets exist. *Petters v. Williamson & Assocs.*, 151 Wn. App. 154, 164, 210 P.3d 1048 (2009). Summary judgment is appropriate in a trade secrets case when a party fails to meet its burden of proof with evidence generating a genuine issue of material fact. *MP Med., Inc. v. Wegman*, 151 Wn. App. 409, 420, 213 P.3d 931 (2009). Merely labeling information as a trade secret does not establish the existence of a trade secret. *Id.* at 421 n.40.

The plaintiff must show: (1) that the information derives independent economic value from not being generally known or readily ascertainable to others who can obtain economic value from knowledge of its use, and (2) that reasonable efforts have been taken to maintain the secrecy of the information. *Precision Moulding & Frame, Inc. v. Simpson Door Co.*, 77 Wn. App. 20, 25, 888 P.2d 1239 (1995); *see also* RCW 19.108.010(4). The information must be novel and unique. *Woo v. Fireman's Fund Ins. Co.*, 137 Wn. App. 480, 489, 154 P.3d. 236, *rev'd in part on other grounds*, 161 Wn.2d 43, 164 P.3d 454 (2007). Information already in the public domain or readily ascertainable by proper means by someone who can derive economic benefit from it, regardless of its application, is not novel and derives no independent economic value from not being known. *Precision Moulding*, 77 Wn. App. at 26-27; *cf. Stampede Tool Warehouse, Inc. v. May*, 651 N.E.2d 209, 215 (Ill. App. 1995) (key factor is ease with which information can be readily duplicated without considerable time, effort or expense).

Whether or not a particular item of information is a trade secret will depend upon the factual circumstances of a given case. *See* 16A WASH. PRAC., TORT LAW & PRAC. § 22.31. Thus, the fact that a type of business document has been considered a trade secret in other contexts in other jurisdictions does not prove its status as a trade secret in every case. *See, e.g, Ed Nowogroski*, 137 Wn.2d at 449 (discussing how customer lists have and have not been found to be trade secrets depending on facts of case); *MP Med.*, 151 Wn. App. at 420-21 (summary judgment where plaintiff failed to meet burden of proof that customer list was trade secret).

To avoid summary judgment, a plaintiff "must describe its trade secret with a 'reasonable degree of precision and specificity . . . such that a reasonable jury could find that plaintiff established each statutory element of a trade secret.'" *Savor, Inc. v. FMR Corp.*, No. Civ.A 00C-10-149JRS, 2004 WL 1965869, at *6 (Del. Super. July 15, 2004). Disclosure must be with sufficient particularity to distinguish trade secrets from matters of general knowledge or special knowledge of persons skilled in the trade, and what suffices to meet this standard depends on the case. *Advanced Modular Sputtering, Inc. v. Superior Court*, 132 Cal. App. 4th 826, 835-36, 33 Cal. Rptr. 3d 901 (2005). Trade secret case law[15] uniformly rejects as inadequate mere reference to generic categories or "areas" of trade secrets,[16] vague references to "knowledge" of production

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[15] In adopting UTSA, the Washington Legislature directed that it "be applied and construed to effectuate its general purpose to make uniform the law with respect to the subject of this chapter among states enacting it." RCW 19.108.910. Thus, decisions from other jurisdictions under UTSA are "highly persuasive." *World Wide Prosthetic Supply, Inc. v. Mikulsky,* 640 N.W.2d 764, 768 (Wis. 2002).

[16] *See, e.g., StonCor Group, Inc. v. Campton*, No. C05-1225JLR, 2006 WL 314336, at **1-2 (W.D. Wash. Feb. 7, 2006); *Whyte v. Schlage Lock Co.*, 101 Cal. App. 4th 1443, 1452, 125 Cal. Rptr. 2d 277 (2002) (mere reference to

process,[17] or use of catch-all phrases.[18] Trade secrets consisting of compilations of public information must generally "be identified with even greater specificity."[19]

Most significantly, the particularity standard is not satisfied by mere citation to entire documents and generic descriptions of trade secrets. *See, e.g., Mextel, Inc. v. Air-Shields, Inc.*, No. Civ. A.01-CV-7308, 2005 WL 226112, at *42 (E.D. Pa. Jan. 31, 2005) (summary judgment where plaintiff failed to identify what information in documents was allegedly secret). Courts frequently dismiss trade secret claims under CR 56 where, as here, there has been a failure to sufficiently identify the trade secret at issue.[20] In *IDX Sys. Corp. v. Epic Sys. Corp.*, 285 F.3d 581 (7th Cir. 2002),

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"information" about new products failed to differentiate between secret information and information which had been publicly disclosed); *Unicure, Inc. v. Thurman*, 97 F.R.D. 7, 10 (W.D.N.Y. 1982) (generic and conclusory phrases and generalized reference to ratio of ingredients deemed "evasive, ambiguous and incomplete"); *Cromaglass Corp. v. Ferm*, 344 F. Supp. 924, 928 (M.D. Pa. 1972); *Del Monte Fresh Produce Co. v. Dole Food Co.*, 148 F. Supp. 2d 1322, 1325-26 (S.D. Fla. 2001).

[17] *Combined Metals of Chicago, Ltd. v. Airtek, Inc.*, 985 F. Supp. 827 (N.D. Ill. 1997) (trade secret disclosure must identify specific, concrete secrets underlying the process of producing the catalytic converters).

[18] *See, e.g., Imax Corp. v. Cinema Techs., Inc.*, 152 F.3d 1161, 1167 (9th Cir. 1998); *StonCor*, 2006 WL 314336.

[19] *Savor*, 2004 WL 1965869, at *6 (citing *Struthers Scientific & Int'l Corp. v. Gen. Foods Corp.*, 51 F.R.D. 149, 153 (D. Del. 1970)).

[20] *See, e.g., IMAX Corp. v. Cinema Techs, Inc.*, 152 F.3d 1161, 1167-68 (9th Cir. 1998) (granting summary judgment where interrogatory responses failed to specify trade secret claims with sufficient particularity); *VFD Consulting, Inc. v. 21st Servs.*, 425 F. Supp. 2d 1037, 1048-49 (N.D. Cal. 2006) (referring only to "the MedDiag system" and former employee's "experience and best judgment in the combination of the research data" for that system was a "fatal" error because it failed to identify "with any particularity" an alleged trade secret); *Bradbury*

the court dismissed the trade secret claims as a matter of law based on the plaintiff's failure to adequately identify the trade secret at issue:

> "[U]nless the plaintiff engages in a serious effort to pin down the secrets a court cannot do its job. . . . . [Citing to documents describing methods and processes making up a software package] does not separate the trade secrets from the other information that goes into any software package. Which aspects are known to the trade, and which are not? . . . [T]ender of the complete documentation for the software leaves mysterious exactly which pieces of information are the trade secrets. . . . [A] plaintiff must do more than just identify a kind of technology and then invite the court to hunt through the details in search of items meeting the statutory definition."

Id. at 583-84 (citation omitted).

The trial court's holding that Fluke did not meet its burden on summary judgment is entirely consistent with its prior admonition (after reviewing the same evidence at the evidentiary hearing) that the "case is not about trade secrets," and with its order that Fluke identify the trade secrets at issue with particularity. RP 6/3/2008 at 3; CP 985-87. Indeed,

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Co. v. Teissier-duCros, 413 F. Supp. 2d 1209, 1222-24 (D. Kan. 2006) (granting summary judgment where plaintiff provided no detail on technology; plaintiff has the burden under the UTSA "to define its trade secrets with the precision and particularity necessary to separate it from the general skill and knowledge possessed by others"); *Callaway Golf Co. v. Dunlop Slazenger Group Ams., Inc.*, 318 F. Supp. 2d 205, 215-16 (D. Del. 2004) (claim rejected where plaintiff made only "conclusory allegations" about golf ball technology, referring generally to information that former employee obtained); *Glynn Interactive, Inc. v. iTelehealth, Inc.*, No. Civ.A. DKC 2003-0449, 2004 WL 439236, at *5 (D. Md. Mar. 9, 2004) (summary judgment where plaintiff made only generic claim that secrets were in "expertise and information provided" and thus failed to identify alleged secrets); *Julie Research Labs., Inc. v. Select Photographic Eng'g, Inc.*, 810 F. Supp. 513, 520 (S.D.N.Y. 1992) (plaintiff failed to identify an alleged secret separate from public domain information), *aff'd in part and vacated in part on other grounds*, 998 F.2d 65 (2d Cir. 1993).

of the thousands of documents Fluke cited in discovery as containing trade secrets, it proffered only three in opposition to Morrow's motion: (1) a December 2007 marketing plan relating to Fluke's laser distance finders; (2) a summary of interviews with electrical channel distributors; and (3) excerpts of the Cross Market products analysis. But even as to those documents, Fluke failed to identify what specifically within them was a trade secret. Vague references to "future sales projections," unspecified "plans for introducing" a laser distance finder, "information about Fluke's marketing plans" and "internal assessments" of suppliers, or "gaps or 'white spaces' in" the "value segment of the T&M market" are inadequate.

The trial court correctly refused to "hunt through the details in search of items meeting the statutory definition" of information that was not known or obvious to a competitor. *IDX*, 285 F.3d at 584.

b. <u>Fluke's Evidence Does Not Establish a Question of Fact of Misappropriation</u>.

"[I]t is the burden of the [trade secret plaintiff] to demonstrate that [an alleged trade secret] has actually been misappropriated in order to have a right to any damage award." *Petters*, *supra*, 151 Wn. App. at 164. "A nonmoving party . . . may not rely on speculation [or] argumentative assertions . . . [but rather] must set forth specific facts that sufficiently rebut the moving party's contentions and disclose that a genuine issue as to a material fact exists." *Seven Gables Corp. v. MGM/UA Entm't Co.*, 106 Wn.2d 1, 13, 727 P.2d 1 (1986); *see also Retired Pub. Employees*

Council of Wash. v. Charles, 148 Wn.2d 602, 612, 62 P.3d 470 (2003) (nonmoving party may not rely on speculation). Proof of mere *access* to one employer's confidential information does not establish disclosure or misappropriation when employed elsewhere.

Here, there is no actual evidence that Morrow misappropriated anything constituting a trade secret. There was no evidence that Morrow took any confidential or proprietary materials with him. Morrow's SIM card contained no contact information. Ultimately, Fluke offers only unsupported speculation that Morrow copied a PST file, a theory that collapses upon scrutiny of the actual evidence. Similarly, Fluke offered no evidence – direct or circumstantial – to support its speculation that Morrow's "I know stuff" email referred to Fluke's marketing plan for laser distance finders. There is no evidence he even read the document, shared information in it with MET, or that MET's decisions regarding its products were in any way shaped or otherwise impacted by Fluke's plans. Morrow's testimony is unrebutted: the "stuff" he knew was what he learned after trying out some *ultrasonic* distance finders, which he ultimately did not share. CP 1746-47. Even Fluke does not claim that this was a trade secret.

Finally, Morrow's reference in emails to "actionable distributor data" and "low hanging fruit" related to work performed at MET. *Id.* No evidence supports Fluke's hypothesis that Morrow was actually referring to information in the Amprobe Rep Performance Market Research Report

(CP 3963-75), or that MET's actions were affected by information therein. Nor is there evidence that Morrow remembered, much less used, information in the Cross Market Analysis (CP 7472-533), or that it influenced MET's decisions before Morrow joined MET regarding products in a different market segment.[21]

2. **<u>Fluke Failed To Distinguish Its Common Law Claims From Its Trade Secret Claims</u>.**

Washington's Uniform Trade Secrets Act ("UTSA") preempts other causes of action related to the misappropriation of a trade secret. RCW 19.108.900.[22] Washington cases interpreting this statute draw a theoretical distinction between the statutory trade secret and common law breach of confidentiality claims. *See Boeing Co. v. Sierracin Corp.*, 108 Wn.2d 38, 48, 738 P.2d 665 (1987). But common law claims are nevertheless preempted if the facts asserted in support of them are the same, and not independent from, facts offered in support of trade secrets claims. *Thola v. Henschell*, 140 Wn. App. 70, 82, 164 P.3d 524 (2007) (common law claims for use of confidential information preempted to extent the same evidence constitutes trade secret misappropriation).

Fluke's common law claims for breach of "confidential relationship" and duty of loyalty were premised on the same evidence as

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[21] The document is far too large to infer that Morrow somehow memorized it.

[22] The UTSA "displaces conflicting tort, restitutionary, and other law of this state pertaining to civil liability for misappropriation of a trade secret. . . . [but] does not affect: (a) [c]ontractual or other civil liability or relief that is not based upon misappropriation of a trade secret. . . ." RCW § 19.108.900.

its trade secret claims – Morrow's alleged sharing and use of "confidential and proprietary information and trade secrets with" MET. CP 248. As Fluke refused to clarify what "confidential" information in particular was the subject of Fluke's breach of confidential relationship claim (CP 7300-03), any common law confidentiality claims were preempted.[23]

3. <u>The Trial Court Properly Dismissed Fluke's Contract Claims Against MET and Morrow</u>.

The Court of Appeals' holding that "Fluke has no legal rights under the Agreement" is binding as the law of the case. COA Opinion at 12. *See* RAP 12.2; *State v. Schwab*, 163 Wn.2d 664, 672, 185 P.3d 1151 (2008) ("[O]nce there is an appellate court ruling, its holding must be followed in all of the subsequent stages of the same litigation."). Fluke nevertheless argues that whether the JCA should be deemed "equitably assigned" to Fluke is a factual issue. Fluke is wrong.

First, Fluke's *standing* to enforce the JCA via "equitable" assignment is a red herring. Fluke could acquire by assignment – express or equitable – no more than what Jacobs Chuck had to assign.[24] This

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[23] Alternatively, Fluke's common law claims failed for the same reasons as Fluke's trade secret claims – inadequate identification of the confidential information at issue, lack of evidence of misappropriation, and as discussed below, no evidence of causal damages.

[24] *Moore v. Weinberg*, 644 S.E.2d 740, 745 (S.C. App. 2007) (assignee stands in shoes of assignor) *aff'd*, 681 S.E.2d 875 (2009); *Singletary v. Aetna Cas. & Sur. Co.*, 447 S.E.2d 869 (S.C. App. 1994) (same); *Twelfth RMA Partners, L.P. v. Nat'l Safe Corp.*, 518 S.E.2d 44, 46 (S.C. App. 1999) (assignee has same rights and privileges as the assignor); *Trancik v. USAA Ins. Co.*, 581 S.E.2d 858, 861 (S.C. App. 2003) (assignee received no greater rights than had assignor); *Rosemond v. Campbell*, 343 S.E.2d 641, 645 (S.C. App. 1986) (at common law, assignee's rights can be no greater than those of assignor).

court construed as a matter of law what Jacobs Chuck has to assign: an agreement that "by its plain terms . . . remain[ed] in effect only as to 'the Company,' which is Jacobs Chuck, and [which] expired 12 months after Morrow's termination from Jacobs Chuck." COA Opinion at *5. Equitable assignment of an agreement not to compete with Jacobs Chuck that expired in 2005 would be significant only if the term "the Company" was amended to refer to Fluke. Amendments had to be in writing signed by Jacobs Chuck and Morrow. JCA ¶ 13. No such amendment exists.

Second, this court's ruling was not limited to the construction of the JCA; it also held that Fluke had to prove equitable assignment by "clear and specific" evidence of "the conduct of the parties. . . ."." COA Opinion at *5. This court held that Fluke's evidence – the transmittal of the personnel file to Fluke, Fluke's maintenance of that file apart from its own personnel records, Loring's testimony of Fluke's unexpressed subjective intent in requesting the file, etc. – failed to meet this standard. Its holding remains the law of the case

Fluke's attempt to save its claims with duplicative declarations does not compel a different outcome on remand. The testimony of subjective intent of other Fluke and Jacobs Chuck employees regarding, e.g., sending the Jacobs Chuck personnel file to Fluke, why Fluke's practice of "assuming" agreements with prior agreements was appropriate, or in making cryptic notes in Morrow's file,[25] simply mimicked that of

[25] *See* CP 1071-89. The author of notes on a fax cover sheet in Fluke's file stating

Kurt Loring, whose testimony was part of the record that this previously court held was inadequate to meet Fluke's burden. Such testimony of unexpressed subjective intent is no more relevant to determining the intent of parties regarding an "equitable" assignment than it is in assessing the parties' intent in interpreting a written assignment. *Cf. Lynott v. Nat'l Union Fire Ins. Co.*, 123 Wn.2d 678, 684, 871 P.2d 146 (1994). Otherwise, the "equitable assignment" doctrine would be abused by parties collusively trying to prove an assignment after the fact.

This court held that an equitable assignment may be imposed only based on "clear and specific" objective evidence of the conduct of the parties. The *objective* evidence offered on summary judgment was no different than that before: Jacobs Chuck sent the file to Fluke, which contained the JCA and other documents. Fluke maintained that file separately from its own personnel records. Affiliated Fluke entities did *not* assume prior agreements, but rather had transferring employees sign new agreements. Fluke does not advise its hires that non-competition agreements signed with one Danaher subsidiary followed them to other subsidiaries. Morrow was not told that during his interview, and Fluke's

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"Danaher Transfer Signed agreement already done Needs to be sent from Jacobs Chuck" (CP 1084), stated that she intended to refer to the JCA. But the objective evidence consists of the fax attachment, which was Morrow's signed acceptance of Fluke's offer including comments regarding reimbursement of moving expenses (Ex. 37, *see also* Ex. 31) and the next document in Fluke's file, which was not the JCA, but rather the signed agreement regarding repayment of moving expenses. Ex. 31.

offer was not conditioned on being subject to a noncompetition agreement. Fluke no longer "assumes" prior agreements.[26] Fluke failed to establish by clear and specific evidence an intent to assign the JCA upon transfer.

The transfer clause in the JCA highlights the mechanism contemplated by the JCA that Fluke easily could have, but did not, employ to protect its interests: condition Morrow's offer on signing a noncompetition agreement, and require that he sign one more form agreement. Fluke never addresses this critical aspect of this court's holding – that an equitable assignment may be imposed only to avoid injustice. That remains the law of the case.

The trial court correctly applied the standards of this court's prior opinion in the case in dismissing Fluke's contract claims against Morrow and tortious interference claims against MET.

4. <u>Fluke's Claims May Also Be Dismissed for Lack of Evidence of Damages</u>.

A plaintiff may "recover damages for the actual loss . . . [or] for the unjust enrichment caused by misappropriation that is not taken into account in computing damages for actual loss." RCW 19.108.030(1). But Fluke offered no evidence that any act of any defendant caused any compensable damages. All of Fluke's claims should also be dismissed for lack of evidence of causal damages.[27]

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[26] RP 5/21/2008 at 699, 768, 775-83, 790-99, 828-29, 860-62, 870.

[27] This court may affirm on any basis supported by the record. *Mudarri v. State*, 147 Wn. App. 590, 600, 196 P.3d 153 (2008), *review denied*, 166 Wn.2d 1003,

a. **<u>No Evidence of Damages Caused By Morrow.</u>**

Damages in general and under UTSA must be proven with reasonable certainty and not speculation.[28] Actual losses under the UTSA are those that compensate for and repay a proven loss, including lost profits. *Eagle Group*, 114 Wn. App. at 420-20. Lost profits may be recovered only if they are the proximate result of a defendant's breach, and are proven with reasonable certainty.[29] Conversely, "damages which are remote and speculative cannot be recovered." *Tiegs*, 135 Wn.2d at 18.

Fluke offered no evidence of profits lost by Fluke or realized by MET that were caused by any alleged misconduct. Indeed, MET had not yet released any competing product when the trial court dismissed Fluke's last claims. Fluke's damage theory was for recovery of *projected* Fluke losses or MET gains caused by misappropriation. Fluke's proposed methods of calculating these amounts were both based on projected MET sales, and it was Fluke's burden to prove this essential variable.[30] But Fluke offered no estimate or supporting evidence of that or other variables.

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208 P.3d 1123 (2009).

[28] *Eagle Group, Inc. v. Pullen*, 114 Wn. App. 409, 418, 58 P.3d 292 (2002); *McKernan v. Aasheim*, 102 Wn.2d 411, 421-22, 687 P.2d 850 (1984); *Seattle & Mont. Ry. Co. v. Gilchrist*, 4 Wash. 509, 515, 30 P. 738 (1892).

[29] *Tiegs v. Watts*, 135 Wn.2d 1, 17, 954 P.2d 877 (1998) (citing *Larsen v. Walton Plywood Co.*, 65 Wn.2d 1, 390 P.2d 677 (1964)); *see Farm Crop Energy, Inc. v. Old Nat'l Bank*, 109 Wn.2d 923, 750 P.2d 231 (1988).

[30] RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 45 cmt. f at 516-17 (1995); *Petters*, 151 Wn. App. at 165.

Indeed, one such variable – the amount of Fluke's losses or MET's profits caused by Morrow's alleged misappropriation – is precisely what its vice president Konopa swore that Fluke could *never* prove. RP 5/20/2008 at 310. Konopa's admission is grounds to dismiss all of Fluke's claims.[31]

Fluke's claim that it was prejudiced because it did not obtain discovery from MET regarding its projected sales and profit margins is unfounded. Fluke conceded that MET's T&M division would have to be treated as a new business. Any claim to recover lost profits or for disgorgement based on MET's projected sales and profits would be governed by Washington's "new business" rule, under which projected profits must be estimated based on an analysis of market conditions and a profit showing of *identical or similar businesses* in the vicinity. *Farm Crop Energy*, 109 Wn.2d at 928. The requisite evidence, therefore, had to come not from MET, but from other sources. Fluke's and MET's discovery disputes had no impact on Fluke's ability to amass such evidence in the 18 months since the case was filed. Accordingly, the trial court correctly denied Fluke's motion for a continuance pursuant to CR 56(f) after Fluke failed to meet its burden of proving damages.

b. **Fluke's Claims Are Barred By Collateral and Judicial Estoppel.**

Fluke's claims are also barred by collateral and judicial estoppel.

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[31] Konopa's testimony suffices to carry Respondents' burden of proving the lack of restitutionary damages caused by alleged misappropriation. *See Petters*, 151 Wn. App. at 165.

The collateral estoppel doctrine – issue preclusion – prevents relitigation of an issue previously litigated by the same parties. *Shoemaker v. City of Bremerton*, 109 Wn.2d 504, 507, 745 P.2d 858 (1987). To establish the inadequacy of its legal remedy (damages), Fluke contended that it would be unable to distinguish between profits lost as a result of Respondents' alleged misconduct, and profits lost due to legitimate competition by MET. It prevailed on that issue when the trial court granted preliminary injunction. Fluke is foreclosed from relitigating the same issue to a different outcome. As a matter of law, Fluke cannot recover damages that were already adjudicated "unprovable."

The judicial estoppel doctrine also applies to prevent Fluke from "asserting one position in a court proceeding and later seeking an advantage by taking a clearly inconsistent position." *CHD, Inc. v. Taggart*, 153 Wn. App. 94, 101, 103-04, 220 P.3d 229 (2009); *Arkison v. Ethan Allen, Inc.*, 160 Wn.2d 535, 538, 160 P.3d 13 (2007). Its purpose is to prevent the perversion of the judicial process that would inure were a party allowed to play fast and loose by gaining an advantage by litigation on one theory, and then changing positions based on the exigencies of the moment to obtain an inconsistent advantage based on an incompatible theory. *See Skinner v. Holgate*, 141 Wn. App. 840, 849, 173 P.3d 300 (2007); *New Hampshire v. Maine*, 532 U.S. 742, 749-50 (2001). Its application is guided by three core factors: (1) is a party's later position inconsistent with its earlier position; (2) would judicial acceptance of the later position create the perception that the court was previously misled; and (3) would the party asserting the inconsistent position derive an unfair advantage or impose an unfair detriment on the other party if not estopped? *Arkison*, 160 Wn.2d at 538-39; *CHD, Inc.*, 153 Wn. App. at 101; *Skinner*, 141 Wn. App. at 848.

Here, Fluke asserted factually that it would be unable to prove what losses were caused by Respondents' tortious conduct. The trial court accepted this evidence in granting injunctive relief. Fluke then reversed itself in opposition to summary judgment, claiming that it could, in fact, prove the damages caused by improper conduct. There would be no threat to judicial integrity only if the court had *not* accepted Flukes's prior position. *New Hampshire*, 532 U.S. at 750-51; *Teledyne Indus., Inc. v. Nat'l Labor Relations Bd.*, 911 F.2d 1214, 1218 (6th Cir. 1990). The trial court declined to apply the doctrine of judicial estoppel on the ground that the doctrine is "applied sparingly." RP 9/18/2009 at 69. Application of this doctrine should be based on the facts of this case, not its application in other cases, and in this instance is amply justified.

V. ASSIGNMENTS OF ERROR ON CROSS-APPEAL

1. The trial court erred in entering its Orders dated October 21, 2009, denying Morrow's and MET's motion for fees incurred in defense of claims related to conduct by Morrow, and denying MET"s motion for fees incurred in defense of claims related to conduct of Nguyen. (CP 6018-23)

VI. ISSUES PERTAINING TO ASSIGNMENTS OF ERROR ON CROSS-APPEAL

1. Did the trial court err as a matter of law in holding that Morrow and MET were not entitled to an award of prevailing party attorneys' fees pursuant to RCW 4.84.330, Washington's public policy and equitable grounds of mutuality of remedy, and established equitable grounds requiring an award of fees incurred in obtaining dissolution of wrongfully granted injunctive relief?

2. Did the trial court err as a matter of law in holding that MET was not entitled to prevailing party attorneys' fees incurred in defending tortious interference with contract claims under RCW 4.84.330, where such fees were inseparable from the fees incurred defending the contract claims against Nguyen?

3. Did the trial court abuse its discretion in holding that Morrow and MET were not entitled to an award of prevailing party attorneys' fees incurred in defending against trade secrets claims, in the face of substantial evidence that the claims were maintained in bad faith?

VII. ARGUMENT IN SUPPORT OF CROSS-APPEAL

A. Morrow and MET Are Entitled to Fees Incurred in Obtaining Dissolution of Wrongfully Issued Injunctive Relief.

This court's previous decision established conclusively that the trial court erred in granting injunctive relief and denying Morrow's motion to dissolve the TRO. Except in circumstances inapplicable here, a defendant is entitled as a matter of law to its attorneys' fees and costs incurred in obtaining dissolution of a wrongfully issued injunction. *See Ino Ino., Inc. v. City of Bellevue*, 132 Wn.2d 103, 143, 937 P.2d 154 (1997). The purpose of this rule is to deter a plaintiff from seeking relief prior to a trial on the merits. An injunction is wrongfully obtained where there is a judicial determination establishing the wrongfulness of the restraint based upon the merits of the case. *Swiss Baco Skyline Logging Co. v. Haliewicz*, 14 Wn. App. 343, 346, 541 P.2d 1014 (1975). Only the quantum of fees to be awarded is within the trial court's discretion. *Ino Ino*, 131 Wn. 2d at 143. The trial court's denial of any fees was error.

B. Morrow and MET Are Entitled to Fees Incurred in Defense of Claims Related to the JCA and the Standard Agreement Under RCW 4.84.330 and on Equitable Grounds Requiring Mutuality of Remedy.

The JCA contains a unilateral attorneys' fees provision, allowing an award of fees only to "the Company" if it prevails in a civil action brought for its breach. JCA ¶ 9. As MET and Morrow prevailed on Fluke's claims under the JCA, they are entitled to an award of related fees and costs under RCW 4.84.330 (if any action "on a contract" contains a unilateral fee clause, the prevailing party "shall be entitled to reasonable attorney's fees" and costs). RCW 4.84.330 is mandatory; entitlement to fees is not a matter of discretion. Fees must be awarded pursuant to this statute even though a party prevails by virtue of successfully establishing that no contract ever existed, or that the contract had terminated. *Herzog Aluminum, Inc. v. Gen. Am. Window Corp.*, 39 Wn. App. 188, 191-197, 692 P.2d 867 (1984). The statute applies as long as the contract with the fee provision is central to the controversy. *Hemenway v. Miller*, 116 Wn.2d 725, 742, 807 P.2d 863 (1991). Thus, Morrow and MET are entitled to fees related to their defense of Fluke's contract and derivative tortious interference claims.

While the JCA contains a South Carolina choice of law clause, Fluke alleged that the agreement was governed by Washington law. CP

288-94. Moreover, nothing in RCW 4.84.330 excludes claims brought in Washington on contracts governed by law other than Washington. And even if the law of South Carolina and Washington is in conflict,[32] the right to fees requires a choice of law analysis distinct from determining the law that governs interpretation of a contract. *See, e.g., Boise Tower Assocs. v. Wash. Capital Joint Master Trust Mortgage Income Fund*, No. 03-141-S-MHW, 2007 WL 4355815, at **3-4 (D. Idaho Dec. 10, 2007) (law governing underlying cause of action, e.g., breach of contract, does not automatically control fee issue); *see also Arno v. Club Med Boutique, Inc.*, 134 F.3d 1424 (9th Cir. 1998). In a Washington case filed by a Washington company (Fluke) that alleged breach of a contract governed by Washington law against its Washington employee (Morrow), where it has been determined that "Fluke has no rights" under the contract in question, Washington's interests prevail.[33]

Finally, Washington law recognizes a public policy and equitable principle of mutuality of remedy in awarding attorneys' fees. *Kaintz v.*

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[32] While South Carolina law does not have a comparable statute, it does apply the doctrine of mutuality of remedy in appropriate circumstances. *See, e.g., Simpson v. MSA of Myrtle Beach, Inc.*, 644 S.E.2d 663, 672 (S.C. 2007).

[33] RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 (1965) (contractual choice of law clause does not apply where law of the chosen state is contrary to a fundamental policy of a state which has materially greater interest in issue). Washington's choice of law jurisprudence applies Section 187 in cases involving choice of law clauses. *See, e.g., Schnall v. AT&T Wireless Servs.*, 168 Wn.2d 125, 131-32, 225 P.3d 929 (2010).

PLG, Inc., 147 Wn. App. 782, 788-89, 197 P.3d 710 (2008). Fees related to claims based on the JCA should have been awarded based on this equitable ground, even if RCW 4.84.330 does not apply. *Kaintz,* 147 Wn. App. at 786-89 (awarding fees based on equitable ground of mutuality of remedy, even though RCW 4.84.330 did not apply).

The Standard Agreement between Fluke and Nguyen, which is governed by Washington law, also contains a unilateral fee clause. While the trial court awarded fees incurred in defending Fluke's contract claims against Nguyen under RCW 4.84.330, it denied recovery of any fees incurred in defending the companion tortious interference claims. CP 6021-23) But a claim for tortiously interfering with Fluke's rights under the Standard Agreement is no less an action "on a contract" than claim for breach of the Standard Agreement itself. *MP Medical*, *supra*, 151 Wn. App. at 426 (affirming award of fees incurred in defending breach of contract claim and companion tortious interference with contract claim); *Deep Water Brewing, LLC v. Fairway Res., Ltd.*, 152 Wn. App. 229, 262-63, 215 P.3d 990 (2009) ("valid contractual relationship" required to establish liability for tortious interference with contract). The trial court should not have excluded recovery of fees incurred, in part, in defense of the tortious interference claims.

Further, Fluke's contract and tortious interference claims related to Nguyen were based on the same facts, and were defended on the same grounds by the same firm, such that fees incurred in defense of these claims were necessarily so inextricably intertwined as to preclude segregation. *MP Medical*, 151 Wn. App. at 426. The trial court should have awarded *all* fees reasonably incurred in defense of the claims against Nguyen, including those that also benefited MET's defense of the tortious interference claim.

C. Respondents Are Entitled to Fees Incurred in Defense of Trade Secret Claims Maintained in Bad Faith.

Respondents were also entitled to an award of fees incurred in defending against Fluke's trade secrets claims under RCW 19.108.040, which allows award of fees for trade secrets claims made in bad faith. A prevailing defendant need not prove that the claims were frivolous to establish bad faith, but rather only that the claims were objectively specious (i.e., a lack of evidence) and brought *or maintained* in subjective bad faith (i.e., to cause unnecessary delay, harass or for an improper motive). *See generally FLIR Systems, Inc. v. Parrish*, 174 Cal. App. 4^{th} 1270, 1275-82, 95 Cal. Rptr. 3d 307 (2009).

Objective speciousness exists where the action superficially appears to have merit but there is a complete lack of evidence to support the claim. *Id.* at 1276. Subjective bad faith may be inferred from evidence that the plaintiff intended to cause unnecessary delay, filed or maintained the action to harass, or harbored an improper motive, e.g., failure to identify the trade secrets at issue with specificity, inflammatory settlement demands,[34] pursuit of claims after their shortcomings are pointed out by opposing counsel, among other potentially relevant facts. *Id.* at 1278-82.

Respondents sought only an award of fees incurred after May 13, 2009, when they pointed out the deficiencies in Fluke's claims and gave it a chance to withdraw. CP 5685-5700. The grant of summary judgment alone establishes the objective speciousness of Fluke's claims. *Flir Sup.*, 174 Cal. App. 4th at 1276-78. There is ample evidence of Fluke's subjective bad faith – an inflammatory settlement offer,[35] Fluke's failure throughout the case to identify the trade secrets at issue, grossly overbroad discovery requests, and its continued pursuit of these claims long after the lack of evidence was called to its attention (in fact, even after its claims were dismissed), and testimony by Fluke's 30(b)(6) witness who quickly admitted the lack of basis for a number of Fluke's claims, and who had done no investigation as to the facts supporting Fluke's trade secrets claims. CP 3819-61.

Unlike the facts in *Precision Airmotive Corp. v. Rivera*,[36] the flaws

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[34] Washington law also allows the admission of settlement offers for purposes of proving the subjective intent of the offering party. *Bulaich v. AT&T Info. Sys.*, 113 Wn.2d 254, 262-64, 778 P.2d 1031 (1989).

[35] Prior to the evidentiary hearing, Fluke made a "settlement offer" that ensured that the litigation – and its rights of discovery – would continue. For example, it demanded that MET fire Mike Jones, disclose sensitive business plans, suppliers and significant customers to Fluke, and pay Fluke $2 million, among other clearly unacceptable terms. Supp. CP _____. Fluke's position changed little throughout the remainder of the case.

[36] 288 F. Supp. 2d 1151 (W.D. Wash. 2003). *Precision Airmotive* is the only

in Fluke's claims were called out in advance of motion practice, and there was ample other evidence of bad faith on Fluke's part in pursing the claims after that date. The trial court erred in refusing to award trade secret fees incurred after May 13, 2009.

D. Respondents Are Entitled to Fees Incurred in This Appeal.

Respondents also respectfully request an award of fees and expenses incurred in defending against Fluke's appeal. RAP 18.1. Fees are proper on each of the grounds relied upon above. *Richter v. Trimberger*, 50 Wn. App. 780, 786, 750 P.2d 1279 (1988) (party entitled to fees in trial court is entitled to fees upon prevailing on appeal).

VIII. CONCLUSION

This court should affirm the summary dismissal of Fluke's claims and denial of its procedural motions, and reverse the trial court's denial of prevailing party fees.

DATED this 5th day of May, 2010.

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case discussing a prevailing defendant's entitlement to fees under RCW 19.108.040. The court denied fees due to the defendant's failure to call out the deficiencies prior to the filing of the dispositive motion, and the lack of other evidence of bad faith.

EDWARDS, SIEH, SMITH
& GOODFRIEND, PS

Howard M. Goodfriend, WSBA # 14355
Attorneys for Evans Nguyen and
Milwaukee Electric Tool Corporation

PROOF OF SERVICE

The undersigned certifies that on the 5th day of May, 2010, he caused to be served in the manner noted below, a copy of Respondents' Brief on the following counsel of record:

VIA EMAIL:

Kevin J. Hamilton
James E. Sanders
Brian M. Flock
Perkins Coie LLP
1201 Third Avenue, 40th Floor
Seattle, WA 98101-3099
Attorneys for Respondents Fluke Corporation and Danaher Corporation

DATED this 5th day of May, 2010.

EXHIBIT A

DANAHER

STANDARD TERMS AND CONDITIONS OF EMPLOYMENT

Danaher Corporation, an "at will" employer, believes that recruiting and retaining the very best people to work in its highly competitive businesses means treating them fairly, rewarding their contributions, and thereby establishing a strong partnership for our collective well-being and continued success. Employment at Danaher and its divisions typically provides associates with specialized and unique knowledge and confidential information, which, if used in competition with Danaher, would cause harm to Danaher. As such, it is reasonable to expect a commitment from our associates that protects Danaher's interests and therefore their own interests. You are encouraged to read and sign this Agreement in the spirit intended: our collective long-term growth and success.

Fluke Corporation, 6920 Seaway Blvd., Everett Washington, ("the Company") and Evans Nguyen, who resides at 12500 S.E. 100 St, Renton, WA, 98056 ("the Associate") agree as follows:

1. General. The Company employs the Associate and the Associate accepts employment to render services on behalf of the Company, subject to the supervision and direction of the President of the Company or his duly authorized designee. Said employment shall continue until the date on which the employment relationship is terminated at the will of either party.

2. Nonpiracy. During the Associate's employment and for one year following the termination of the Associate's employment with the Company, whether the termination is voluntary or involuntary, the Associate will not directly or indirectly, on behalf of himself or herself, or for any other entity, business, or person:

(1) hire, entice, induce, solicit or attempt to hire, entice, induce or solicit any employee of the Company to leave the Company's employ (or the employ of Danaher Corporation ("Danaher") or another subsidiary of Danaher, as applicable) or cause any employee of the Company to become employed in any business that is directly or indirectly competitive with the Company for any reason whatsoever,

(2) assist or encourage in any manner, including without limitation through the providing of advice or information, any employee of the Company to leave the Company's employ (or the employ of Danaher or another subsidiary of Danaher, as applicable), or

(3) suggest or recommend in any manner, including through the providing of advice or information, that any business, person or entity hire, entice, induce, solicit, cause or attempt to hire, entice, induce or solicit or cause any employee of the Company to leave the Company's employ (or the employ of Danaher or another subsidiary of Danaher, as applicable).

For purposes of this Agreement, the term "employee of the Company" shall include each person who as of the date of termination of the Associate's employment is, or at any time within the 6-month period preceding such date was, (1) employed by Danaher or any of its subsidiaries (including without limitation the Company) whether on a full-time or part-time basis, or (2) providing full-time services to, or working as an independent contractor for, Danaher or any of its subsidiaries (including without limitation the Company).

3. Nondisclosure.

(a) The Associate agrees with the Company that he or she will not at any time during the Associate's employment by the Company or at any time after any termination of said employment, whether it be voluntary or involuntary, except in performing his or her employment duties to the Company or any affiliate of the Company under this Agreement, directly or indirectly, use, disclose, or publish, or knowingly or negligently permit others not so authorized to use, disclose, or publish, (1) any information, data or other assets or property of the Company or any of its affiliates, in whatever form, including without limitation the Danaher Business System and any information relating to any current or former employee of the Company, or (2) without limiting the foregoing, any Confidential Information that the Associate may learn or become aware of, or may have learned or become aware of, because of the Associate's prior or continuing employment, ownership, or association with the Company or any predecessors or affiliates thereof, or use, or knowingly or negligently permit others not so authorized to use, any such information in a manner detrimental to the interests of the Company or any affiliates thereof.

(b) The Associate agrees not to use in working for the Company or any of its affiliates and not to disclose to the Company or any affiliate thereof any trade secrets or other information the Associate does not have the right to use or disclose and that the Company and its affiliates are not free to use without liability of any kind. The Associate agrees to inform the Company promptly in writing of any patents, copyrights, trademarks, or other proprietary or intellectual property rights known to the Associate that the Company or any of its affiliates might violate because of information provided by the Associate.

(c) The Associate confirms that all assets and properties of the Company and its affiliates, including without limitation Confidential Information, is and must remain the exclusive property of the Company or the relevant affiliate thereof. All such assets and property, including without limitation all office equipment (including computers) the Associate receives from the Company or any affiliate thereof in the course of the Associate's employment and all business records, business papers, and business documents the Associate keeps or creates, whether on digital media or otherwise, in the course of the Associate's employment relating to the Company or any affiliate thereof, must be and remain the assets and property of the Company or the relevant affiliate. Upon the termination of the Associate's employment with the Company, whether it be voluntary or involuntary, whenever that termination of employment may occur, or upon the Company's request at any time, the Associate must promptly deliver to the Company or to the relevant affiliate all such assets and property, including without limitation any such office equipment (including computers) and any Confidential Information or other records or documents (written or otherwise), and any copies, excerpts, summaries or compilations of the foregoing, made by the Associate or that came into the Associate's possession during the Associate's employment. The Associate agrees that he or she will not retain any such assets or property, including without limitation copies, excerpts, summaries, or compilations of the foregoing information, records and documents.

(d) "Confidential Information" includes, without limitation, any matters protected under the Uniform Trade Secrets Act and any information that neither the Company nor any of its affiliates has previously disclosed to the public with respect to the present or future business of the Company or of any of its affiliates, including their respective operations, services, products, research, inventions, invention disclosures, discoveries, drawings, designs, plans, processes, models, technical information, facilities, methods, systems, trade secrets, copyrights, software, source code, object code, patent applications, procedures, manuals, specifications, any other intellectual property, confidential reports, price lists, pricing formulas, customer lists, financial information (including the revenues, costs, or profits associated with any products or services), Talent Reviews and Organizational Plans, business plans, information regarding all or any portion of the Danaher Business System, lease structure, projections, prospects, opportunities or strategies, acquisitions or mergers, advertising or promotions, personnel matters, legal matters, any other confidential or proprietary information, and any other information not generally known outside the Company and its affiliates that may be of value to the Company or any of its affiliates, but excludes any information already properly in the public domain. "Confidential Information" also includes, without limitation, confidential and proprietary information and trade secrets that third parties entrust to the Company or any of its affiliates in confidence.

(e) The Associate understands and agrees that the rights and obligations set forth in this Nondisclosure section will continue indefinitely and will survive termination of the Associate's employment with the Company.

4. Works-made-for-hire and Intellectual Property.

(a) The Associate agrees that all records (in whatever media), written works, documents, papers, notebooks, drawings, designs, technical information, source code, object code, algorithms, processes, methods, ideas, formulas, inventions (whether patentable or not), invention disclosures, discoveries, improvements, other copyrightable or protected works, or any other intellectual property, developed, conceived, acquired, created, authored, reduced to practice, from which derivative works are prepared, made, invented, or discovered by the Associate (whether or not during usual working hours, and whether individually or jointly with others) that relate to, result from or are suggested by any work or task performed by the Associate for or on behalf of the Company or any affiliate thereof, or that arise from the use or assistance of the facilities, materials, personnel, or Confidential Information of the Company or any affiliate thereof, or that otherwise relate to the actual or anticipated research, development or business of the Company or any affiliate thereof, will be and remain the absolute property of the Company (or the relevant affiliate thereof), as will all the worldwide patent, copyright, trademark, service mark and trade secret rights, any associated registrations, applications, renewals, extensions, continuations, continuations-in-part, requests for continued examination, divisions, or reissues thereof or any foreign equivalents thereof, and all other intellectual property rights relating to the foregoing (all items referred to in this sentence are collectively referred to as the "Intellectual Property"). The Associate irrevocably and unconditionally waives all rights, wherever in the world enforceable, that vest in the Associate (whether before, on, or after the date of this Agreement) in connection with any such Intellectual Property in the course of the Associate's employment with the Company, any affiliate thereof or any predecessor of any of the foregoing. The Associate recognizes all such Intellectual Property constitutes "works made for hire" for which the Company retains all rights, title, and interest to any underlying rights, including copyright protections. If for any reason any such Intellectual Property is not deemed to be a "work made for hire," consistent with the undertakings below, the Associate hereby assigns all rights, title and interest in any such Intellectual Property to the Company (or the applicable affiliate thereof, as directed by the Company).

(b) The Associate will promptly disclose, and hereby grants, and assigns all rights, title, and interest in all Intellectual Property, to the Company (or the applicable affiliate thereof, as specified by the Company) for its or their sole use and benefit. At all times, both during and after the Associate's employment by the Company, the Associate agrees to assist the Company in taking the proper steps, including executing any required documents, to obtain patents, copyrights or other legal protection for the Intellectual Property and to assign such Intellectual Property and the rights to any applications associated therewith to the Company, if the Company so desires, but all at the Company's direction and expense. At all times, both during and after the Associate's employment by the Company, the Associate agrees not to claim any rights to any Intellectual Property as having been created, conceived or acquired by the Associate prior to the Associate's employment by the Company, unless such Intellectual Property is identified on a sheet attached to this Agreement and signed by the Associate as of the date of this agreement.

(c) The Associate understands and agrees that the rights and obligations set forth in this **Works-made-for-hire and Intellectual Property** section will continue indefinitely and will survive termination of the Associate's employment with the Company, whether the termination is voluntary or involuntary.

(d) This agreement does not apply to Intellectual Property for which no equipment, supplies, facilities, or trade secret information of the Company was used and which was developed entirely on the Associate's own time, unless (a) the Intellectual Property relates (i) directly to the business of the Company, or (ii) to the Company's actual or demonstrably anticipated research or development, or (b) the Intellectual Property results from any work performed by the Associate for the Company.

5. Enforceability. It is the intention of the parties that the provisions of the restrictive covenants herein shall be enforceable to the fullest extent permissible under applicable law, but the unenforceability (or modification to conform to such law) of any provision or provisions hereof shall not render unenforceable, or impair, the remainder thereof. If any provision or provisions hereof shall be deemed invalid or unenforceable, either in whole or in part, this Agreement shall be deemed amended to delete or modify, as necessary, the offending provision or provisions and to alter the bounds thereof in order to render it valid and enforceable.

6. Damages and Relief. The Associate acknowledges and agrees that damages are an inadequate remedy for any breach of the terms and conditions set forth in Sections 2, 3, 4 and 12 of this Agreement and agrees that in the event of a breach of such paragraphs, the Company may, with or without pursuing any remedy for damages, immediately obtain and enforce an ex parte, preliminary and permanent injunction prohibiting the Associate from violating this policy. Further, in any civil action brought for a breach of this Agreement, the Company shall be entitled to recover from the Associate all reasonable attorneys' fees, litigation expenses, and costs incurred by Company if the Company prevails in that action.

7. Consideration. The Associate acknowledges and agrees that this Agreement is supported by the Associate's eligibility to be considered for recommendation of annual option grants . The Associate further agrees that such consideration is fair, reasonable and enforceable to its full extent; that the Associate was given adequate time to consider this Agreement; that the Company has an important and legitimate business interest that it is seeking to protect with this Agreement; and that enforcement of this Agreement would not interfere with the interests of the public.

8. Governing Law. This Agreement shall be governed by and construed in accordance with the substantive laws of the State of **Washington** without regard for the choice of law provisions thereof.

9. Termination. The Associate understands, acknowledges and agrees that the obligations and restrictions imposed upon him/her under this Agreement shall apply regardless of whether the termination of his/her employment is voluntary or involuntary, with or without cause.

10. Amendment and Waiver; Entire Agreement. This Agreement shall not be amended except by a written instrument hereafter signed by the Company and the Associate. The failure of the Company to enforce, or delay in enforcing, any term of this Agreement shall not constitute a waiver of any rights or deprive the Company of the right to insist thereafter upon strict adherence to that or any other term of this Agreement, nor shall a waiver of any breach of this Agreement constitute a waiver of any preceding or succeeding breach. No waiver of a right under any provision of this Agreement shall be binding on the Company unless made in writing and signed by the Board of Directors of the Company. This Agreement contains the entire understanding of the Company and the Associate relating to the subject matter hereof and supersedes all prior agreements and understandings relating to the subject matter hereof; provided, that any agreement entered into on or prior to the date hereof between the Associate, on the one hand, and the Company, Danaher and/or any other subsidiary of Danaher on the other hand that contains any provisions relating directly or indirectly to noncompetition and/or nonsolicitation of customers shall remain valid and in full force and effect, and the parties agree that the continued validity and enforceability of any such agreement shall in no way affect the validity or enforceability of any provision of this Agreement.

11. Successors and Assigns. This Agreement shall be binding upon the Associate and his/her heirs, successors, assigns and personal representatives, and inure to the benefit of the Company, its successors and its assigns. The Associate may not assign any rights or duties under this Agreement; the Company may assign any or all of its rights and/or duties herein to Danaher and/or any other subsidiary or subsidiaries of Danaher. The term "affiliate," when used herein, shall not include any officers or directors of the Company or of Danaher.

12. Nondisparagement. The Associate agrees that except as required under the law, the Associate will refrain from making derogatory or disparaging written or oral comments regarding the Company, any of its affiliates or any of their respective products, services or personnel.

13. Acknowledgment of Understanding; Livelihood. The Associate acknowledges that s/he has read this Agreement in its entirety and understands all of its terms and conditions, that s/he has had the opportunity to consult with legal counsel of his/her choice regarding his/her agreement to the provisions contained herein, that s/he is entering into this Agreement of his/her own free will, without coercion from any source, and that s/he agrees to abide by all of the terms and conditions herein contained. The Associate further acknowledges that in consideration of the Associate's right to terminate his/her employment with the Company at any time for any reason, Associate agrees that s/he is employed by the Company on an at-will basis. Nothing contained in this Agreement or elsewhere shall be construed as limiting the effect of

this paragraph. The Associate acknowledges that Associate's knowledge, skills and abilities are sufficient to enable the Associate, in the event of the termination of employment with the Company, to earn a satisfactory livelihood without violating this Agreement.

Associate: [signature] Date: 6/2/04

Company: By: [signature] Date: 6/4/04
Name: [signature]
Title: HR Mgr

[signature] VP, HR 10/26/04

EXHIBIT B

DANAHER

NONCOMPETITION AGREEMENT

Danaher Corporation, an "at will" employer, believes that recruiting and retaining the very best people to work in its highly competitive businesses means treating them fairly, rewarding their contributions, and thereby establishing a strong partnership for our collective well-being and continued success. Employment at Danaher and its divisions typically provides associates with specialized and unique knowledge and confidential information, which, if used in competition with Danaher, would cause harm to Danaher. As such, it is reasonable to expect a commitment from our associates that protects Danaher's interests and therefore their own interests. You are encouraged to read and sign this Agreement in the spirit intended: our collective long-term growth and success.

The Jacobs Chuck Manufacturing Company, Clemson, SC, a division of Danaher Corporation, ("the Company") and Jonathan Morrow who resides at 214 Butler Avenue, Greenville, South Carolina 29601, ("the Associate") agree as follows:

1. General. The Company employs the Associate and the Associate accepts employment to render services on behalf of the Company, subject to the supervision and direction of the President of the Company or his duly authorized designee. Said employment shall continue until the date on which the employment relationship is terminated at the will of either party.

2. Noncompetition and nonsolicitation.

(a) During the Associate's employment with the Company, the Associate shall not directly or indirectly:

(A) perform services of any nature or in any capacity whatsoever for any business, person, or entity which is engaged in product lines which compete with and/or which is in competition with the Company, Danaher Corporation ("Danaher") or any other subsidiary of Danaher;

(B) engage in any product lines which compete with the Company, Danaher or any other subsidiary of Danaher;

(C) except on behalf of the Company, Danaher or any other subsidiary of Danaher, sell, offer to sell or solicit any orders for the purchase of any products and/or services which are the same as or similar to those sold by the Company, Danaher or any other subsidiary of Danaher, to or from any customer, person or entity; or

(D) otherwise perform any services, sell any products or engage in any activities in any capacity whatsoever which are in competition with the Company, Danaher or any other subsidiary of Danaher.

(b) For a 12-month period following the termination of the Associate's employment with the Company, whether the termination is voluntary or involuntary, the Associate will not, directly or indirectly, on behalf of himself or herself or for any entity, business or person other than, the Company, Danaher or any other subsidiary of Danaher:

(A) compete with the Company (for purposes of this Section 2(b)(A), the term "Company" shall be deemed to include, in addition to the Company, all affiliates of the Company with whom the Associate was employed at any time during the 12 month period preceding termination of the Associate's employment with the Company) in North America, Asia, Europe (the "Restricted Area"), or

(i) accept employment (as a director, officer, employee, independent contractor, representative, consultant, member or otherwise) with a business, entity (including without limitation any business or entity started by the Associate) or person that competes directly or indirectly with any product or service of the Company within the Restricted Area,

(ii) provide any services similar to the services the Associate provided to or on behalf of the Company, or any other advice or consulting services, to a business, entity (including without limitation any business or entity started by the Associate) or person that competes directly or indirectly with any product or service of the Company within the Restricted Area, or

(iii) invest in or otherwise hold any interest in (except for passive ownership of up to 3% of the outstanding capital stock of any publicly traded corporation, so long as the Associate complies with clauses (i) and (ii) above), a business, entity (including without limitation any business or entity started by the Associate) or person that competes directly or indirectly with any product or service of the Company within the Restricted Area.

The businesses, entities and persons referred to in this Section 2(b)(A) shall include, without limitation, those businesses, entities and persons referred to on Exhibit A attached hereto.

(B) sell, offer to sell, or solicit any orders for the purchase of, to or from any customer, any products and/or services similar to those upon which or with which the Associate worked, or about which the Associate acquired knowledge, while employed by the Company, Danaher or any other subsidiary of Danaher. For purposes of this Agreement, the term "customer" means any person, business or entity, or any person, business, or entity subject to the control of any such person, business or entity, that during the 24 months immediately preceding termination of Associate's employment with the Company:

(i) sought, inquired about, or purchased any products or services of the Company or of any other Danaher entity for whom Associate worked during such 24 month period (the Company and any such other Danaher entity or entities are referred to as the "Employing Companies");

(ii) contacted any of the Employing Companies for the purpose of seeking or purchasing any products or services of any of the Employing Companies;

(iii) was contacted by any of the Employing Companies for the purpose of selling its products or services; and/or

(iv) received a written and/or verbal sales proposal from any of the Employing Companies.

The foregoing restriction will include, but not be limited to the customers referred to on Exhibit B hereto; or

(C) use, incorporate or otherwise create any business entity or organization or domain name using, any name confusingly similar to the name of Danaher Corporation, of the Company or of any other subsidiary of the Company, or any other name under which any of those entities does business.

3. Nonpiracy. During the Associate's employment and for a 12-month period following the termination of the Associate's employment with the Company, whether the termination is voluntary or involuntary, the Associate will not directly or indirectly, on behalf of himself or herself, or for any other entity, business, or person:

(1) hire, entice, induce, solicit or attempt to hire, entice, induce or solicit any employee of the Company to leave the Company's employ (or the employ of Danaher or another subsidiary of Danaher, as applicable) or cause any employee of the Company to become employed in any business that is directly or indirectly competitive with the Company for any reason whatsoever,

(2) assist or encourage in any manner, including without limitation through the providing of advice or information, any employee of the Company to leave the Company's employ (or the employ of Danaher or another subsidiary of Danaher, as applicable), or

(3) suggest or recommend in any manner, including through the providing of advice or information, that any business, person or entity hire, entice, induce, solicit, cause or attempt to hire, entice, induce or solicit or cause any employee of the Company to leave the Company's employ (or the employ of Danaher or another subsidiary of Danaher, as applicable).

For purposes of this Agreement, the term "employee of the Company" shall include each person who as of the date of termination of the Associate's employment is, or at any time within the 6-month period preceding such date was, (1) employed by Danaher or any of its subsidiaries (including without limitation the Company) whether on a full-time or part-time basis, or (2) providing full-time services to, or working as an independent contractor for, Danaher or any of its subsidiaries (including without limitation the Company).

4. Nondisclosure.

(a) The Associate agrees with the Company that he or she will not at any time during the Associate's employment by the Company or at any time after any termination of said employment, whether it be voluntary or involuntary, except in performing his or her employment duties to the Company or any affiliate of the Company under this Agreement, directly or indirectly, use, disclose, or publish, or knowingly or negligently permit others not so authorized to use, disclose, or publish, (1) any information, data or other assets or property of the Company or any of its affiliates, in whatever form, including without limitation the Danaher Business System and any information relating to any current or former employee of the Company, or (2) without limiting the foregoing, any Confidential Information that the Associate may learn or become aware of, or may have learned or become aware of, because of the Associate's prior or continuing employment, ownership, or association with the Company or any predecessors or affiliates thereof, or use, or knowingly or negligently permit others not so authorized to use, any such information in a manner detrimental to the interests of the Company or any affiliates thereof.

(b) The Associate agrees not to use in working for the Company or any of its affiliates and not to disclose to the Company or any affiliate thereof any trade secrets or other information the Associate does not have the right to use or disclose and that the Company and its affiliates are not free to use without liability of any kind. The Associate agrees to inform the Company promptly in writing of any patents, copyrights, trademarks, or other proprietary or intellectual property rights known to the Associate that the Company or any of its affiliates might violate because of information provided by the Associate.

(c) The Associate confirms that all assets and properties of the Company and its affiliates, including without limitation Confidential Information, is and must remain the exclusive property of the Company or the relevant affiliate thereof. All such assets and property, including without limitation all office equipment (including computers) the Associate receives from the Company or any affiliate thereof in the course of the Associate's employment and all business records, business papers, and business documents the Associate keeps or creates, whether on digital media or otherwise, in the course of the

Associate's employment relating to the Company or any affiliate thereof, must be and remain the assets and property of the Company or the relevant affiliate. Upon the termination of the Associate's employment with the Company, whether it be voluntary or involuntary, whenever that termination of employment may occur, or upon the Company's request at any time, the Associate must promptly deliver to the Company or to the relevant affiliate all such assets and property, including without limitation any such office equipment (including computers) and any Confidential Information or other records or documents (written or otherwise), and any copies, excerpts, summaries or compilations of the foregoing, made by the Associate or that came into the Associate's possession during the Associate's employment. The Associate agrees that he or she will not retain any such assets or property, including without limitation copies, excerpts, summaries, or compilations of the foregoing information, records and documents.

(d) "Confidential Information" includes, without limitation, any matters protected under the Uniform Trade Secrets Act and any information that neither the Company nor any of its affiliates has previously disclosed to the public with respect to the present or future business of the Company or of any of its affiliates, including their respective operations, services, products, research, inventions, invention disclosures, discoveries, drawings, designs, plans, processes, models, technical information, facilities, methods, systems, trade secrets, copyrights, software, source code, object code, patent applications, procedures, manuals, specifications, any other intellectual property, confidential reports, price lists, pricing formulas, customer lists, financial information (including the revenues, costs, or profits associated with any products or services), Talent Reviews and Organizational Plans, business plans, information regarding all or any portion of the Danaher Business System, lease structure, projections, prospects, opportunities or strategies, acquisitions or mergers, advertising or promotions, personnel matters, legal matters, any other confidential or proprietary information, and any other information not generally known outside the Company and its affiliates that may be of value to the Company or any of its affiliates, but excludes any information already properly in the public domain. "Confidential Information" also includes, without limitation, confidential and proprietary information and trade secrets that third parties entrust to the Company or any of its affiliates in confidence.

(e) The Associate understands and agrees that the rights and obligations set forth in this **Nondisclosure** section will continue indefinitely and will survive termination of the Associate's employment with the Company.

5. Works-made-for-hire and Intellectual Property.

(a) The Associate agrees that all records (in whatever media), written works, documents, papers, notebooks, drawings, designs, technical information, source code, object code, algorithms, processes, methods, ideas, formulas, inventions (whether patentable or not), invention disclosures, discoveries, improvements, other copyrightable or protected works, or any other intellectual property, developed, conceived, acquired, created, authored, reduced to practice, from which derivative works are prepared, made, invented, or discovered by the Associate (whether or not during usual working hours, and whether individually or jointly with others) that relate to, result from or are suggested by any work or task performed by the Associate for or on behalf of the Company or any affiliate thereof, or that arise from the use or assistance of the facilities, materials, personnel, or Confidential Information of the Company or any affiliate thereof, or that otherwise relate to the actual or anticipated research, development or business of the Company or any affiliate thereof, will be and remain the absolute property of the Company (or the relevant affiliate thereof), as will all the worldwide patent, copyright, trademark, service mark and trade secret rights, any associated registrations, applications, renewals, extensions, continuations, continuations-in-part, requests for continued examination, divisions, or reissues thereof or any foreign equivalents thereof, and all other intellectual property rights relating to the foregoing (all items referred to in this sentence are collectively referred to as the "Intellectual Property"). The Associate irrevocably and unconditionally waives all rights, wherever in the world enforceable, that vest in the Associate (whether before, on, or after the date of this Agreement) in connection with any such Intellectual Property in the course of the Associate's employment with the Company, any affiliate thereof or any predecessor of any of the foregoing. The Associate recognizes all such Intellectual Property constitutes "works made for hire" for which the Company retains all rights, title, and interest to any underlying rights, including copyright protections. If for any reason any such Intellectual Property is not deemed to be a "work made for hire," consistent with the undertakings below, the Associate hereby assigns all rights, title and interest in any such Intellectual Property to the Company (or the applicable affiliate thereof, as directed by the Company).

(b) The Associate will promptly disclose, and hereby grants, and assigns all rights, title, and interest in all Intellectual Property, to the Company (or the applicable affiliate thereof, as specified by the Company) for its or their sole use and benefit. At all times, both during and after the Associate's employment by the Company, the Associate agrees to assist the Company in taking the proper steps, including executing any required documents, to obtain patents, copyrights or other legal protection for the Intellectual Property and to assign such Intellectual Property and the rights to any applications associated therewith to the Company, if the Company so desires, but all at the Company's direction and expense. At all times, both during and after the Associate's employment by the Company, the Associate agrees not to claim any rights to any Intellectual Property as having been created, conceived or acquired by the Associate prior to the Associate's employment by the Company, unless such Intellectual Property is identified on a sheet attached to this Agreement and signed by the Associate as of the date of this agreement.

(c) The Associate understands and agrees that the rights and obligations set forth in this **Works-made-for-hire and Intellectual Property** section will continue indefinitely and will survive termination of the Associate's employment with the Company, whether the termination is voluntary or involuntary.

6. Termination Payment. In consideration of the Associate's promises and commitments reflected in paragraphs 2, 3, 4, 5 and 15 herein, the Company agrees that if the Company terminates the Associate's employment "without cause" (as defined below) prior to termination of this Agreement, the Associate shall be entitled to nine months salary (excluding incentive compensation, bonus amounts, benefits and similar items) at the rate in effect at the time of termination to be paid on the same schedule as if Associate were still employed (the "Termination Payments"). The Company will reduce the amount of any Termination Payments for withholding and FICA taxes and any other withholdings and contributions required by law. If the Company terminates the Associate for "cause," or if the Associate terminates his or her employment for any reason, the Associate shall not be entitled to any Termination Payments. The Associate further acknowledges that a transfer to Danaher or another subsidiary of Danaher shall in no event constitute a "termination" of any kind for purposes of Sections 6 or 7 hereof.

(a) For purposes of this Agreement, termination "without cause" shall mean that the Company terminates the Associate's employment for any reason, including in a reduction-in-force, other than for "cause." "Cause" shall include the following, to be determined in the reasonable judgment of the Company:

(i) the Associate's fraud, misappropriation, embezzlement, willful misconduct or gross negligence with respect to the Company, Danaher or any subsidiary thereof, or any other action in willful disregard of the interests of the Company, Danaher or any subsidiary thereof;

(ii) the Associate's conviction of, or pleading guilty or no contest to (1) a felony, (2) any misdemeanor (other than a traffic violation) with respect to his/her employment, or (3) any other crime or activity that would impair his/her ability to perform his/her duties or impair the business reputation of the Company, Danaher or any subsidiary thereof;

(iii) the Associate's refusal or willful failure to adequately perform any duties assigned to him/her;

(iv) the Associate's willful failure or refusal to comply with Company or Danaher standards, policies or procedures, including without limitation Danaher's Standards of Conduct as amended from time to time;

(v) the Associate's material misrepresentation or breach of any of his or her representations, obligations or agreements under this Agreement;

(vi) the Associate's death; or

(vii) the Associate's incapacity due to physical or mental illness that results in his/her absence from work on a full-time basis for twelve consecutive months.

(b) Notwithstanding anything in this Section 6 to the contrary, the Associate agrees that in the event of a breach by the Associate of any of his/her covenants contained in Sections 2, 3, 4, 5 or 15 herein, in addition to any and all other remedies available to the Company, (1) the Associate shall return to the Company any Termination Payments theretofore received, in addition to any other damages or remedies available to the Company, and (2) the Company shall have no obligation to pay, and the Associate shall have no right to receive, any and all unpaid or remaining Termination Payments. Notwithstanding anything to the contrary herein, to the extent a court, governmental authority or other administrative body invalidates or renders unenforceable all or any portion of the covenants contained in Sections 2, 3, 4, 5 or 15 herein, the parties hereto agree that the Termination Payments otherwise payable (including any installments that have already been paid to Associate) shall be reduced proportionally, up to and including eliminating the Termination Payment in its entirety to the extent the Agreement is rendered unenforceable in its entirety.

7. Severance Payment. The Company agrees that if the Company terminates the Associate's employment "without cause" (as defined in paragraph 6(a) above) prior to termination of this Agreement, the Associate shall be entitled to severance pay of three months salary (excluding incentive compensation, bonus amounts, benefits and similar items) at the rate in effect at the time of termination to be paid on the same schedule as if the Associate were still employed (the "Severance Payments") provided the Associate signs a release of all claims arising out of the Associate's employment, and discontinuance of employment, with the Company and with Danaher and/or any other subsidiaries of Danaher to the extent applicable. Such release must be executed at the time of termination, and will be in the format of the Company's standard release in effect at the time of termination (a copy of the current version is available for the Associate's review.) The Severance Payments will commence upon completion of the Termination Payments provided for in paragraph 6 above, if any. The Company will reduce the amount of any Severance Payments for withholding and FICA taxes and any other withholdings and contributions required by law. Notwithstanding anything in this Section 7 to the contrary, the Associate agrees that in the event of a breach by the Associate of any of his/her covenants contained in the aforementioned release, in addition to any and all other remedies available to the Company, (1) the Associate shall return to the Company any Severance Payments theretofore received, in addition to any other damages or remedies available to the Company, and (2) the Company shall have no obligation to pay, and the Associate shall have no right to receive, any and all unpaid or remaining Severance Payments.

8. Enforceability. It is the intention of the parties that the provisions of the restrictive covenants herein shall be enforceable to the fullest extent permissible under applicable law, but the unenforceability (or modification to conform to such law) of any provision or provisions hereof shall not render unenforceable, or impair, the remainder thereof. If any provision or provisions hereof shall be deemed invalid or unenforceable, either in whole or in part, this Agreement shall be deemed amended to delete or modify, as necessary, the offending provision or provisions and to alter the bounds thereof in order to render it valid and enforceable.

9. Damages and Relief. The Associate acknowledges and agrees that damages are an inadequate remedy for any breach of the terms and conditions set forth in Sections 2, 3, 4, 5 and 15 of this Agreement and agrees that in the event of a breach of such paragraphs, the Company may, with or without pursuing any remedy for damages, immediately obtain and enforce an ex parte, preliminary and permanent injunction prohibiting the Associate from violating this policy. Further, in any civil action brought for a breach of this Agreement, the Company shall be entitled to recover from the Associate all reasonable attorneys' fees, litigation expenses, and costs incurred by the Company if the Company prevails in that action.

10 Consideration. The Associate acknowledges and agrees that this Agreement is supported by the Termination Payment provision set forth in Section 6 above without regard to whether the Associate receives any or all of the Termination Payment. The Associate further agrees that such consideration is fair,

reasonable and enforceable to its full extent; that the Associate was given adequate time to consider this Agreement; that the Company has an important and legitimate business interest that it is seeking to protect with this Agreement; and that enforcement of this Agreement would not interfere with the interests of the public.

11. Governing Law. This Agreement shall be governed by and construed in accordance with the substantive laws of the State of South Carolina without regard for the choice of law provisions thereof.

12. Termination.

(a) The Associate understands, acknowledges and agrees that the obligations and restrictions imposed upon him/her under this Agreement shall apply regardless of whether the termination of his/her employment is voluntary or involuntary, with or without cause.

(b) Unless the Associate is sooner terminated pursuant to the terms of Section 6 of this Agreement, terminated by the Company for cause or the Associate terminates his or her employment for any reason, the Company shall upon prior written notice to the Associate have the right to terminate this Agreement (1) on the second anniversary of this Agreement and on every second anniversary thereafter, and (2) in connection with any promotion of the Associate or transfer of the Associate to Danaher or another subsidiary of Danaher; provided, that in connection with any such termination the Company (or Danaher or another subsidiary of Danaher, as applicable) shall offer to the Associate an agreement containing terms substantially similar to the terms set forth herein but taking into account the then-current status of the applicable law.

(c) Notwithstanding anything to the contrary set forth herein, all of the Company's obligations under this Agreement shall terminate upon the earliest of the termination of the Associate's employment for cause, the Associate's termination of his or her employment for any reason, or the Company's fulfillment of its obligations, if any, as set forth in Sections 6 and 7 hereof.

13. Amendment and Waiver; Entire Agreement. This Agreement shall not be amended except by a written instrument hereafter signed by the Company and the Associate. The failure of the Company to enforce, or delay in enforcing, any term of this Agreement shall not constitute a waiver of any rights or deprive the Company of the right to insist thereafter upon strict adherence to that or any other term of this Agreement, nor shall a waiver of any breach of this Agreement constitute a waiver of any preceding or succeeding breach. No waiver of a right under any provision of this Agreement shall be binding on the Company unless made in writing and signed by the Board of Directors of the Company. This Agreement contains the entire understanding of the Company and the Associate relating to the subject matter hereof and supersedes all prior agreements and understandings relating to the subject matter hereof between the Associate on the one hand and the Company, Danaher and/or any other current or former subsidiary of Danaher on the other hand, including without limitation any similar agreement entered into prior to the date hereof between the Associate on the one hand and the Company, Danaher and/or any other current or former subsidiary of Danaher on the other hand.

14. Successors and Assigns. This Agreement shall be binding upon the Associate and his/her heirs, successors, assigns and personal representatives, and inure to the benefit of the Company, its successors and its assigns. The Associate may not assign any rights or duties under this Agreement; the Company may assign any or all of its rights and/or duties herein to Danaher and/or any other subsidiary or subsidiaries of Danaher. The term "affiliate," when used herein, shall not include any officers or directors of the Company or of Danaher.

15. Nondisparagement. The Associate agrees that except as required under the law, the Associate will refrain from making derogatory or disparaging written or oral comments regarding the Company, any of its affiliates or any of their respective products, services or personnel.

16. Right of Set-Off. The Company shall have the right, but not the obligation, to set off, in whole or in part, against any obligation it owes to the Associate under this Agreement or under any release, amounts owed to the Company, Danaher or any other Danaher subsidiary by the Associate.

17. Acknowledgment of Understanding; Livelihood. The Associate acknowledges that s/he has read this Agreement in its entirety and understands all of its terms and conditions, that s/he has had the opportunity to consult with legal counsel of his/her choice regarding his/her agreement to the provisions contained herein, that s/he is entering into this Agreement of his/her own free will, without coercion from any source, and that s/he agrees to abide by all of the terms and conditions herein contained. The Associate further acknowledges that in consideration of the Associate's right to terminate his/her employment with the Company at any time for any reason, Associate agrees that s/he is employed by the Company on an at-will basis. Nothing contained in this Agreement or elsewhere shall be construed as limiting the effect of this paragraph. The Associate acknowledges that Associate's knowledge, skills and abilities are sufficient to enable the Associate, in the event of the termination of employment with the Company, to earn a satisfactory livelihood without violating this Agreement.

Associate: ______________________ Date: 6/17/04

Company: By: Karen Bergendorf Date: 7-12-04

Name: Karen Bergendorf

Title: VP Finance

EXHIBIT A COMPETITORS

ROHM
YUKIWA
PEACOCK (SHANDONG WEIDA MACHINERY COMPANY, LTD.)
CHINA MILITARY
SAN OU
LFA
CHUMPOWER
CHAO LI

EXHIBIT B CUSTOMERS

AROMAT MEXICANA SA DE CV
ATLAS COPCO
BLACK AND DECKER
BOSCH
HITACHI
LINVATEC
MAKITA
MILWAUKEE ELECTRIC TOOL
STRYKER CORP.
TECHTRONIC INDUSTRIES CORP
FIDELITONE DISTRIBUTION S
SNAP ON TOOLS CORP
METABOWERKE GMBH & CO
PORTA SPA
CHOON NANG
JACOBS IRON WORKS
JIA HE
JIN DING
JU HUA
MOBILETRON
TAIHU
TECHWAY
TOP ELECTRICAL
TOP HOST

EXHIBIT C

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INTELLECTUAL PROPERTY

Identification of Trade Secret Claims in Litigation: Solutions for a Ubiquitous Dispute

Charles Tait Graves and Brian D. Range

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Identification of Trade Secret Claims in Litigation:

Solutions for a Ubiquitous Dispute

By Charles Tait Graves and Brian D. Range*

I. INTRODUCTION

¶1 Trade secret cases pose special problems distinct from other intellectual property lawsuits because alleged trade secrets are rarely defined in advance of litigation. For every patent, registered copyright, or trademark, there is a document filed with the federal government identifying the details and boundaries of the asserted intellectual property. But in trade secret cases, the plaintiff's attorneys typically develop the trade secret claims at the same time that they file a misappropriation suit against a former employee or business partner – or afterwards.

¶2 Trade secret plaintiffs rarely provide a precise and complete identification of the alleged trade secrets at issue without a court order requiring them to do so. This is a strategy, not an accident. The tactical advantages a plaintiff gains from non-identification are too tempting for a plaintiff to voluntarily provide such identification. In a typical case, the plaintiff has filed suit against a recently departed employee who joined or started a competing business, and then provide little more than a list of high-level, generic categories in which its alleged secrets are said to reside.

¶3 It is also common for a trade secret plaintiff to alter its list of trade secret claims as the case proceeds – sometimes dramatically, by replacing entire categories of information or technology, or by re-combining slippery, multi-element "combination trade secret" claims into new subsets. In a 2006 New Jersey case, for example, the plaintiff first identified four alleged secrets in an initial interrogatory response, then added six, later added thirty-nine in an expert report, then claimed ninety-two in a supplemental interrogatory response, and had its expert give what the court called "moving target" testimony about the alleged secrets.[1] We have seen many similar alterations during the course of cases in several jurisdictions, and defendants sometimes

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* Charles Tait Graves and Brian D. Range are associates at Wilson Sonsini Goodrich & Rosati in San Francisco, California and Austin, Texas. This article is the fourth in a series that seeks to clarify frequently litigated but obscure areas of trade secret law, in the interest of protecting employee mobility and the right to use information in the public domain.

[1] *See, e.g.*, Civil Action No. 01-4677 (SRC) 2006 WL 1344084, at *1-3 (D.N.J. May 16, 2006) (acknowledging plaintiff's "moving target" allegations but holding that defense had sufficient opportunity to take discovery on shifting claims); Thomas & Betts Corp. v. Richards Mfg. Co., No. Civ. 01-4677, 2006 WL 902148, at *8-9 (D.N.J. Apr. 4, 2006) (barring some expert testimony).

spend months disproving one set of allegations only to face a new, replacement set as the close of discovery nears.

¶4 Precise identification of the alleged trade secrets is a crucial component of trade secret litigation. This is especially true when complex technology is at issue, but also in cases featuring simpler claims. Without a precise identification of software code elements, hardware architecture components, or even the names of allegedly secret customers, the defendant cannot compare the claims against public domain information to challenge the alleged secrecy of such information. It is difficult to conduct a public domain analysis if the claims are identified at only a generic level such as "source code," "ASIC design elements," or "customer lists." Stated differently, the parties and the court cannot accurately decide the question of whether a trade secret exists without first understanding what precisely is asserted as a secret.

¶5 It is not surprising, then, that disputes over identification of the plaintiff's alleged trade secrets are common. However, it is notable that courts nationwide have not yet articulated a set of guidelines and standards to assist judges who must rule on identification questions. Indeed, courts in various jurisdictions have issued rulings on the same identification issues with almost opposite results – a majority requiring more identification, but a minority allowing the plaintiff to proceed with only general, conclusory descriptions of the alleged trade secrets. The published rulings indicate that courts subjectively reach their own conclusions, often with little or no reference to other published decisions. The problem is further exacerbated because courts rarely, if ever, quote precise descriptions of potentially valuable trade secrets in publicly available opinions, and thus most published opinions do not clarify the degree of specificity required.[2] As a result, the scattered case law in this area does not always serve as precedent, and it is difficult for parties to predict the result in any given case. The lack of a uniform set of guidelines invites trade secret plaintiffs to avoid identifying their alleged secrets in detail, because there is always a fair chance that the reviewing court will not require them to do so.

¶6 Despite the frequency of disputes over the identification of alleged trade secrets, the issue has received little scholarly attention.[3] Perhaps this is because the case law is scattered across multiple jurisdictions, in state and federal courts, without any unifying doctrine apart from citations to a few well-known cases. Most treatises refer to the problem in only general terms,[4] and a handful of practitioner-oriented articles note particular cases without a nationwide survey or detailed proposals.[5]

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[2] *See* Savor, Inc. v. FMR Corp., No. Civ. A. 00C-10-149JRS, 2004 WL 1965869, at *6-7 (Del. Super. Ct. Aug. 16, 2004) (redacting alleged trade secrets).

[3] The single full-length article we have found devoted to the identification question is Kevin R. Casey, *Identification of Trade Secrets During Discovery: Timing and Specificity*, 24 AIPLA Q.J. 191, 281 (1996) (summarizing case law and noting different stages of the case, but apparently recommending that "precise" detail need not be disclosed until trial; no specific focus on identification of different types of information). We disagree that identification should be withheld until trial, for reasons discussed below. The majority of the case law since 1996 supports our position.

[4] *See, e.g.*, RUDOLF CALLMANN, CALLMANN ON UNFAIR COMPETITION, TRADEMARKS AND MONOPOLIES § 14:30 (4th ed. Supp. 2006) (briefly noting issue with citations); MELVIN A. JAGER, TRADE SECRETS LAW §§ 5:32, 9:8 (West 2006) (1985) (general description of some identification cases); ROGER M. MILGRIM, MILGRIM ON TRADE SECRETS §§ 15.01[1][d][i], 16.01[5][b] (Matthew Bender 2006) (1967) (general summary of issue and its importance with a few citations); ROBERT I. WEIL & IRA A. BROWN, JR., CALIFORNIA PRACTICE GUIDE: CIVIL PROCEDURE BEFORE TRIAL § 8:58 (2006) (general description of

¶7 Given that most of the identification disputes on record have occurred in the past decade, the time is right for a detailed analysis of the identification problem. We believe that courts nationwide facing trade secret disputes should apply a recognized set of guidelines and standards to resolve disputes over the identification of alleged trade secrets in litigation. This would reduce unpredictable and inconsistent rulings, deter plaintiffs from strategically withholding information by gambling that any given court will not require a precise identification, and deter defendants from making the wrong demands as to identification at the wrong stage of the case. We believe that a proper standard would take into account the type of information being alleged as secret, the stage of the case, and the defendant's own diligence in raising the issue.

¶8 To that end, we have reviewed substantially all of the trade secret identification rulings available, including unpublished rulings and slip opinions, in order to paint a picture of how courts are reacting to similar arguments and disputes across the country. We will describe both outlier and mainstream opinions to illustrate why a set of common standards is needed.[6]

¶9 Yet merely summarizing holdings does not provide sufficient information to propose guidelines. Few courts have attempted to state rules of general applicability beyond the dispute at issue. Outlining the policy grounds supporting detailed identification of trade secret claims is therefore necessary. We will organize the discussion by the stage of the case, the type of information at issue, and the skill with which the defense has properly raised the issue. We will also offer solutions that courts can apply for the specific types of alleged secrets at issue in a given case.

¶10 In short, we offer five proposals as a standard for identification of alleged secrets in litigation:

California's Code Civ. Proc. sec. 2019.210). The most detailed existing commentary on the identification question is JAMES POOLEY, TRADE SECRETS § 11.02 (Supp. 2005). However, we respectfully disagree with the view expressed there that courts should not always require precise identification, especially during the discovery stage, because without precision the plaintiff has too easy an opportunity to continually alter its claims, and because plaintiffs who file multi-million dollar technology lawsuits are fully capable of providing such precision. Moreover, we have seen many cases where highly technical details were located in the public domain, and such research would have been impossible absent precision.

[5] *See, e.g.*, JOHN F. HORNICK & MARGARET A. ESQUENET, TRADE SECRET IDENTIFICATION OF TIMING IN DISCOVERY (2005), http://www.finnegan.com/publications/news-popup.cfm?id=1248&type=article (focusing on jurisdictions with pre-discovery requirements); Brent Caslin, *Secret Weapon: Understanding What Constitutes "Reasonable Particularity" Can Be the Decisive Element in Trade Secret Litigation*, L.A. LAW., Apr. 2004, at 44 (noting leading cases and advising defendants about various motions to file regarding an insufficient identification); York M. Faulkner & Margeret A Esquenet, *Putting an End to the Trade Secret Plaintiff's Game of Bait and Switch*, IP LITIGATOR, Sept. 2001, at 24-25 (noting problem and describing a few leading cases); Randy Kay, *Identifying Trade Secrets in Litigation - Managing the Process*, 28 NEW MATTER 1/2, Sept. 2003, 19-22 (noting problem and providing advice for plaintiffs and defendants); James R. Mckown, *Discovery of Trade Secrets*, 10 SANTA CLARA COMPUTER & HIGH TECH. L.J. 35, 47 (1994) (noting leading cases on identification disputes as of 1994 in article about procedural aspects of disclosing trade secrets in various litigation contexts); David R. Sugden, *C.C.P. Section 2019.210: A Sword, Not a Shield*, ORANGE COUNTY LAW., Mar. 2006, at 51-55 (advising defense counsel to take advantage of California's pre-discovery identification statute and use a plaintiff's failure to identify to move for summary judgment later in the case).

[6] Of course, rulings on most identification disputes take place on discovery calendars in trial courts and thus are never published, so a complete nationwide survey is not possible.

(1) Courts should first separate the question of whether the plaintiff has identified an alleged secret from the question of whether the information is, in fact, a trade secret;

(2) Courts should require a reasonably detailed identification of the alleged secrets before a plaintiff can proceed with discovery – a rule already required by statute in California, and by common law in several other states;

(3) Perhaps most importantly, if a defendant properly requests a precise identification during discovery, the court should require a precise, complete identification of whatever type of information is at issue – including an identification of alleged "combination trade secrets";

(4) No trade secret plaintiff should obtain an injunction or avoid summary judgment without a precise identification of alleged secrets;

(5) Trade secret plaintiffs should not be permitted to alter or amend an identification of trade secret claims without a showing of good cause.

¶11 These standards would remove the uncertainty that prevails in identification disputes. A trade secret plaintiff with a valid claim would have incentive to identify the alleged secrets early on, and a defendant who has misappropriated trade secrets could more easily be shown to have done so. A trade secret plaintiff with a meritless claim, however, would more easily be exposed. These standards would make it more difficult to sue former employees for harassment purposes and to spend them into the ground with protracted litigation, and more difficult to claim public domain information as trade secrets.

¶12 We believe that these proposals are equally applicable in jurisdictions which have enacted the Uniform Trade Secrets Act and those which follow the Restatement (Second) of Torts. Under both, a plaintiff must establish that the information at issue does, in fact, constitute trade secrets.[7] Requiring identification is a necessary case management tool to ensure that the parties and the court accurately understand what information is being asserted as secret in order to proceed to the secrecy question.[8]

¶13 This Article is primarily for courts ruling on identification questions, who must research the issue when parties file pleadings that cite only decisions that favor their positions, and who may need a single source for all of the nationwide case law. We believe that courts do not always realize the degree to which the identification of trade

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[7] *See, e.g.*, CAL. CIV. CODE § 3426.1(d)(1) (West 2006) (California Uniform Trade Secrets Act provision defining trade secrecy); RESTATEMENT (SECOND) OF TORTS § 757 cmt. b (1979) (Restatement definition of trade secrecy).

[8] We note, however, that identification may not always matter in jurisdictions where a former employer can use contract law to bind former employees with non-competition covenants that bar use of non-secret material for some period after resignation. *See, e.g.*, Lason Serv., Inc. v. Rathe, No. Civ.A.3:02CV2110-D, 2003 WL 21728184, at *6 (N.D. Tex. Mar. 14, 2003) (rejecting defendant's argument that plaintiff failed to identify allegedly secret customers because non-solicitation covenant barring solicitation of customers was valid in jurisdiction and it was irrelevant whether customers were secret or non-secret); *Paper Mfg. Co. v. Weiss*, No. 1040, 1972 WL 15994, at *3 (Pa. Ct. Com. Pl. Mar. 13, 1972) (denying motion to require identification of alleged trade secrets given that plaintiff's claim was premised on restrictive non-competition contract valid in that jurisdiction, and thus plaintiff need not prove trade secrets to prevail).

secret claims is a lawyers' game, where one side holds back information and hopes that the opposing party will fail to raise the issue, or hopes that that a court will accept the argument that generic references to complex technology are sufficient.

¶14 This Article should also be of use to litigants, both to plaintiffs who have valid claims and seek to identify them in good faith and to defendants who lack the time or money to canvass the vast jurisprudence on identification, or who want to craft the best possible discovery requests to pin down a trade secret plaintiff and force a precise identification.

¶15 In what follows, we will describe the common mistakes that courts make when ruling on identification disputes, the problems that arise in the absence of a precise identification of trade secret claims, and how courts nationwide have ruled on identification disputes. We will then offer specific proposals for resolving identification questions.

II. THE PROBLEM

¶16 A trade secret case usually begins shortly after a former employee has resigned and either joined a competitor or formed a new, competing business. The plaintiff files a lawsuit that accuses the defendant of misappropriating trade secrets, but the complaint contains only generalities about the nature of the alleged secrets. Once the parties have entered into a protective order that allows the confidential sharing of information between the parties and their attorneys,[9] the plaintiff sometimes issues a written statement that purports to identify the trade secret claims at issue, and sometimes provides such a statement as a discovery response. Because the statement rarely if ever identifies the alleged secrets with precision, a dispute over the specificity of the identification often arises within the first three months of the litigation. In other cases, the identification dispute arises later, when the plaintiff alters its claims or raises a new set of claims.

¶17 In the typical dispute over identification of alleged trade secrets, the defense argues that the plaintiff's list of categories and concepts is not specific enough, and then cites a scattering of cases that may not have been decided at the same stage of the case, that may not have addressed the same type of information, or that provided no real guidance on how much precision was required. The plaintiff, in turn, often responds by arguing that the defendant already knows what the alleged trade secrets are because the defendant knows what it stole, and thus no identification is necessary. The plaintiff will typically argue that a list of high-level concepts is sufficient and make selective citations to cases so holding, and it may also argue that because it alleges "combination" trade

[9] A protective order in a trade secret case usually creates a three-tier classification for information produced in discovery: material that is designated as non-confidential, material that is designated such that only the parties can view it and not the public, and material that only the attorneys and expert witnesses can view. The parties usually agree on terms allowing the individuals actually accused of misappropriating trade secrets to see the list of items they are accused of having stolen. In most cases, employees of the parties rarely see documents and other information produced by the other party, so there is little if any risk that one side will misuse information produced by the other.

secrets rather than individual trade secrets, no identification should be required.[10] Also, if the case is at an early stage, the plaintiff may argue that it cannot yet know every trade secret that was stolen and therefore cannot identify all trade secrets claims it may assert in the future.

¶18 Assessing an identification dispute can be difficult given the lack of uniformity in the published cases and the absence of a set of standards to which courts can look, especially in jurisdictions where trade secret lawsuits are less common.

A. Twelve Policy Considerations Relating to Vague Trade Secret Allegations

¶19 The best place to begin is to step back from the facts of the case at issue and outline the policy reasons why requiring a detailed identification of the trade secret claims makes sense. We believe that there are at least twelve such considerations. Courts have cited some of these considerations when requiring identification, and we have come to recognize the others in the course of litigating scores of trade secret cases.

¶20 The first consideration is that the identification of an alleged trade secret can only come from the plaintiff, because there is no other pre-existing source one can look to for the details of the alleged intellectual property. Trade secrets are not listed claim-by-claim like patents or set forth in their entirety like registered copyrights or trademarks. There is no public source to which the defendant can look in order to determine what potential trade secrets the plaintiff possesses. The plaintiff's decision on what to claim as its trade secrets in litigation is a subjective one. Even if a former employee defendant could guess what trade secret claims the former employer might make, the specifics of the actual claim could differ from that speculation. On this point, it is important to note that the plaintiff's identification of its own alleged intellectual property does not depend on the defendant's documents, because the preliminary question is whether the plaintiff has a trade secret, which must be answered before determining whether the defendant used the secret in its products or services.

¶21 The second consideration is that requiring an early and precise identification of alleged trade secrets will encourage compliance with Federal Rule of Civil Procedure 11 and similar state rules governing frivolous pleadings. Such statutes and the Uniform Trade Secret Act all require that a trade secret plaintiff make allegations of misappropriation in good faith – either directly or through general rules against meritless accusations.[11] Any plaintiff's pre-lawsuit review of a potential trade secret matter should therefore consider whether the basic elements of the tort claim can be met, such as (1) the existence, in fact, of a trade secret; (2) the plaintiff's use of reasonable measures to maintain that secrecy; and (3) the defendant's misappropriation of one or more such secrets.[12] A plaintiff cannot adequately investigate these elements without internally identifying the trade secret claims under consideration. A vague identification of alleged trade secrets once the litigation has begun suggests that the plaintiff did not undertake a

[10] For a discussion of courts which have accepted this "combination trade secret" argument, see *infra* Section III.A.

[11] For example, California's version of the Uniform Trade Secrets Act provides remedies for bad faith trade secret claims, and the state also has a general statute governing frivolous pleadings. *See* CAL. CIV. CODE § 3426.4 (West 2006); CAL. CIV. PROC. CODE § 128.7(b) (West 2006).

[12] *See, e.g.*, CAL. CIV. CODE § 3426.1 (West 2006) (definitions of elements of a trade secret claim).

pre-lawsuit review. If parties know that identification will be required early in litigation, they have greater incentive to do a careful review before filing suit.

¶22 Third, and similarly, a lax identification standard could allow a party to avoid the statute of limitations. As one court noted on this point:

> These facts of cutting edge technological life, to say nothing of the limitations of language generally, have the effect of giving the person asserting trade secret claims in these kinds of cases, very wide definitional latitude, and, with that, considerable power to manipulate the articulation of claims for tactical purposes, e.g., to escape what might otherwise be a perfectly sensible application of the statute of limitations.[13]

¶23 The fourth consideration is that an exact identification is necessary to set the proper bounds and scope of discovery – the areas in which discovery will be permitted. Litigating parties often make and sell products outside the scope of the alleged trade secrets, and requiring a precise identification prevents burdensome and expensive discovery into irrelevant areas. Also, without a detailed identification, a plaintiff may later define its alleged secrets by first looking at the defendant's documents and then crafting claims that match those documents, but that do not match the plaintiff's own information.

¶24 The fifth consideration is that requiring a detailed identification early in a lawsuit may reduce future disputes over identification and thereby reduce the length of the discovery process. By contrast, a plaintiff who identifies the claims only later may cause new rounds of depositions and other discovery as the parties scramble to assess the newly-provided information. Knowing the claims early allows for a focused and efficient discovery plan from the start, and thus serves as a useful case management tool.

¶25 The sixth consideration is that without a precise identification, the defense lacks the information it needs to conduct public domain research and challenge the alleged secrecy of the information at issue. Seventh, and for the same reasons, the reviewing court cannot rule on a secrecy claim with accuracy and confidence if the exact parameters of the information remain unclear. Without details, who can be sure that the alleged secret has not been published elsewhere, by a market competitor, an engineering publication, or in academic work?

¶26 The eighth consideration is that requiring a precise identification prevents a plaintiff from making overbroad secrecy claims encompassing vast categories of information. Plaintiffs sometimes use the trade secret claim as a sort of non-competition covenant by listing wide areas of technology that encompass the former employee's entire set of skills, knowledge, and experience. Ninth, and on a related point, a defendant cannot formulate its arguments for differentiating its technology from the alleged trade secrets at issue without knowing precisely what those trade secrets are. For example, a former employee may well have worked in good faith to ensure that software written for a subsequent employer would not copy or otherwise make use of the former employer's

[13] Intermedics, Inc. v. Ventritex, Inc., 822 F. Supp. 634, 656 (N.D. Cal. 1993) (regarding trade secret statute of limitations under California's UTSA).

non-public information, but cannot make that distinction if the plaintiff asserts only general functionalities common to that general type of software.

¶27 The tenth consideration is that expert reports from both sides will be more useful and focused if the exact nature of the alleged secrets is known before they begin their work. Without an exact identification, the plaintiff's expert may simply declare that broad areas of technology are trade secrets, without actually conducting specific public domain research that could support a valid scientific opinion. Meanwhile, the defense experts may be forced to spend a great deal of effort researching and opining on wider areas of technology than are at issue, without being able to focus on the exact technology the plaintiff claims as intellectual property.

¶28 The eleventh consideration is that the trade secret plaintiff should not be able to unilaterally alter and amend its claims without judicial review as the lawsuit proceeds. Too many trade secret cases feature a kaleidoscope of amorphous, frequently-altered claims that prevent the defense from pinning down and defeating any solid set of claims. Requiring an early and precise identification of alleged secrets can make attempts at unsupervised alteration apparent. By contrast, a broad and non-specific list of concepts and categories allows a plaintiff to alter the details of the claims in a manner more likely to escape judicial review.

¶29 Finally, and perhaps most broadly, requiring a detailed identification protects employees' interests in moving to the jobs of their choice and using public domain information, as they have a right to do. When a plaintiff makes vague trade secret claims against a former employee without narrowly defining the actual items at issue, it is essentially requesting a court-created non-competition agreement against the defendant.[14] Such claims cut into the former employee's general right to take non-secret knowledge, skills, and experience from job to job.[15] But when discovery focuses only on detailed clams susceptible to examination and study, there is less risk that these important public policy interests will be encroached upon.

¶30 At the same time, we do not agree with all of the policy grounds that courts have given for requiring a detailed identification of alleged trade secrets. Some courts and commentators have asserted that identification is needed to prevent a malicious plaintiff from filing suit for the purpose of getting into the defendant's own information and taking the defendant's trade secrets.[16] While we have learned from experience that

[14] It should be noted that an employee seeking to act in good faith may have no affirmative ability to obtain a specific list of potential trade secrets in order to avoid using them. In *Lane v. Baxter Healthcare Corp.*, 905 S.W.2d 39, 40 (Tex. Ct. App. 1995), a former employee sought a declaratory judgment that would force his former employer to list any trade secrets that it contended the former employee could not utilize in his new job. The court held the issue was not justiciable because the former employee had "not invented, and may never invent, anything that is of concern to Baxter." *Id.* at 42. Thus, the former employee's attempt to use a declaratory judgment action to determine how he could fairly compete with his former employer failed.

[15] The concept that former employees are free to use general skills, knowledge, and experience is well established. *See, e.g.*, Winston Research Corp. v. Minn. Mining & Mfg. Co., 350 F.2d 134, 143-144 (9th Cir. 1965) ("[plaintiff's] former employees cannot be denied the right to use their general skill, knowledge and experience, even though acquired in part during their employment by [plaintiff]); Eaton Corp. v. Appliance Valves Corp., 526 F. Supp. 1172, 1180 (N.D. Ind. 1981) ("the general knowledge and skill obtained by an employee during his employment belongs to that employee and can be utilized by him after terminating his employment"), *aff'd*, 688 F.2d 842 (7th Cir. 1982).

[16] *See, e.g.*, Computer Econ., Inc. v. Gartner Group, Inc., 50 F. Supp. 2d 980, 985 (S.D. Cal. 1999)

attorneys are willing to assist their clients by altering claims and by not defining claims, we believe that it is less likely that a law firm would assist a client's scheme to take information from a competitor by filing a lawsuit against the competitor and turning over information produced in discovery and designated as confidential under a protective order. We believe that courts should avoid relying on this purported basis for requiring an identification, and focus instead on the real problems caused by non-identification.

B. Mistakes Courts Make When Ruling on Identification Questions

¶31 Reflecting on these policy considerations should assist courts in making a ruling appropriate to the case at issue, and in avoiding the mistakes courts sometimes make when deciding identification questions.

¶32 Several such mistakes merit special attention. To begin with, a tiny minority of courts have nullified the identification requirement altogether, refusing to require a trade secret plaintiff to identify the trade secret claims even in the face of the defendant's discovery requests or controlling law in the jurisdiction. As one example, a California trial court sanctioned a trade secret defendant in a 2006 case for not providing discovery after the plaintiff failed to serve a trade secret identification statement, and it took an appeal to reverse the sanctions – even though California has a statute requiring that a trade secret plaintiff provide a reasonably particular identification of alleged secrets before pursuing discovery.[17] In another case, a Massachusetts court repeatedly rejected the defendant's efforts to learn the details of the alleged secrets.[18]

¶33 Rulings like these are outliers. But three other mistakes that courts make are more common, and perhaps less obvious. One is not recognizing that the identification of the trade secret claims is a separate issue distinct from whether the information at issue is secret, because that identification is a necessary preliminary step leading to the secrecy analysis. In such cases, courts conflate identification questions with the secrecy question, confusing the discussion.[19]

(identification "prevents plaintiffs from using the discovery process as a means to obtain the defendant's trade secrets."); Data General Corp. v. SCI Sys., Inc., Civ. A. No. 5662, 1978 WL 22033, at *1 (Del. Ch. Nov. 27, 1978) (identification serves to prevent the plaintiff from going through the defendant's information to gain "an unfair business advantage."); WEIL & BROWN, *supra* note 4, at § 8:58 (claiming that purpose of California's identification statute is "to prevent plaintiff from conducting 'fishing expeditions' into competitors' business files by unfounded claims of trade secret misappropriation.").

[17] *See* Roup v. Super. Ct., No. B188652, L.A.S.C. No. BC328972, 2006 WL 710891, at *1 (Cal. Ct. App. Mar. 22, 2006) (unpublished).

[18] *See, e.g.*, Storage Tech. Corp. v. Custom Hardware Eng'g & Consulting, Inc., No. Civ.A. 02-12102-RWZ, 2005 WL 283200, at *1 (D. Mass Feb. 7, 2005) (referring to unspecified "rules" when refusing again to require detailed identification: "CHE objects to the Master's denial of yet another attempt to gain detailed identification of Storage Tech's copyright and trade secret claims. Much of what the Master rejected, the court had previously ruled out of order, or Storage Tech had in the interim supplied. The rules do not sanction the degree of detail CHE seeks to extract."); Storage Tech. Corp. v. Custom Hardware Eng'g & Consulting, Inc., No. Civ.A. 02-12102-RWZ, 2003 WL 22462494, at *1 (D. Mass Oct. 30, 2003) (on pre-discovery order in software case, rejecting defendant's attempt to find out exactly what source code was claimed as secret: "Defendant proposed that plaintiff provide a detailed list of the trade secret allegedly misappropriated to which plaintiff objects. This appears to be another request for the identification of each line of the maintenance source code implicated in these proceedings. I remain unpersuaded that defendant is either entitled to discover that level of detail or that such is necessary to mount an adequate defense.").

[19] *See, e.g.*, Excelligence Learning Corp. v. Oriental Trading Co., No. 5:03-CV-4947 JF (RS), 2004 WL

¶34 The second mistake is assuming that descriptions of technical categories and concepts such as "source code" or "placement of capacitors in the schematic for the ABC project" are sufficient to identify alleged secrets – perhaps because courts do not always recognize how much public domain information exists in such broadly defined technical categories. We will describe several such rulings below.

¶35 The third common mistake, and perhaps the worst, is accepting a plaintiff's argument that because "combination trade secrets" are claimed, the plaintiff need not make a precise identification of such alleged secrets. A "combination trade secret" is a multi-element claim that, when valid, ties non-secret items of information together in a unique manner to form a trade secret. The concept is dangerous, however, because trade secret plaintiffs often string together non-secret items that have no functional interrelationship to avoid a defendant's showing that the individual items are non-secret. Attorneys also use the "combination" concept to alter claims, and to create more sets of alleged intellectual property than the plaintiff ever actually thought about or linked together. But combination claims can fail for a number of reasons, just as individual trade secret claims can, and thus they should not provide a shield against identification.[20]

¶36 Trade secret plaintiffs use the "combination" argument during identification disputes to confuse courts and escape a precise identification of the alleged secrets. If a defendant argues for a precise identification, the plaintiff will often respond that it claims "combination" secrets in an "entire process" rather than individual secrets, and that identifying individual elements should therefore be unnecessary. Or, to the same effect, the plaintiff argues that its secret is its entire base of software source code, its entire chip design, and so forth, without regard to identifying what exactly about those broad categories are asserted as an allegedly misappropriated secret.

¶37 The "combination" concept can create a major loophole for a plaintiff seeking to avoid identification. Perhaps most dangerous, a plaintiff can use the "combination" theory to altèr and revise its claims in different mixes of subsets, to gerrymander a claim so that the defense cannot focus its research efforts on defeating the final version. If we take, for example, seven software algorithms and assume that five are in the public domain, the plaintiff might alter the claim several times to create subsets of the seven where at least one of the included algorithms is secret, in order to claim the non-secret algorithms as secret as well. With a simple set of seven, there is a multiplicity of mathematically possible variations of subsets of two or more elements. Of course, the

2452834, at *3-4 (N.D. Cal. June 14, 2004) (reviewing whether plaintiff's Cal. Civ. Proc. Code. sec. 2019.210 identification statement was sufficient and asking whether the information was secret instead of whether identification was sufficiently specific); Momswin, L.L.C. v. Lutes, No. Civ.A. 02-2195-KHV, 2003 WL 21554944, at *7 (D. Kan. July 8, 2003) (denying plaintiff's motion for summary judgment for failure to establish conclusively that information was secret, but seemingly conflating identification requirement with secrecy requirement in discussion); Lovell Farms, Inc. v. Levy, 641 So. 2d 103, 105 (Fla. Ct. App. 1994) (affirming denial of request for temporary restraining order and requiring that plaintiff first show existence of trade secret; seemingly blending an identification requirement and proof of secrecy through an in-camera review procedure); Gabriel Int'l, Inc. v. M&D Indus. of Lou., Inc., 719 F. Supp. 522, 524-25 (W.D. La. 1989) (in confusing ruling, court required that a trade secret plaintiff prove the existence of a secret early in the lawsuit, apparently before seeking third party discovery, but in so doing appears to have conflated the need to identify the alleged secrets with the ultimate proof of secrecy or non-secrecy).

[20] For a detailed description of "combination trade secret" claims and citations to numerous cases where such claims have failed, see Tait Graves & Alexander Macgillivray, *Combination Trade Secrets and the Logic of Intellectual Property*, 20 SANTA CLARA COMPUTER & HIGH TECH. L.J. 261 (2004).

algorithms may not in reality interoperate together, and perhaps should properly be defined as individual trade secret claims rather than "combination" claims. But without requiring a precise identification of the "combination" trade secret at issue, the defense may be unable to raise that argument. Courts need to be aware of this common litigation tactic and nail down exactly what permutations and subsets are actually claimed as secret.

¶38 But all too often, courts have confused the question of (1) whether the plaintiff claims "combination" secrets instead of individual secrets with (2) whether the plaintiff should be required to precisely identify its alleged trade secrets regardless of whether they are claimed in combinations or individually.

¶39 There are several published rulings where courts have failed to require a precise identification of the alleged secrets as a result of conflating these two issues.[21] In one, a plaintiff vaguely claimed secrets somewhere within 500 pages of materials, and the defendant argued on appeal after a jury verdict that the plaintiff did not specify what the secrets were. The court merely noted that a plaintiff can have a combination trade secret in material that includes elements that are individually non-secret, and did not ask whether any such combination had been properly identified.[22] And in one of the most questionable trade secret rulings on record, a Pennsylvania district court rejected a defendant's identification argument by holding that the plaintiff's set of generalized business concepts for running a tanning salon was an "entire methodology" that added up to form a trade secret, without any specific identification. By avoiding the identification analysis and stringing together vague business concepts into a combination trade secret, the decision essentially created a non-competition agreement and held the defendant liable for violating it.[23] Of course, a plaintiff certainly is capable of properly identifying an alleged combination trade secret.[24] Indeed, many courts have required precise identification of "combination trade secrets." We will discuss those cases below when proposing solutions.

¶40 With these policy considerations and common mistakes in mind, we will survey the nationwide case law, and then offer specific proposals for addressing identification disputes.

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[21] Courts sometimes sidestep the identification question by accepting a plaintiff's argument that its entire process or software was at issue. *See, e.g.*, Trandes Corp. v. Guy F. Atkinson Co., 996 F.2d 655, 662 (4th Cir. 1993) (refusing to overturn jury verdict despite plaintiff's failure to identify precise secrets, and affirming on questionable ground that entire object code software was secret without addressing whether any secrets were identified in the functionality or other aspects of the executable software; even with finalized object code, we believe that a plaintiff should identify what about the software is not generally known to the trade); Touchpoint Solutions, Inc. v. Eastman Kodak Co., 345 F. Supp. 2d 23, 28-29 (D. Mass. 2004) (granting in part plaintiff's motion for preliminary injunction despite defendant's argument that plaintiff had not specifically identified alleged secrets; court accepted plaintiff's characterization of "source code, implementation, overall design and 'distributed computing model'" as a design that was "unique, complex, and apparently valuable" without focusing on whether specific details had been identified).

[22] *See* 3M Co. v. Pribyl, 259 F.3d 587, 595-96 (7th Cir. 2001).

[23] *See* Tan-Line Studios, Inc. v. Bradley, Civ.A. No. 84-5925, 1986 WL 3764, at *7 (E.D. Pa. Mar. 25, 1986) (ruling following bench trial; referring to general definition of a combination trade secret).

[24] *See* Rohm & Haas Co. v. Adco Chem. Co., 689 F.2d 424, 432 n.7 (3d Cir. 1982) (plaintiff claimed combination trade secret in chemical process and "did put in evidence detailed descriptions of the Process," though specificity unclear from published decision).

III. HOW COURTS NATIONWIDE HAVE ADDRESSED IDENTIFICATION DISPUTES

¶41 There are several stages of a case where courts face disputes over the identification of alleged trade secrets: the pleading stage, on a request for a temporary restraining order or preliminary injunction, just before discovery begins, during discovery, on a motion for summary judgment, during trial, and after trial.

¶42 For the most part, the majority trend is to require a detailed identification of alleged secrets – particularly on a request for an injunction, during discovery, and on a motion for summary judgment. Rulings are inconsistent at the pleading stage, probably because of liberal notice pleading requirements. In turn, rulings after trial often go against the defendant, likely because the defense waited too long to raise the identification issue and, more importantly, because courts are loath to overturn jury verdicts.

A. The Pleading Stage

¶43 In some cases, trade secret defendants have moved to dismiss the complaint, or to obtain a more definite statement, when the plaintiff is vague regarding the alleged secrets. Some courts have required more information at the pleading stage,[25] though plaintiffs obviously need not disclose material believed to be secret in a public complaint, and liberal notice pleading standards often mean little is required.[26] As one court explained the general rule, "courts are in general agreement that trade secrets need not be disclosed in detail in a complaint alleging misappropriation . . . . The query is whether

[25] *See, e.g.*, Metis Int'l, L.L.C. v. Ace INA Holdings, Inc., No.Civ.A.SA.04CA-1033-XR, 2005 WL 1072587, at *5 (W.D. Tex. May 6, 2005) (granting Rule 12(e) motion and requiring plaintiff to plead more about the categories of alleged secrets being claimed); Cambridge Internet Solutions, Inc. v. Avicon Group, No. 99-1841, 1999 WL 959673, at *2 (Mass. Ct. App. Sept. 21, 1999) (granting in part motion for a more definite statement where plaintiff alleged that some alleged secrets where in specific document, but did not do so for alleged "customer material" secrets); Diodes, Inc. v. Franzen, 260 Cal. App. 2d 244, 253 (Cal. Ct. App. 1968) (sustaining demurrer to third amended complaint where plaintiff failed to provide more than highly generalized description of alleged secrets; "the complainant should describe the subject matter of the trade secret with sufficient particularity to separate it from matters of general knowledge in the trade or of special knowledge of those persons who are skilled in the trade, and to permit the defendant to ascertain at least the boundaries within which the secret lies."); AMP, Inc. v. McCaughey, 38 Pa. D. & C.2d 109, 118 (Pa. Ct. Cm. Pl. 1966) ("In requiring a more specific pleading, we are not indicating that plaintiff must plead trade secret processes, trade secrets, or the like. However, it is apparent that plaintiff can provide defendants with at least an identification and nature of the products, persons, time and places involved, so as to permit them to know that against which they are to prepare a defense.").

[26] *See, e.g.*, Automed Tech., Inc. v. Eller, 160 F. Supp. 2d 915, 921 (N.D. Ill. 2001) (general references to categories of alleged secrets sufficient to withstand motion to dismiss, but "plaintiff will ultimately need to identify which specific designs, software or research defendant allegedly misappropriated."); Kosower v. Gutowitz, No. 00 Civ. 9011(JGK), 2001 WL 1488440, at *8 (S.D.N.Y. Nov. 21, 2001) (general references to claimed secrets permissible because facts as alleged must be treated as true; motion to dismiss denied); Labor Ready, Inc. v. Williams Staffing, L.L.C, 149 F. Supp. 2d 398, 411 (N.D. Ill. 2001) (denying Rule 12(e) motion because general identification of alleged secrets met notice pleading standards; noting that more would be required at the summary judgment stage;); Cinebase Software v. Media Guaranty Trust, Inc., No. C98-1100 FMS, 1998 WL 661465, at *7-8 (N.D. Cal. Sept. 22, 1998) (on motion to dismiss, identification "in general terms" sufficed, but "plaintiff will have to identify its alleged trade secrets with much greater particularity in order to prevail on this claim"); Savor, Inc. v. FMR Corp., No. CIV.A. 00C-10-249JRS, 2002 WL 393056, at *4 (Sup. Ct. Del. Mar. 14, 2002) (dismissing third amended complaint with prejudice where plaintiff did not provide any detail for allegedly misappropriated trade secrets, even though complaint filed partially under seal and plaintiff pointed to attached documents, claiming "whole process" as secret), *rev'd*, 812 A.2d 894, 897 (Del. 2002) (reversing based on liberal pleading standards).

the allegations provide the defendant with notice as to the substance of the claims."[27] In some cases where courts have required more detail in a complaint, it is unclear whether the amended complaint would be filed under seal, though it would seem that a confidential or redacted filing would be appropriate.[28]

B. Requests for Injunctive Relief

¶44 Many trade secret cases begin with a rushed request for a temporary restraining order or preliminary injunction. At that stage, trade secret plaintiffs sometimes make only vague references to the alleged secrets, without providing details. As a result, courts have repeatedly used the identification requirement as a ground to deny the request.[29] Given the courts' general reluctance to enjoin a defendant's

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[27] *See* Dick Corp. v. SNC-Lavalin Constr., Inc., No. 04 C 1043, 2004 WL 2967556 (N.D. Ill. Nov. 24, 2004) (on motion to dismiss and for a more definite statement, general reference to "Joint Venture Data" sufficed).

[28] *See* Combined Metals of Chi. Ltd. Part. v. Airtek, Inc., 985 F. Supp. 827, 832 (N.D. Ill. 1997) (to prevent cross-plaintiff from modifying claims later, and to provide fair notice, court ordered party to identify "specific, concrete secrets" in amended cross-complaint).

[29] *See, e.g.*, MAI Sys. Corp. v. Peak Computer, Inc., 991 F.2d 511, 522-23 (9th Cir. 1993) (reversing preliminary injunction in part where plaintiff failed to "specifically identify" alleged secrets claimed to reside within a "diagnostic software and operating system"); Litton Sys., Inc. v. Sundstrand Corp., 750 F.2d 952, 956 (Fed. Cir. 1984) (applying apparent federal common law to affirm denial of preliminary injunction where, among other things, "Litton's Achilles Heel on this record is its insistence on postponing identification or description of such a broad universe of *thousands* of unidentified trade secrets"); Cataphote Corp. v. Hudson, 422 F.2d 1290, 1296 (5th Cir. 1970) (noting that trial court had correctly denied earlier permanent injunction request because plaintiff had no first "specifically identified and proved" its alleged secrets); Internet Inc. v. Tensar Polytech., Inc., No. Civ. 05-317RHKAJB, 2005 WL 2453170, at *6 n.8 (D. Minn. Oct. 3, 2005) (denying request for preliminary injunction when, inter alia, plaintiff did not "identif[y] specific products that have been successfully modified with the use of information from Brand, much less with the use of specific information alleged to be Internet's trade secrets"); Diamond Power Int'l, Inc. v. Clyde Bergemann, Inc., 370 F. Supp. 2d 1339, 1346 (N.D. Ga. 2005) (denying motion for preliminary injunction when plaintiff claimed secrets in dry hub carriage for sootblower cleaning system but could not identify specific items claimed as trade secrets); Hypred S.A. v. Pochard, No. Civ.04-2773(JNE/JGL), 2004 WL 1386149, at * 5 (D. Minn. June 18, 2004) (rejecting trade secret portion of requested preliminary injunction because plaintiff failed to identify specific alleged secrets and claimed only generic categories of "product formation and manufacturing secrets"); Vital State Can., Ltd. v. Dreampak, LLC, 303 F. Supp. 2d 516, 521-23 (D.N.J. 2003) (denying preliminary injunction where plaintiff identified "overbroad and vague" technology categories, and repeatedly "shifted" its attempted identifications); Compuware Corp. v. IBM, No. 02-CV-70906, 2003 WL 23212863, at *6-7 (E.D. Mich. Dec. 19, 2003) (rejecting motion for preliminary injunction where plaintiff claimed secrets in "unique combination of functions and capabilities" in certain software, "customer preferences," product documentation, and source code; court rejected claims, noting "As for its source code, Compuware has for whatever reason failed to identify any specific lines of source code that have been taken by IBM."); Motorola, Inc. v. Dbtel Inc., No. 02 C 3336, 2002 WL 1610982, at *16-17 (N.D. Ill. July 22, 2002) (plaintiff offered somewhat detailed testimony making general claims about several aspects of its technology, but court found that evidence "confusing, inconsistent, and lacks specificity;" court was unable to tell what exactly plaintiff wanted to enjoin, particularly where "many aspects of Motorola's process for creating a cellular phone involve publicly available equipment and standards," and refused to issue injunction); FSI Int'l v. Shumway, No. CIV.02-402RHKSRN, 2002 WL 334409, at *9 (D. Minn. Feb. 26, 2002) (same where plaintiff sought temporary restraining order but offered only generalized categories instead of identifying alleged secrets); Newleaf Designs, L.L.C v. Bestbins Corp., 168 F. Supp. 2d 1039, 1043-44 (D. Minn. 2001) (same where plaintiff failed to identify several alleged secrets); Am. Sci. & Eng'g Inc. v. Kelly, 69 F. Supp. 2d 227, 238 (D. Mass. 1999) (preliminary injunction denied where plaintiff failed to identify alleged secrets in collimator device); Visionair, Inc. v. James, 606 S.E.2d 359, 364 (N.C. Ct. App. 2004) (affirming denial of request for preliminary injunction where plaintiff "has failed to identify

employment or business on an expedited proceeding without a careful review of the evidence, it is not surprising that plaintiffs' failures to identify the information at issue provides a ready reason for a denial.

¶45 Of course, some trade secret plaintiffs do provide a sufficient identification of their claims when seeking injunctive relief.[30] Indeed, one would expect that in egregious cases – where, say, a former employee downloaded key non-public files the day before resigning – a plaintiff should easily be able to make a precise identification of the alleged secrets to support its request.

¶46 At least one court has required little identification on a request for injunctive relief. That court held that "source code" was a sufficient identification on a request for a preliminary injunction, and attacked the defendant for considering its own software to be confidential while also seeking a better identification of the plaintiff's claim.[31] The court may have conflated the separate considerations of whether or not alleged trade secret is truly secret and whether or not the plaintiff adequately identified the alleged trade secret,

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with any specificity the trade secrets allegedly misappropriated, mentioning only broad product and technology categories."); IBM Corp. v. Seagate Tech., Inc., 941 F. Supp. 98, 100 (D. Minn. 1992) (same where plaintiff admitted that its descriptions of alleged disk drive secrets "do not purport to define precisely the boundaries of each trade secret."); CVD, Inc. v. Raytheon Co., Civil Action No. 81-2216-S, 1981 WL 2162 (D. Mass. Dec. 3, 1981) (request denied where plaintiff failed to identify alleged secrets); Lee Pharms. v. Den-Mart, Inc., 1976 WL 21026 (C.D. Cal. 1976) (somewhat confusing early case where court delayed hearing on requested preliminary injunction in part because plaintiff had refused to identify alleged secrets); Analog Devices, Inc. v. Michalski, 579 S.E.2d 449, 453-54 (N.C. Ct. App. 2003) (affirming denial of motion for preliminary injunction where plaintiff claimed combination trade secret in chip designs, submitted documents and schematics, and listed general concepts such as "the overall design and implementation of Analog's 94xx products"; Court stated "Analog invites this Court to acknowledge the existence of trade secrets in the submitted information without bearing the burden of identifying those trade secrets. We will not read into Analog's claims specific identification of devices worthy of trade secret protection when it is Analog's burden to come forward with evidence of such devices."); Grow Co., Inc. v. Chokshi, 2006 WL 551367, at *4 (N.J. Super. Ct. Mar. 3, 2006) (unpublished) (motion to reconsider denial of preliminary injunction denied where plaintiff "fails to specifically identify a trade secret" in "processes and formulations"); Iron Age Corp. v. Dvorak, 880 A.2d 657, 665-66 (Pa. Ct. App. 2005) (denying preliminary injunction based on "inevitable disclosure"-type theory denied, in part because plaintiff failed to identify allegedly confidential information at issue); Southwest Research Inst. v. Keraplast Tech., Ltd., 103 S.W.3d 478, 483 (Tex. Ct. App. 2003) (vacating temporary restraining order where plaintiff "failed to identify any specific trade secret that should be protected," and instead broadly claimed that everything defendant learned from plaintiff was secret).

[30] *See e.g.*, Whyte v. Schlage Lock Co., 101 Cal. App. 4th 1443, 1453 (2002) (holding that plaintiff sufficiently identified alleged secrets during request for temporary restraining order though combination of generic categories and "descriptions made pursuant to" California Code of Civil Procedure section 2019.210 and other pleadings; published opinion did not quote from the latter documents, no doubt to preserve the claimed secrecy, thus leaving unclear what level of precision was supplied); Lowell Anderson, *Litigation Issues*, *in* TRADE SECRETS PRACTICE IN CALIFORNIA § 11.21 (2d ed. Supp. 2005) ("Unfortunately for practitioners seeking guidance on §2019(d), the court based its ruling in part on information contained in the plaintiff's §2019(d) statement, which was not disclosed in the published opinion."). At least two subsequent federal cases have incorrectly assumed that *Whyte* stood for the proposition that California's section 2019.210 allows identification by generic categories – though the subsequent *Advanced Modular Sputtering* case, discussed below, mooted the question by setting forth the California standard. *See, e.g.*, Pixion, Inc. v. Placeware, Inc., 421 F. Supp. 2d 1233, 1242 (N.D. Cal. 2005); Excelligence Learning Corp v. Oriental Trading Co., Inc., No. 5:03-CV-4947 JF (RS), 2004 WL 2452834, at *3-4 (N.D. Cal. June 14, 2004).

[31] *See* Cisco Sys., Inc v. Huawei Tech., Co., 266 F. Supp. 2d 551, 555-56 (E.D. Tex. 2003) (granting preliminary injunction; no sign in published opinion that plaintiff provided specific identification of alleged software code trade secrets).

because it did not provide a separate analysis for identification and then secrecy in sequential order.

¶47 An issue related to injunctive relief is whether the court itself properly identifies the alleged secrets in the order so that the defendant knows exactly what it is forbidden from using. Some appellate courts have reversed orders for injunctive relief on this basis.[32] It stands to reason that if a trade secret plaintiff fails to provide a precise identification of its alleged secrets, a court will not be able to issue an appropriately specific order against the defendant.

C. The Pre-Discovery Stage

¶48 If a defendant does not challenge the specificity of the complaint, and if the plaintiff does not seek immediate injunctive relief, the next phase of the case where identification disputes arise is the moment when the plaintiff seeks to commence discovery on its trade secret accusations. Several jurisdictions have required that trade secret plaintiffs make at least a "reasonably particular" identification of their alleged secrets as a condition precedent to seeking discovery from the defendant. In those jurisdictions, pre-discovery identification disputes are common.

¶49 Courts in several states (or federal courts applying state law) have required a pre-discovery identification procedure by common law: Delaware,[33] Illinois,[34] Massachusetts,[35] Minnesota – which requires the most detail[36] – and possibly Florida.[37]

[32] *See, e.g.*, Corning Inc. v. Picvue Elec., Ltd., 365 F.3d 156 (2d Cir. 2004) (remanding where trial court's preliminary injunction was too vague under FRCP Rule 65; impossible to tell from order what information was subject of the injunction); Roton Barrier, Inc. v. Stanley Works, 79 F.3d 1112, 1121-22 (Fed. Cir. 1996) (two post-judgment inunctions overbroad under Rule 65(d) for failure to specify exactly what information was barred from use); American Can Co. v. Mansukhani, 742 F.2d 314, 333 (7th Cir. 1984) (reversing preliminary injunction in part because order was too vague under Rule 65(d); order barred used of "compositionally similar" inks which could be "attributed principally" to the plaintiff's trade secrets without identifying precisely what was barred); E.W. Bliss Co. v. Struthers-Dunn, Inc., 408 F.2d 1108, 1114-15 (8th Cir. 1969) (setting aside preliminary injunction where order was "excessively broad" under FRCP 65(d) and listed only high-level technical categories instead of specifying exactly what information was subject of injunction); Microstrategy, Inc. v. Business Objects, S.A., 331 F. Supp. 2d 396, 431 (E.D. Va. 2004) (in post-trial, permanent injunction following finding of misappropriation, plaintiff's proposed injunction "too broad" in scope; limiting injunction to "specific documents identified as trade secrets").

[33] *See, e.g.*, Leucadia, Inc. v. Applied Extrusion Tech., Inc., 755 F. Supp. 635, 637 (D. Del. 1991) (denying discovery against defendant because plaintiff's statement too high-level); Miles Inc. v. Cookson Am., Inc., Civ. A. No. 12,310, 1992 WL 136381, at *1 (Del. Ch. June 16, 1992) (unpublished) (statement generally outlining alleged secrets insufficient to take discovery against defendant); Magnox v. Turner, Civ. A. No. 11951, 1991 WL 182450, at *1 (Del. Ch. Sept. 10, 1991) (unpublished) (same where plaintiff served discovery without first making identification of alleged secrets with reasonable particularity); Engelhard Corp. v. Savin Corp., 505 A.2d 30, 33 (Del. Ch. 1986) (same where plaintiff failed to make required statement with reasonable particularity); Data Gen. Corp. v. SCI Sys., Inc., Civ. A. No. 5662, 1978 WL 22033, at *2 (Del. Ch. Nov. 27, 1978) (unpublished) (early case allowing defendant to file papers with court stating which alleged secrets in plaintiff's identification it was "unable to comprehend" in order to rule on motion for protective order).

[34] *See* Automed Tech., Inc. v. Eller, 160 F. Supp. 2d 915, 925-26 (N.D. Ill. 2001) (citing Delaware law to hold that plaintiff must identify alleged secrets with "reasonable particularity" before taking discovery "so that we can evaluate the relevance of plaintiff's discovery and address any objections.").

[35] *See* L-3 Comm. Corp. v. Reveal Imaging Tech., Inc., 2004 WL 2915743, at *13 (Mass. Sup. Ct. Dec. 2, 2004) (holding that plaintiff must specifically identify alleged secrets before commencing discovery). This decision is only an unpublished trial court order, however, so the status of pre-discovery identification remains unclear in Massachusetts.

In addition, a federal court in New York has addressed a defendant's argument that the plaintiff should not be able to start discovery on the trade secret claim without first making an identification of the alleged secrets by sending the dispute to a discovery master, but it did not attempt to craft a rule of general application to other cases.[38]

¶50 California is the only state to codify a pre-discovery identification rule by statute.[39] California's legislature enacted what is now Code of Civil Procedure section 2019.210 in 1985 as part of the state's Uniform Trade Secrets Act. The impetus for the statute came from a state bar memorandum to the state legislature proposing the text of the statute and noting the discovery abuses that trade secret plaintiffs often engage in when they fail to identify the alleged secrets:

> One area not addressed by the Uniform Act is the area of plaintiff's abuse in initiating trade secret lawsuits for the purpose of harassing or even driving a competitor out of business by forcing the competitor to spend large sums in defending unwarranted litigation. For example, when a plaintiff's employee quits and opens a competing business, a plaintiff often files a lawsuit for trade secret misappropriation which states that the defendant took and is using plaintiff's trade secrets, but does not identify the trade secrets. The plaintiff can then embark upon extensive discovery which the new business is ill equipped to afford. Furthermore, by not informing the defendant with any degree of specificity as to what the alleged trade secrets are, defendant may be forced to disclose its own business trade secrets, even though those matters may be irrelevant, and the defendant may not learn the exact nature of the supposedly misappropriated trade secrets until the eve of trial.[40]

¶51 Courts and commentators have identified a number of salutary policy goals California's statute serves,[41] though again we do not agree with all of them and find their

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[36] *See* Porous Media Corp. v. Midland Brake, Inc., 187 F.R.D. 598, 600 (D. Minn. 1999) (where plaintiff described only six high-level concepts, court held that trade secret plaintiffs must provide an identification with "the same specificity" required on a motion for preliminary injunction or at trial; "The orderly disposition of cases involving claims of misappropriation of trade secrets cannot permit a situation where the details concerning the claimed trade secrets are not disclosed at an early date in the litigation.").

[37] *See* Del Monte Fresh Produce Co. v. Dole Food Co., 148 F. Supp. 2d 1322, 1325 (S.D. Fla. 2001) (applying both California pre-discovery statute and Florida common law to require identification with reasonable particularity in a case where some discovery had already begun; not entirely clear whether court believed that district courts applying Florida trade secret law should apply a pre-discovery identification procedure in future cases).

[38] *See* Power Conversion, Inc. v. Saft Am., Inc., 1985 WL 1016, at *1-3 (S.D.N.Y. May 1, 1985) (where both parties accused one another of misappropriation, matter sent to independent expert to receive parties' submissions and designate areas for discovery). It should be noted that discovery masters are subject to confidentiality requirements – often as defined in the parties' protective order governing the case.

[39] CAL. CIV. PROC. CODE § 2019.210 (West 2006) ("In any action alleging the misappropriation of a trade secret under the Uniform Trade Secrets Act . . . before commencing discovery relating to the trade secret, the party alleging the misappropriation shall identify the trade secret with reasonable particularity subject to any orders that may be appropriate under [the UTSA subsection relating to confidentiality orders].").

[40] Computer Econ., Inc. v. Gartner Group, Inc., 50 F. Supp. 2d 980, 985 n.6 (S.D. Cal. 1999) (quoting from statute's legislative history).

[41] Policies cited include (1) preventing overbroad trade secret accusations that improperly include information in the public domain; (2) giving the defendants fair notice of the exact charges against them before discovery begins; and (3) preventing plaintiffs from conducting "fishing expeditions" into the files

summaries incomplete. Federal courts in California have applied the statute in trade secret cases under the Erie Doctrine,[42] and courts elsewhere have also used it in cases under California law.[43]

¶52 Because so many trade secret cases have arisen in Silicon Valley, rulings on the degree of specificity required under California's pre-discovery statute have been common in the federal Northern District of California.[44] One such ruling is worth quoting, to illustrate how courts applying California law differ from courts in those jurisdictions which lack a pre-discovery identification requirement:

¶53 The Amended Identification of Trade Secrets shall be narrowed to include only items that Plaintiff considers are its actual trade secrets, and only those trade secrets that Plaintiff has reasonable grounds to allege were misappropriated. . . . If Plaintiff contends that a trade secret consists of a specific combination of items, it shall so state and concisely describe the combination. If Plaintiff contends that its specific use of an otherwise publicly known item constitutes its secret, it shall so state and concisely describe the use. All trade secrets shall be described in narrative form, rather than by cross-reference to other trade secrets or documents. If Plaintiff references a document as setting forth one or more trade secrets, it shall specify precisely which portions of the document describe the trade secret(s).[45]

¶54 And in 2005, a California appellate court for the first time issued a ruling providing guidelines for what the statute requires. The court held that while absolute precision is not required at the pre-discovery stage, enough must be provided to separate alleged secrets from matters known to the trade:

> The letter and spirit of section 2019.210 require the plaintiff, subject to an appropriate protective order, to identify or designate the trade secrets at issue with "'sufficient particularity'" to limit the permissible scope of discovery by distinguishing the trade secrets "'from matters of general knowledge in the trade or of special knowledge of those persons . . . skilled in the trade.'" . . . The degree of "particularity" that is "reasonable" will differ, depending on the alleged trade secret at issue in each case. Where, as here, the alleged trade secrets at issue consist of incremental variations on, or advances in the state of the art in a highly special-

of business rivals in order to concoct charges against them. *See id.* at 985; WEIL & BROWN, *supra* note 4, at § 8.60 (describing purposes of statute); MILGRIM, *supra* note 4, at § 16.01[5][b] (noting fair notice aspect of the statute).

[42] *See Computer Econ.*, 50 F. Supp. 2d at 985 (detailing purposes of statute and its legislative history). *See also* Neothermia Corp. v. Rubicor Med., Inc., 345 F. Supp. 2d 1042, 1044 (N.D. Cal. 2004) (noting that using the statute in a manner inconsistent with the Federal Rules of Civil Procedure regarding amendments could create an *Erie* problem).

[43] *See, e.g.*, Convolve, Inc. v. Compaq Computer Corp., 2002 WL 14361, at *1 (S.D.N.Y. Jan. 4, 2002) (noting that special master had ruled on section 2019.210 issues such that discovery could commence).

[44] *See, e.g.*, Myrio Corp. v. Minerva Network Inc., 2001 U.S. Dist. LEXIS 10461, at *1-3 (N.D. Cal. April 4, 2001) (finding statement insufficient); Sys. Am., Inc. v. Softline, Inc., 1996 U.S. Dist. LEXIS 22415, at *1 (N.D. Cal. October 30, 1996) (finding statement "insufficient" and "extremely broad" where it outlined "a number of categories of documents"); Cal. Micro Devices Corp. v. Universal Semiconductor, Inc., 1995 WL 705144, at *1 (N.D. Cal. Nov. 21, 1995) (noting that because plaintiff had provided Cal. Civ. Proc. Code sec. 2019.210 statement, defendant had to respond to deposition questions by plaintiff).

[45] *See Myrio Corp.*, 2001 U.S. Dist. LEXIS 10461, at *1-3.

> ized technical field, a more exacting level of particularity may be required to distinguish the alleged trade secrets from matters already known to persons skilled in that field.[46]

¶55 It remains somewhat unclear what "reasonable particularity" means in any given case. Does it mean that a plaintiff must provide 51 percent of the details that would be necessary for a completely precise identification of each claim, 67 percent, 75 percent, or more? None of the jurisdictions that require a pre-discovery identification with "reasonable particularity" have yet defined exactly what minimum degree of precision a trade secret plaintiff must aim for.

D. The Discovery Stage

¶56 The discovery stage is the heart of where identification disputes arise, because discovery is the means by which the defense can demand a complete, precise identification of each alleged secret. Again, however, the courts have been inconsistent in the amount of detail they have required – though the skill with which the defense demands identification no doubt plays a role in the varying holdings.

¶57 Some courts have readily granted defense motions to compel a detailed identification of the trade secret claims, usually in response to defense interrogatories.[47] In a 2006 Washington case, for example, the defendant served an identification interrogatory. In response, the plaintiff "referenced its complaint and then listed generic categories of trade secrets: 'installer list/network,' 'pricing strategy and policies,' and 'customer lists.'" It also included the evasive phrase "among other things." The court granted a motion to compel, noting that "[d]efendants are entitled to discovery related to all of the so-called 'other things' allegedly misappropriated."[48]

¶58 In turn, a 2005 Texas case describes how, on a motion to compel, a trial court addressed a plaintiff's recitation of generic concepts in its initial response by flipping

[46] *See* Advanced Modular Sputtering, Inc. v. Super. Ct., 132 Cal. App. 4th 826, 835-36 (2005).

[47] *See* Dapco Indus., Inc. v. Matec Corp., 1998 WL 563847, at *1 (Fed. Cir. 1998) (unpublished) (affirming dismissal of complaint because plaintiff did not respond to identification interrogatory or court order on motion to compel requiring the same); StonCor Group, Inc. v. Campton, 2006 WL 314336, at *1-2 (W.D. Wash. Feb. 7, 2006) (granting motion to compel); Excelligence Learning Corp v. Oriental Trading Co., 2004 WL 2452834, at *3-5 (N.D. Cal. Jun. 14, 2004) (granting motion to compel interrogatory requesting that plaintiff "identify in detail" alleged secrets where plaintiff had apparently listed only general categories); Compuware Corp. v. Health Care Serv. Corp., 2002 WL 485710, at *7 (N.D. Ill. Apr. 1, 2002) (issuing sanctions where defendant won motion to compel regarding interrogatory requesting identification of alleged secrets but plaintiff "dragged its feet" in responding, and merely listed functions of allegedly secret software); Multimedia Cablevision, Inc. v. Cal. Sec. Co-op, Inc., 1996 WL 447815, at *1-2 (D. Kan. Jul. 30, 1996) (defendant's interrogatory only asked plaintiff to identify the *documents* which comprised the basis for the trade secret claim; nonetheless, court granted motion to compel a better answer regarding the documents in question and issued sanctions against plaintiff); Uresil Corp. v. Cook Group, Inc., 135 F.R.D. 168, 174 (N.D. Ill. 1991) (granting motion to compel better interrogatory responses; "[I]t is clear that Uresil has not identified the components and/or concepts incorporated in the products Uresil claims Cook misappropriated. Nor does Uresil identify all information and documents alleged by Uresil to be confidential and to have been misappropriated by the defendant."); *See also* Microwave Research Corp. v. Sanders Assoc., Inc., 110 F.R.D. 669, 673-75 (D. Mass. 1986) (denying plaintiff's motion to compel defendant to produce documents where, after depositions, plaintiff identified only a general list of products in which it claimed trade secrets; discussion and holding are somewhat unclear).

[48] *See StonCor*, 2006 WL 314336, at *1-2.

those categories back at the plaintiff and requiring a precise identification regarding each of them:[49] There, the court ordered the plaintiff to

> "state specifically the identity of each 'functionality,' 'data field,' 'rule,' reflex,' 'structure,' 'design,' 'architecture,' 'integration of combination of various components,' 'negative knowledge,' 'method or process utilized for manipulation information,' 'trigger,' 'calculation code,' 'formula,' 'distribution,' and 'format, content, sequence, total structure and record selection of various reports,' or other feature, function or element of [plaintiff's] automobile dealership management system or related written materials that is the subject of this case that [plaintiff] contend[s] is a trade secret accessed or misappropriated by [appellees]. Each trade secret claimed by [plaintiff] shall be separately identified by [it] in such answers."[50]

¶59 In another case, a court rejected the plaintiff's initial interrogatory response, which listed a set of generic and conclusory phrases and made generalized references to a "ratio of ingredients." The court noted that the plaintiff "does not state how the ratio of ingredients relates to the manufacturing process, nor does it precisely describe how the manufacturing process varies according to the factors it has recited." In requiring a better response, the court held that the plaintiff's "answers concerning the nature of its alleged trade secrets are evasive, ambiguous, and incomplete."[51]

¶60 Similarly, a Pennsylvania court in an early case from 1972 found a trade secret plaintiff's responses to interrogatories seeking a specific identification of the alleged secrets "wholly evasive and nonresponsive," and reacted to the plaintiff's recitation of generic categories by rhetorically asking the plaintiff what within them was alleged to be secret:[52] "The answers to #20 can hardly be construed to enlighten Defendants as to the information allegedly misappropriated. What are the confidential materials? Who are the confidential suppliers of such materials? What are the confidential names and addresses of such customers, potential customers, dealers, distributors and health department officials?"[53]

¶61 Other courts have ruled against the plaintiff based on issues arising during a deposition,[54] or sent the matter to a special master to oversee the identification process.[55]

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[49] *See* Universal Computer Sys., Inc. v. Dealer Solutions, L.L.C., 183 S.W.3d 741, 745 (Tex. Ct. App. 2005) (dicta discussion of prior case proceedings; holding concerned arbitration issues).
[50] *Id.* at 745 n.1.
[51] *See* Unicure, Inc. v. Thurman, 97 F.R.D. 7, 13-14 (W.D.N.Y. 1982).
[52] *See* Cromaglass Corp. v. Ferm, 344 F. Supp. 924, 928 (M.D. Penn. 1972) (granting motion for imposition of sanctions for failure to answer interrogatories, including designation of facts alleged by defendants as being established for purposes of litigation).
[53] *Id.* at 927.
[54] *See* Diversified Tech., Inc. v. Dubin, 156 F.R.D. 132 (S.D. Miss. 1994) (depublished) (issue preclusion sanctions where plaintiff's refusal to identify alleged secrets included plaintiff's attorney giving instructions not to answer identification questions during Rule 30(b)(6) deposition).
[55] *See* Xerox Corp. v. IBM Corp., 64 F.R.D. 367, 371-72 (S.D.N.Y. 1970) (in early case where special master ordered identification, plaintiff's submission of list of documents in which alleged secrets were claimed to reside was insufficient).

¶62 But at least two courts have allowed plaintiffs to respond to interrogatories with more generalized information such as categories in which the alleged secrets fall. These appear to be the minority position, and it is not clear from the rulings how the defense worded its discovery requests.[56] At least one court has not ordered more detail where the defendant's request was badly constructed.[57]

E. The Summary Judgment Stage

¶63 A plaintiff's failure to identify its alleged secrets during discovery can, and often does, lead to summary judgment. Courts have frequently granted summary judgment for the defense based on a failure to sufficiently identify the trade secret claims.[58]

¶64 In one of the most famous such cases,[59] the Ninth Circuit affirmed summary judgment on a trade secret claim where the plaintiff asserted secrets in a film projection

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[56] *See* AlliantGroup, LP v. Axiom Custom Bus. Solutions, Inc., 2006 WL 568363, at *1 (S.D. Tex. 2006) (denying motion to compel regarding interrogatory requesting identification of specific alleged secrets because plaintiff "has sufficiently identified six categories of purported trade secret at issue"); C&F Packing Co. v. IBP, Inc., 1994 WL 36874, at *12 (N.D. Ill. 1994) (denying motion to compel where plaintiff attached further information identifying alleged secrets in its supplemental response though court did not clearly state whether any precision was supplied and held only that "IBP has been sufficiently *apprised of the basis* for C&F's trade secret claim.") (emphasis added).

[57] *See* Norbrook Labs., Ltd. v. G.C. Hanford Mfg. Co., 2003 WL 1956214, at *2-4 (N.D.N.Y. 2003) (court faulted defendant for the way it crafted its discovery requests in denying further identification).

[58] *See* VFD Consulting, Inc. v. 21st Serv., 425 F. Supp. 2d 1037, 1048-49 (N.D. Cal. 2006) (Minnesota law; plaintiff's "fatal" error of failing to identify "with any particularity" an alleged secret, referring to "the MedDiag system" and former employee's "experience and best judgment in the combination of the research data" for that system); Bradbury Co. v. Teissier-Ducros, 413 F. Supp. 2d 1209, 1222-24 (D. Kan. 2006) (granting summary judgment for defendant where plaintiff provided no detail at all on allegedly secret technology and explaining that "Plaintiff has the burden under the KUTSA to define its trade secrets with the precision and particularity necessary to separate it from the general skill and knowledge possessed by others"); Mextel, Inc. v. Air-Shields, Inc., 2005 WL 226112, at *42 (E.D. Pa. Jan. 31, 2005) (summary judgment for defendant on trade secret claim about a "sensor module" where plaintiff failed to identify what information in documents was allegedly secret); Callaway Golf Co. v. Dunlop Slazenger Group Am., Inc., 318 F. Supp. 2d 205, 215-16 (D. Del. 2004) (California law; one claim rejected where plaintiff made only "conclusory allegations" about golf ball technology, referring generally to information that former employee obtained); Glynn Interactive, Inc. v. Itelehealth, Inc., 2004 WL 439236, at *5 (D. Md. Mar. 9, 2004) (summary judgment for defendant where plaintiff made only exceedingly generic claim that secrets were in "expertise and information provided" and thus failed to identify alleged secrets); Nutrition Mgmt. v. Harborside Healthcare Corp., 2004 WL 764809, at *5 (E.D. Pa. Mar. 19, 2004) (summary judgment for defendant where fraud and other claims involved a trade secret accusation, but plaintiff did not identify secret); Storage Tech. Corp. v. Cisco Sys., Inc., 2003 WL 22231544, at *5-6 (D. Minn. Sep. 25, 2003) (summary judgment for defendant where, among other things, plaintiff failed to specifically identify alleged secrets in a network storage appliance); Canter v. West Pub. Co., 31 F. Supp. 2d 1193, 1203 (N.D. Cal. 1999) (depublished) (same where, among other things, plaintiff disobeyed court's order to identify alleged secrets pursuant to Cal. Civ. Code. sec. 2019.210 by pointing to 21 pages of documents); Utilase, Inc. v. Williamson, 1999 WL 717969, at *7 (6th Cir. Sep. 10, 1999) (unpublished) (summary judgment where plaintiff vaguely identified alleged secrets); Lynchval Sys., Inc. v. Chi. Consulting Actuaries, Inc., 1998 WL 151814, at *5-6 (N.D. Ill. Mar. 27, 1998) (summary judgment where plaintiff pointed only to defendant's technology instead of identifying alleged secrets in its own technology); Furniture Consultants, Inc. v. Acme Steel Door Corp., 658 N.Y.S.2d 284, 285 (N.Y. Ct. App. 1997) (total failure to identify alleged secrets); Julie Research Lab., Inc. v. Select Photographic Eng'g, 810 F. Supp. 513, 520 (S.D.N.Y. 1992) (same where plaintiff failed to identify an alleged secret separate from public domain information), *aff'd*, 998 F.2d 65 (2d Cir. 1993); Universal Analytics, Inc. v. MacNeal-Schwendler Corp., 707 F. Supp. 1170, 1177-78 (C.D. Cal. 1989) (same where plaintiff failed to identify any alleged secrets at all).

[59] *See* IMAX Corp v. Cinema Tech., Inc., 152 F.3d 1161, 1167-68 (9th Cir. 1998) (granting summary

system. The plaintiff failed to identify the precise dimensions and tolerances that constituted its alleged secrets in responding to discovery requests, and the court affirmed the district court and noted that the lack of identification in a "sophisticated and highly complex projector system" left the defendant unable to "prepare its rebuttal."[60]

¶65 In another case, the Seventh Circuit used harsh language against the plaintiff when affirming summary judgment on a software-based trade secret allegation.[61] The plaintiff argued that it had identified its trade secret claims in a 43-page document, but the court rejected that attempt:

> According to IDX, "a 43-page description of the methods and processes underlying and the interrelationships among various features making up IDX's software package" is enough. No, it isn't. These 43 pages describe the software; although the document was created for litigation, it does not separate the trade secrets from the other information that goes into any software package. Which aspects are known to the trade, and which are not? That's vital under the statutory definition. Likewise, IDX's tender of the complete documentation for the software leaves mysterious exactly which pieces of information are the trade secrets.[62]

¶66 In another detailed ruling on a software analysis, a Wisconsin court affirmed a grant of summary judgment on a software claim by noting the many components that make up a software system, and faulted the plaintiff for not identifying what about its own CAD software was distinct from "general knowledge in this niche" of the CAD software industry.[63]

¶67 But some courts, in our view, have gotten it wrong and allowed a plaintiff to survive summary judgment based on generic and non-specific sets of claims.[64] As an example, a federal court in Illinois denied a summary judgment motion where a plaintiff pointed to a long list of items which apparently included such high-level category descriptions as "[a] series resonant inverter driven by a half-bridge" and "[m]eans for reducing the cathode heating voltage after lamp ignition." The court found these non-specific categories to be "quite specific" in denying the motion.[65]

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judgment to defendant where plaintiff claimed secrets in film projector but in response to defendant's interrogatory failed to specific exact trade secret claims "in the precise numerical dimensions and tolerances with sufficient particularity").

[60] *See id.* at 1167.

[61] *See* IDX Sys. Corp. v. Epic Sys. Corp., 285 F.3d 581, 583-84 (7th Cir. 2002).

[62] *Id.* at 583-84.

[63] *See* ECT Int'l, Inc. v. Zwerlein, 597 N.W.2d 479, 483 (Wis. Ct. App. 1999) (affirming grant of summary judgment based on plaintiff's failure to identify alleged software secrets in "software file system" because it did not "describe which of the components" of the software were allegedly misappropriated).

[64] See Twin Vision Corp. v. Bellsouth Commc'n Sys., Inc., 1998 WL 385135, at *3 (9th Cir. Jun. 22, 1998) (unpublished) (though affirming grant of summary judgment on some claims, the court found plaintiff's generic identification of "factory access code" to be specific enough to identify one trade secret claim); *see also* McElmurry v. Fergusson, Inc., 2006 WL 572330, at *19 (M.D.N.C. Mar. 8, 2006) (denying motion for summary judgment where plaintiff pointed to "formulas"; unclear whether any further detail was given).

[65] *See* Nilssen v. Motorola, Inc., 963 F. Supp. 664, 673 (N.D. Ill. 1997). It is possible that the defense failed to explain to the court that the phrases quoted above are not unique in themselves, and that any trade secret would exist in the specific implementation details rather than the broader concepts. For example, the asserted but not identified "means" might be the place where the actual claimed trade secret would reside.

¶68 In another highly questionable ruling, a federal court in Connecticut denied a motion for summary judgment where the plaintiff apparently identified alleged secrets surrounding an executable software program in seven generic categories such as "'descriptions . . . with regard to the concept of how the program worked,'" (ellipsis in original) and "'the program itself.'" The court appears to have allowed the "combination trade secret" tactic described above, and held that because combination trade secrets can exist, the plaintiff's "metaphorical 'recipe'" was a good enough trade secret claim to survive the motion.[66]

¶69 And in some cases, of course, the plaintiff does provide detail sufficient to defeat the defendant's motion for summary judgment.[67]

F. The Pre-Trial, Trial, and Post-Trial Stages

¶70 In some cases, the plaintiff evades identification until the pre-trial stage, and courts sometimes react strongly against the plaintiff.[68] In other cases, some cases make it all the way into trial or post-trial proceedings before the identification dispute comes to a head. In many of these cases, it appears that the defense failed to raise the issue earlier, and sometimes the waiver is apparent.[69] Some courts have ruled against the plaintiff,[70]

A phrase that may appear complex to an outsider may be generic to one skilled in the art, but such distinctions must be drawn for a court reviewing an identification dispute.

[66] *See* Dreamcatcher Software Dev., L.L.C. v. Pop Warner Little Scholars, Inc., 298 F. Supp. 2d 276, 282-83 (D. Conn. 2004).

[67] *See* Charles Schwab & Co. v. Carter, 2005 WL 2369815, at *12 (N.D. Ill. 2005) (denying motion for summary judgment where plaintiff, in opposition papers, detailed its alleged software secrets by Bates number and file type. The court noted that plaintiff had previously been vague in interrogatory responses, but "perhaps in part due to the way in which Defendants framed the question."); Do it Best Corp. v. Passport Software, Inc., 2005 WL 743083, at *13 (N.D. Ill. Mar. 31, 2005) (plaintiff came "dangerously close" to losing on identification issue, but unlike other cases provided "specific lines of code and specific software features for which it claims protection."); Luigino's, Inc. v. Peterson, 2002 WL 122389, at *8-9 (D. Minn. Jan. 28, 2002) (granting and denying in part motion for summary judgment where plaintiff sufficiently identified some alleged secrets, though degree of precision was not described, but alleged only general categories and referred to documents for others); Thermodyne Food Serv. Prod., Inc. v. McDonald's Corp., 940 F. Supp. 1300, 1304-05 (N.D. Ill. 1996) (denying motion for summary judgment on trade secret claim where, among other things, plaintiff attached an identification to complaint that "identifies each component" of alleged secrets and was thus sufficient; presumably the identification was filed under seal); Harbor Software, Inc. v. Applied Sys., Inc., 887 F. Supp. 86, 90 (S.D.N.Y. 1995) (denying summary judgment where plaintiff identified alleged secrets in appendix to complaint, but no details given about level of specificity); Savor, Inc. v. FMR Corp., 2004 WL 1965869, at *6-7 (Del. Super. Ct. Jul. 15, 2004) (noting that "[w]hen the plaintiff claims a 'compilation' trade secret, courts generally require that the trade secret be identified with even greater specificity"; plaintiff's identification, redacted from the published opinion, was sufficient to withstand motion for summary judgment on trade secret element).

[68] *See* Compuware Corp. v. Health Care Serv. Corp., 2002 WL 485710, at *8 (N.D. Ill. Apr. 1, 2002) (where plaintiff refused to provide exact identification of alleged secrets until "less than two weeks before the close of discovery, [it] severely prejudiced [defendant's] ability to chart a course for discovery and its defense in this case."); Package Mach. Co. v. Hayssen Mfg. Co., 164 F. Supp. 904, 910 (E.D. Wis. 1958) (dismissing case for plaintiff's failure to obey pre-trial order and identify its alleged secrets; "Nor should defendants have to wait until plaintiff puts in its case to see what it has to defend against.").

[69] *See* Cargill, Inc. v. Sears Petroleum & Transp. Corp., 388 F. Supp. 2d 37, 65 n.19 (N.D.N.Y. 2005) (on post-judgment motions, jury misappropriation verdict affirmed and by not previously objecting, defendant waived argument that verdict form did not specifically identify alleged secrets).

[70] *See* Composite Marine Propellers, Inc. v. Van Der Woude, 962 F.2d 1263, 1266-68 (7th Cir. 1992) (reversing judgment based on jury verdict where plaintiff failed to specifically identify alleged secrets; noting that specificity was especially important given that defendant held a patent in the technology at

but in many others, especially those after a final judgment, courts leave the ruling against the defendant in place.[71]

¶71 It is worth noting that the defendant's failure to raise the issue until the last minute leads to post-hoc justifications for a faulty judgment or jury verdict, when a timely argument might have changed the course of the case.[72] Because appellate courts tend to uphold jury verdicts, untimely argument can lead to questionable holdings. In one case, a plaintiff apparently failed to identify any specific alleged secrets within its software during a long jury trial, but the defendant does not appear to have raised the issue until post-trial motions. The district court affirmed the jury verdict by resorting to

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issue); AMP Inc. v. Fleischhacker, 823 F.2d 1199, 1203 (7th Cir. 1987) (affirming judgment for defendant where, among other things, plaintiff "consistently failed throughout this litigation to identify any particularized trade secrets actually at risk. Prior to trial, AMP submitted six single-spaced, typewritten pages listing by general item and category hundreds of pieces of AMP internal information. Other courts have warned plaintiffs of the risks they run by failing to identify specific trade secrets and instead producing long lists of general areas of information which contain unidentified trade secrets."), *superceded by statute*, 765 Ill. Comp. Stat. 1065 (1988), *as recognized in* PepsiCo, Inc. v. Redmond, 54 F.2d 1262, 1268-69 (7th Cir. 1995); SL Montevideo Tech., Inc. v. Eaton Aerospace, L.L.C, No. 03-3302, 2006 WL 1472860, at *3 (D. Minn. May 26, 2006) (judgment as a matter of law where plaintiff claimed combination trade secret in motor design failed to specifically identify alleged secrets and instead gave only high-level descriptions; court noted that plaintiff "has not identified the 'guts' of the Montevideo motor or how the specific component parts of the Montevideo motor are combined in the 'guts' to constitute a trade secret when taken as a whole."); MBL (USA) Corp. v. Diekman, 445 N.E.2d 418, 426-27 (Ill. App. Ct. 1983) (early case affirming ruling on motion *in limine* that plaintiff must identify alleged secrets before questioning defendant's witnesses about defendant's technologies); Electro-Craft Corp. v. Controlled Motion, Inc., 332 N.W.2d 890, 897-98 (Minn. 1983) (in early case on appeal after trial, court affirmed misappropriation holding for one alleged secret, but reversed on claimed secrets in brushless motor where no dimensions or tolerances were identified; to the reader, however, neither alleged secrets appears to have been identified in detail).

[71] *See* Roton Barrier, Inc. v. Stanley Works, 79 F.3d 1112, 1117 (Fed. Cir. 1996) (losing defendant argued on appeal that plaintiff failed to prove specific secrets; to the extent this was an identification argument (which is not entirely clear), court held that plaintiff had proved specific secrets, but no discussion of how much detail the plaintiff actually provided in the trial court); Trandes Corp. v. Guy F. Atkinson Co., 996 F.2d 655, 662 (4th Cir. 1993) (refusing to overturn jury verdict despite plaintiff's failure to identify precise secrets, and affirming on questionable ground that entire object code software was secret without questioning whether any particular secrets were identified in such code); Static Control Components, Inc. v. Darkprint Imaging, Inc., 240 F. Supp. 2d 465, 476-77 (M.D.N.C. 2002) (on post-trial motion for judgment as a matter of law, court held that plaintiff's corporate deposition witness failed to identify alleged secrets, and identification was still an open issue about "one week before trial," but refusing to grant new trial because of general misconduct by both sides); Smithkline Beecham Pharms. Co. v. Merck & Co., 766 A.2d 442, 447-48 (Del. 2000) (affirming trial judgment for plaintiff despite defendant's argument that plaintiff had, early on, given only a broad identification, because a more precise identification was given "following discovery").

[72] *See* 3M Co. v. Pribyl, 259 F.3d 587, 595-96 (7th Cir. 2001) (refusing to overturn jury verdict; allowing judgment against defendant based on vague claims that secrets existed somewhere in 500 pages of documents; it is unclear if defendant ever raised identification issue before appeal); Forro Precision, Inc. v. IBM Corp., 673 F.2d 1045, 1057 (9th Cir. 1982) (in early case still cited by trade secret plaintiffs seeking to avoid identification, appellate court rejected identification argument in cursory language following trial court judgment and jury verdict in favor of plaintiff; court's reasoning was apparently that because defendant obtained materials in which plaintiff claimed secrets, identification of precise secrets was unnecessary); Forscan Corp. v. Dresser Indus., Inc., 789 S.W.2d 389, 391-92 (Tex. App. 1990) (rejecting defendant's post-trial argument that plaintiff went beyond alleged secrets previously identified in interrogatory response; defendant waited too long to object);.

the all-too-familiar "combination trade secret" evasion, essentially validating the plaintiff's non-identification.[73]

IV. PROPOSALS

¶72 Having reviewed the policy reasons why identification of alleged secrets is a crucial question, the mistakes courts all too often make when ruling on identification disputes, and the nationwide case law, we are in a position to offer guidelines and standards for ruling on identification disputes in trade secret litigation.

¶73 As a general proposition, we believe that courts should require trade secret plaintiffs to identify their alleged secrets in detail as early as possible in the litigation.[74] What follows are proposals tied to the stage of the litigation and the type of information claimed as secret, with general guidelines appropriate to all identification disputes. We also propose a model interrogatory requesting a precise identification of the plaintiff's trade secret claims.

A. General Guidelines

¶74 Some general considerations are appropriate for all identification disputes.

- Separating Identification From the Secrecy Analysis: As described above, courts should always treat the identification requirement as a separate, threshold question before reaching the distinct issue of whether the claimed information actually amounts to a trade secret. Identification is not so much a fact issue as a drafting issue.

- Non-Confidential Identification: Courts should be wary of plaintiffs' purported identifications that list only general, high-level categories or technical terms. One general rule might be that if the list of alleged secrets is not marked as a confidential document or could have been listed verbatim in the complaint without actually disclosing the plaintiff's alleged trade secrets, the list is prima facie insufficient. No plaintiff making a good faith identification would disclose its alleged secrets in a non-confidential document.[75]

- Incomplete Identification: Another basic consideration is that if an identification list expressly includes phrases suggesting that it is incomplete – such as "including," and "among other things" – it should likewise be prima facie insufficient. Some courts have

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[73] *See* Data Gen. Corp. v. Grumann Sys. Support Corp., 825 F. Supp. 340, 358-59 (D. Mass. 1993) (plaintiff gave testimony at trial about its alleged software secrets, but apparently did not actually define them with precision).

[74] To this end, courts should assist the parties by expediting review of protective orders that allow the plaintiff to identify the alleged secrets in a confidential manner, and by permitting identifications of trade secret claims to be filed under seal when it is necessary to refer to such information in a pleading before the court. These practices are routine in jurisdictions where trade secret litigation is common, but other courts are not as familiar with them.

[75] For a useful article providing advice for a plaintiff seeking to identify alleged secrets in good faith, see Victoria A. Cundiff, *How to Identify Your Trade Secrets in Litigation*, 574 PLI/Pat 557 (1999).

noted the problem of such "catch all" phrases when requiring more.[76]

- Avoid References to Voluminous Documents: Courts should not allow trade secret plaintiffs to point to documents in which trade secrets are said to reside as a substitute for a detailed identification. Documents such as design specifications may contain far more information that what is claimed as trade secrets, and reading a complex document may not inform the reader what precisely is being asserted as secret.[77] As an example, the Southern District of New York once recognized this problem by holding that a mere list of documents was an insufficient identification. The court required the plaintiff to identify all trade secrets claims, to list all documents referring to such claims, and "to key all documents or portions thereof to specific trade secrets and confidential information alleged to have been misappropriated" because "[a]t the very least, a defendant is entitled to know the bases for plaintiff's charges against it."[78]

- Requiring Identification of Combination Trade Secret Claims: We also believe that courts should require identification of alleged "combination trade secrets," and should not confuse the existence of such allegations with whether identification of particular combinations is necessary. We described above several rulings, mistaken in our view, where trade secret plaintiffs asserted "combination" secrets and avoided having to identify them. But many other courts have correctly held that trade secret plaintiffs must identify "combination trade secret" claims just as they must identify individual trade secret claims.[79] We believe that these decisions reflect

[76] *See* StonCor Group, Inc. v. Campton, No. C05-1225JlR, 2006 WL 314336, at *1-2 (W.D. Wash. Feb. 7, 2006) (granting motion to compel; plaintiff used phrase "among other things"); Systems Am., Inc. v. Softline, Inc., No. C96-20730 RMW PVT nl, 1996 U.S. Dist. LEXIS 22415, at *1 (N.D. Cal. Oct. 30, 1996) (finding plaintiff's Cal. Civ. Proc. § 2019.210 statement "insufficient" in part because it employed a "catch-all" phrase concerning "relevant business activities"); Struthers Scientific Int'l Corp. v. Gen. Foods Corp., 51 F.R.D. 149, 154 (D. Del. 1970) (where plaintiff's response to defendant's identification interrogatory included a "'catch-all' provision" claiming additional unspecified combination trade secrets, motion to compel more specific answer granted; "Struthers should be required to specifically describe what particular combination of components it has in mind, how these components are combined, and how they operate in a unique combination. This matter cannot be left to pure speculation and conjecture.").

[77] We have seen a case, for example, where the trade secret plaintiff attempted to identify its alleged trade secrets by pointing to over one thousand documents and more than forty million lines of source code. The case settled before any ruling on that tactic, but we believe that the practice is not uncommon.

[78] *See* Xerox Corp. v. IBM Corp., 64 F.R.D. 367, 371-72 (S.D.N.Y. 1974).

[79] *See* Staffbridge, Inc. v. Gary D. Nelson Assoc., Inc., No. 024912BLS, 2004 WL 1429935, at *4 (Mass. June 11, 2004) (where plaintiff failed to identify alleged secrets in software product "literally on the eve of trial," and where plaintiff's expert report seeking to make such identification was too vague and conclusory, plaintiff ordered to serve a affidavit "that sets forth with rigorous and focused particularity what, and only what, the plaintiffs claim to constitute the trade secrets allegedly misappropriated by either of the defendants" or face summary judgment); Compuware Corp. v. IBM, No. 02-CV-70906, 2003 WL

the better reasoning, and should be followed by other courts. One such ruling, an early 1958 decision by a federal court in Wisconsin, is worth quoting for the court's indignation at the plaintiff's refusal to identify its combination claims of one hundred unspecified modifications:

> Just specify the hundred different machines you claim, and diagram them. Let's find out what you claim was a trade secret that was improperly communicated to and used by the defendant. If there are a hundred, let's have a hundred, but let's have it specific so when this case comes on for trial, or if the defendant wants to take further discovery on those matters they will know what the issues are going to be and the court will know what the issues are going to be, and we won't come in here with a broad shotgun charge and be weeks putting in testimony on matters that could be handled in very short order. I think they are entitled to have that made very definite.[80]

- Keep the Identification Within the Scope of the Complaint: A final general consideration applicable at any stage of the case is that a plaintiff should not be permitted to allege trade secrets outside of the fact pattern pleaded in the complaint. While this may be rare, we have seen at least one case where a plaintiff alleged a customer list-type set of allegations in a complaint against its former salespeople, but then generally described hardware-based trade secrets in its California identification statement. In an unpublished ruling, the court granted the defendants' motion for an order limiting the scope of the trade secret claims after the defense raised the basic principle that the alleged secrets were beyond the claims and defenses at issue in the complaint.[81]

23212863, at *6-7 (E.D. Mich. Dec. 19, 2003) (rejecting motion for preliminary injunction where plaintiff claimed secrets in "unique combination of functions and capabilities" in certain software, "customer preferences," product documentation, and source code; court rejected claims, noting "As for its source code, Compuware has for whatever reason failed to identify any specific lines of source code that have been taken by IBM."); Jostens, Inc. v. Nat'l Computer Sys., Inc., 318 N.W.2d 691, 699-700 (Minn. 1982) (affirming summary judgment where court was "plagued with the elasticity of plaintiff's claim. Simply to assert a trade secret resides in some combination of other known data is not sufficient, as the combination itself must be delineated with some particularity in establishing its trade secret status."; rejecting plaintiff's various efforts at cobbling together an alleged combination trade secret); Struthers Scientific Int'l Corp. v. Gen. Foods Corp., 51 F.R.D. 149, 154 (D. Del. 1970) (where plaintiff's response to defendant's identification interrogatory included a "'catch-all' provision" claiming additional unspecified combination trade secrets, motion to compel more specific answer granted; "Struthers should be required to specifically describe what particular combination of components it has in mind, how these components are combined, and how they operate in a unique combination. This matter cannot be left to pure speculation and conjecture."); Package Mach. Co. v. Hayssen Mfg. Co., 164 F. Supp. 904, 907, 910 (E.D. Wis. 1958) (rejecting plaintiff's effort to avoid identifying alleged secrets by asserting "a hundred different modifications" of technology at issue; dismissing case for failure to identify on motion to compel compliance with pre-trial order).

[80] *See Package Mach. Co.*, 164 F. Supp. at 910.

[81] *See* Mentor Graphics Corp. v. Verplex Sys., Inc., No. 5:00-CV-20562, (N.D. Cal. Mar. 15, 2001) (order

B. Type of Information

¶75 Another important consideration is that the possibilities for identification differ according to the type of information being claimed as trade secrets. Some information can only be identified by naming it, such as customer contact information. With information in source code, however, there can be more than one plausible way to provide a precise identification.

- **Customer Lists and Business Information**: It should be clear that in cases involving simpler types of information such as customer lists, there are no choices other than defining exactly what the alleged secret is or merely listing generic categories. When a plaintiff claims trade secrets in customer list information, pricing or sales information, or business or marketing plans, it should be easy to tell the defendant exactly what the alleged secrets are – the plaintiff can simply name the supposedly secret customers, prices, ideas, and the like.[82]

- **Formulas, Measurements, and Mathematical Information**: As complex as chemical formulas, measurements, and math-based calculations can be, they too can be identified only by stating exactly what the item is: the numerical measurements or dimensions, the calculation expressed in mathematical terms, and so on. The same precise and detailed nature that can make this type of information secret also makes it easy to fully identify.

- **Software Code**: Identification of trade secret claims in software code can take many forms. For example, trade secrets could exist as (1) the functionality of compiled and executable object code; (2) source code implementing higher level algorithms that may or may not be secret; (3) information or formulas within source code; (4) algorithms or architecture; or (5) data structure items.[83] At the same time, software can contain non-secret information in those

granting defendants' motion for protective order).

[82] *See, e.g.*, Anderson, *supra* note 30, at § 11.23 (noting that with categories like customer lists, "there is no middle ground between identifying a customer and not making such an identification").

[83] One court has stated that "a computer program generally 'includes source code, which is the developer's tool in creating software, object code, and other technical information, including program architecture, design definitions or specifications, flow diagrams and flow charts, data structures, data compilations, formulae and algorithms embodied and used in the software.'" ECT Int'l, Inc. v. Zwerlein, 597 N.W.2d 479, 483 (Wis. Ct. App. 1999) (affirming summary judgment in part due to failure to identify trade secrets adequately) (quoting Robert C. Scheinfeld & Gary M. Butter, *Using Trade Secret Law to Protect Computer Software*, 17 RUTGERS COMPUTER & TECH. L.J. 381, 383 (1991) (footnotes omitted)). We find this characterization confusing. Source code is the human readable version of the instructions the computer will carry out. A computer program called a "compiler" transforms source code into executable object code that the computer may read directly. The "other technical information" referenced in the article could be characterized as either specific formulas embodied by and readable within a few lines of source code or overall high-level plans for what the program should accomplish and how it will accomplish it through certain algorithms and structure.

same categories, as well as auto-generated code, open source material, or basic code mandated by the programming language or type of program. Identification of each of these categories is thus worthy of independent consideration.

¶76 In the rare case where a trade secret plaintiff alleges that executable object code was misappropriated, the plaintiff should name the executable files, and identify what about their functionality is alleged to be secret.[84] Second, where the plaintiff alleges misappropriation of source code, it should identify the specific lines of code or programs claimed to be secret by, for example, printing out the code on paper with numbered lines and identifying the allegedly misappropriated lines by page and line number, by highlighting, or by color-coding.[85] Third, algorithms or formulas existing within code should be identified with exactitude just like mathematical information. Fourth, in the case of algorithms, the plaintiff should identify the precise combination of functions which comprise the algorithms at issue. Similarly, the higher-level architecture of the software should be identified by detailing the combination of the specific algorithms employed. Fifth, where secret data structures are alleged, the nature of those structures should be defined with particularity.[86]

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[84] Trade secret cases about executable software are rare because the final, executable software product is often the version sold to the public, while the underlying source code remains secret. Such a case could arise if, for example, the plaintiff maintains executable object code as a tool used secretly for internal purposes rather than selling it and then accuses the defendant of taking it. Identifying the functionality provided by object code seems necessary to establish that the object code has economic value and differs from other, publicly-available executable files. After all, object code is not source code, and misappropriating an object code file would not be misappropriation of the source code used to make that file. A plaintiff could not accurately identify alleged secrets in object code by describing the source code used to create it. Indeed, in a different trade secret litigation context – that of reasonable measures used to protect the alleged secret, rather than identification of the alleged secret – courts have consistently held that there is a valid distinction between object code and source code, and that revealing object code does not disclose alleged secrets in source code. *See generally* Fabkom, Inc. v. R.W. Smith & Assoc., Inc., No. 95 Civ. 4552 (MBM), 1996 WL 531873, at *7 (S.D.N.Y. Sept. 19, 1996) (same; software "distributed to its customers only in its executable object code form. . . . This means that any person attempted to reveal the programming instructions would see an incomprehensible sequence of numbers . . . ."); ISC-Bunker Ramo Corp. v. Altech, Inc., 765 F. Supp. 1310, 1323 (N.D. Ill. 1990) (plaintiff's "computer programs are only distributed in object code, which is not intelligible to human beings."); Q-Co Indus., Inc. v. Hoffman, 625 F. Supp. 608, 618 (S.D.N.Y. 1985) ("Only the object code is publicly available; this is the version of the program that is intended to be read by the computer and cannot be understood even by expert programmers.") (citing Glenn J. MacGrady, *Protection of Computer Software—an Update and Practical Synthesis*, 20 HOUS. L. REV. 1033, 1063 (1983) ("Secrecy will not be destroyed by the wide distribution of computer programs if they are distributed in object form only.")).Barr-Mullin, Inc. v. Browning, 424 S.E.2d 226, 229 (N.C. Ct. App. 1993) (plaintiff used reasonable measures to protect source code, and sold only object code software made from that source code to the public). Thus, identification of alleged secrets provided by object code differs from identifying trade secret claims in source code, and the two should not be confused.

[85] *See* Compuware Corp. v. IBM, No. 02-CV-70906, 2003 WL 23212863, at *6-7 (E.D. Mich. Dec. 19, 2003) (rejecting motion for preliminary injunction where plaintiff claimed secrets in "unique combination of functions and capabilities" in certain software, "customer preferences," product documentation, and source code; court denied preliminary injunction, noting: "As for its source code, Compuware has for whatever reason failed to identify any specific lines of source code that have been taken by IBM.").

[86] Databases can contain specific content and combinations of content in fields. A plaintiff may believe that such data constitutes trade secrets and, if so, that information should be identified.

- **Mechanical Devices**: Trade secrets might be embodied in mechanical devices that include secret parts unknown to the public or a secret combination of publicly known parts.[87] A plaintiff alleging trade secret claims about a secret part should identify that part in detail. If the plaintiff alleges that the trade secret is a combination of publicly known parts, the plaintiff should identify that combination, and the court should limit the plaintiff's ability to modify the alleged combination.[88]

- **Chemical Mixtures and Recipes**: Mixtures, whether for something as simple as some food product recipes or the combination of ingredients in a certain brand of gasoline, should be identified by the combination of publicly known elements – including the measurements or ratios for each ingredient.

- **Negative Information**: Negative information – sometimes called "what not to do" – can pose difficulties. One prominent commentator believes that because the total invention history of a combination-type trade secret can contain a body of negative knowledge in the sense of many steps not taken and choices not made, identifying that sum total should not be required.[89] We agree in part. It is unlikely that the defendant will be accused of actually taking and using that whole panoply of negative items, and thus there is no need to force the plaintiff to draft a complete invention history. However, where a plaintiff specifically accuses a defendant of taking and using one or more items of negative information, we see no policy reason not to require that those items also be defined in detail.

- **Destroyed Information**: Perhaps the hardest question involves an extreme scenario where a defendant physically destroys information that was valuable and secret, without leaving any copies behind. We know of no cases on this subject, and have never seen it in practice. A deserving plaintiff may have no ability to precisely identify what was destroyed, but a malicious plaintiff could claim purported value in information that never really existed, or that was of little actual value. This is an area where courts should have wide discretion to assess the facts of particular cases. For example, if it were impossible for plaintiff to identify the destroyed secret, a court could require identification of the circumstances of the

[87] In the case of computer hardware, "parts" could include source code – either firmware or software – integrated with physical hardware.
[88] *See infra* Section III(E).
[89] *See* POOLEY, *supra* note 4, at § 11.02 ("[T]he nature of a secret process, with its underlying platform of accumulated negative data, is such that it cannot practically be restated in exhaustive detail.").

alleged creation, destruction, and plaintiff's ownership in the information.

C. *Stage of the Case*

¶77 As discussed above, a court's handling of the identification dispute differs depending on the stage of the case. We believe that the pleading stage is not the time to consider identification questions, except in cases where the complaint fails the ordinary rules for indefinite statements.[90]

¶78 However, we believe that when a trade secret plaintiff requests preliminary injunctive relief that could seriously impact the defendant – by shutting its business, limiting a person's employment options, scaring away investors and customers, and the like – courts should require an identification of the alleged trade secrets at issue with a substantial degree of detail. There might be exceptions for highly unusual circumstances – where, hypothetically, there is concrete evidence that the defendant is planning an imminent foreign transfer of an immense amount of stolen software code, and there is no time to provide all the details. Courts are capable of separating such extreme facts from routine motions against departing employees who have just started a new company.

¶79 Most important, we believe that courts in jurisdictions that have not yet enacted a pre-discovery identification requirement for trade secret cases should do so, both as a valuable case management process and to encourage pre-lawsuit investigations. In addition to the trade secret pre-discovery cases described above, the approach several federal courts have taken in patent cases provides a useful analogy. Federal district courts in California, Georgia, Pennsylvania, and Texas have enacted special local rules for patent cases that require a more specific identification of the patent claims than already exist in the published patent. Specifically, these districts require patentees to explain with precision at a very early stage exactly what patent claims are being asserted and why the allegedly infringing product or process satisfies each element of the asserted patent claims.[91] As one court explained, the patent local rules were adopted to "place the parties on an orderly pretrial track," "require the plaintiff to carefully prepare for the filing of a patent suit," and "require parties to crystallize their theories of the case early in the litigation and to adhere to these theories once they have been disclosed."[92]

¶80 The benefit of identification in the trade secret context is even greater. In a patent case, the court and the defendant have notice of the patent's claims and have a description of the invention from the published patent itself. The local rules described above go a step further by removing any mystery about what particular claims the plaintiff will assert and how the plaintiff intends to argue that those claims cover an accused product or process. In a trade secret case, and absent an identification requirement, the court and the defendant cannot know how the plaintiff will allege that trade secrets were misappropriated, and, even worse, cannot know what the trade secret claims are. The need for identification in trade secret cases is thus more critical than in

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[90] *See, e.g.*, CAL. CIV. PROC. CODE § 430.10(f) (permitting a demurrer to an "ambiguous and unintelligible" pleading); FED. R. CIV. P. 12(e) (permitting a motion for a more definite statement).

[91] *See* N.D. Cal. Patent. L.R. 3-1; N.D. Ga. Patent L.R. 4.1; W.D. Penn. LPR. 3.2; E.D. Tex. P.R. 3-1.

[92] *See* Integrated Circuit Sys., Inc. v. Realtek Semiconductor Co., 308 F. Supp. 2d 1106, 1107 (N.D. Cal. 2004).

patent cases. Enacting local rules akin to these patent-based rules would be a worthy goal for trade secret law. In any event, courts can require pre-discovery identification by common law for case management purposes.

¶81 Finally, detailed identification should always be required by the summary judgment stage, assuming that discovery has taken place. But where a defendant fails to raise the identification issue until after trial, it is understandable why so many courts have refused to reverse on that basis.

D. Defendant's Discovery Request

¶82 As discussed above, the defense sometimes compounds the identification problem by serving badly-phrased discovery requests or, more importantly, failing to timely raise the issue. By failing to ask for a totally precise identification, a defendant can allow the plaintiff to get by with generic concepts and categories, and alter its claims without judicial review.

¶83 In one case, for example, the defendant's interrogatory apparently requested only that plaintiff *describe* the alleged secrets and documents in which they were contained. When the plaintiff responded with a generalized statement pointing to 17 pages and describing a "manufacturing process" "including" seven general concepts, the defendant moved to compel. But the court found the generalized identification sufficient.[93] Perhaps if the defendant had served a better-worded interrogatory demanding precision, the result would have been different.

¶84 Likewise, a defendant in a California case made a mistake when it tied its identification interrogatory to California's *pre-discovery* statute – which does not require absolute precision – instead of asking for complete precision.[94] Yet another defendant asked only for the identification of documents in which the plaintiff's alleged secrets were to be found, instead of asking for a precise identification of the claims themselves.[95] It therefore failed to seek the maximum degree of detail it could have requested. Similarly, a failure to press for complete identification in deposition questioning can allow the plaintiff latitude to alter its claims afterwards.[96]

¶85 We believe that a well-worded interrogatory or other discovery request should demand a totally precise, complete identification of each alleged trade secret. A model interrogatory with an accompanying definition is as follows:

[93] *See* Norbrook Labs., Ltd. v. G.C. Hanford Mfg. Co., No. 5:03CV165(HGH/GLS), 2003 WL 1956214, at *2-4 (N.D.N.Y. Apr. 24, 2003).

[94] *See* Synapsis, L.L.C v. Evergreen Data Sys., Inc., No. C 05-1524 JF, 2006 WL 2053512, at *2 (N.D. Cal. July 21, 2006) (granting motion to compel where plaintiff refused to respond).

[95] *See* Multimedia Cablevision, Inc. v. Cal. Sec. Co-op, Inc., No. 94-1130-MLB, 1996 WL 447815, at *1-2 (D. Kan. July 30, 1996) (Defendant's interrogatory which only asked plaintiff to identify the *documents* which comprised the basis for the trade secret claim; nonetheless, court granted motion to compel a better answer regarding the documents in question and issued sanctions against plaintiff.).

[96] *See* Cacique, Inc. v. V&V Supremo Foods, Inc., No. 03 C 4230, 2004 WL 2222270, at *5 (N.D. Ill. Sept. 30, 2004) (denying motion to strike portions of declaration submitted by plaintiff in opposition to motion for summary judgment; although defendant argued that declaration added additional trade secret claims not previously identified, court noted that defendant failed to "ask any follow-up questions" at deposition regarding area in which alleged secrets were claimed).

¶86 Identify with precision and specificity each and every alleged trade secret [Plaintiff] contends [Defendant] misappropriated. "Identify with precision and specificity each and every alleged trade secret" as used herein means to provide a specific description of each such alleged trade secret, on an individual basis for each such alleged trade secret, in such a manner that the exact identity, scope, boundaries, constitutive elements, and content of each such alleged trade secret are fully disclosed in writing, including any asserted combinations, [and with precision above that required by California Code of Civil Procedure section 2019.210]. Plaintiff should not rely on any vague or conclusory phrases that do not separately list and describe each such alleged trade secret.

¶87 This model request requires a totally precise identification of each alleged secret, without dissembling or deliberate obfuscation. It alerts the reader to typical evasion practices, and thus educates a court ruling on a motion to compel about what exactly is sought and what is insufficient. The request also makes clear that more is sought than what some jurisdictions require at the pre-discovery stage – California law in this model – though of course the request can be adapted to different jurisdictions.

E. Amendment

¶88 The question sometimes arises whether a trade secret plaintiff can unilaterally amend its identification of trade secret claims as the case proceeds. One can envision circumstances where amendment would be proper, such as where a plaintiff learns that a defendant has misappropriated trade secrets beyond those first believed to be at issue. But one can also envision circumstances where the plaintiff drops one set of meritless claims in order to pursue another, alters claims to avoid summary judgment or to add in new claims just before trial, or changes definitions of existing claims to confound the defendant's ability to research the public domain.

¶89 A 2004 federal court case applying California law created a rule that we believe makes sense and should be widely adopted. The court held that because a statement identifying the plaintiff's alleged trade secrets is akin to a pleading, the plaintiff would have to show good cause to amend the statement, just as it would have to do in order to amend its complaint.[97] Subjecting amendments and alterations to judicial review would help prevent the problems we have experienced in many cases where the alleged secrets change repeatedly as the case proceeds, often as the close of discovery nears.

¶90 Another good practice is to prevent the plaintiff from amending its identification of alleged secrets in order to avoid a defendant's pending summary judgment motion.[98] The same practice should apply if the plaintiff claims a "combination

[97] *See* Neothermia Corp. v. Rubicor Med., Inc., 345 F. Supp. 2d 1042, 1045 (N.D. Cal. 2004). This rule is intended to prevent the "shifting sands" problem in intellectual property cases where a plaintiff changes its claims around as the case proceeds. *See id.* (noting the problem to be "a concern which applies with equal force to trade secret allegations."). *See also* Vacco Indus., Inc. v. Van Den Berg, 5 Cal. App. 4th 34, 51 n.16 (Cal. Ct. App. 1992) (prior case under California law finding "no error" in fact that plaintiff amended statement identification statement "several times," but providing no information as to whether trial court oversaw such amendments).

[98] *See* Pixion, Inc. v. Placeware, Inc., 421 F. Supp. 2d 1233, 1242 (N.D. Cal. 2005) (although court's incorrect view of what level of specificity is required under Cal. Civ. Proc. § 2019.210 is clear under the subsequent California state court ruling in *Advanced Modular Sputtering*, *supra* note 40, court refused to allow plaintiff to avoid summary judgment motion by going beyond identification previously stated to be

trade secret" and tries to alter its sub-elements in the face of a summary judgment motion.[99] While this might be inappropriate where discovery has only just begun and the motion is filed too early, we believe that courts would promote and invite litigation abuses if they allowed trade secret plaintiffs to alter the claims and escape a motion for summary judgment filed after significant discovery has taken place.

¶91 In turn, some courts have refused to allow amendment and addition of new trade secret claims after discovery closes, and that too should be a universal rule.[100]

F. Sanctions

¶92 Courts have issued sanctions in several trade secret cases where plaintiffs failed to identify their alleged secrets despite defense efforts to obtain more information.[101] Others have declined to award sanctions even where the failure to identify (among other problems) was manifest.[102] Rule 11 and similar state rules already

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complete by claiming new details of functionality as trade secrets; court instead ruled on claims as previously asserted in identification statement).

[99] *See* Am. Airlines, Inc. v. KLM Royal Dutch Airlines, Inc., 114 F.3d 108 (8th Cir. 1997). In *American Airlines*, the Eighth Circuit affirmed the district court's summary judgment ruling against the trade secret plaintiff, American Airlines. The plaintiff's expert testified that its combination trade secret consisted of five elements and implementation algorithms. *Id.* at 110. After discovering that the defendant had not acquired all five elements, the plaintiff attempted, through expert testimony, to claim that the other four elements constituted a valid combination trade secret. *Id.* The court, rejected this "sham" definition of the combination trade secret and upheld the district court's summary judgment based on the original definition of the combination trade secret that included all five elements of the plaintiff's system. *Id.* at 111-12. The court concluded "After careful examination of American's expert's testimony we agree with the district court's conclusion that American attempted to manufacture a material issue of fact just to evade the impact of summary judgment by inexplicably changing its testimony. Thus, the district court correctly disregarded the subsequent manufactured contradictory testimony of American and concluded that no factual issue for trial existed for the reason that KLM never received any trade secret of American's.").

[100] *See* Hickory Specialties, Inc. v. Forest Flavors Int'l, Inc., 12 F. Supp. 2d 760, 770 (M.D. Tenn. 1998) (prohibiting plaintiff from submitting 36 new trade secret claims after discovery closed; prior interrogatory response had identified 31 *other* alleged secrets); Rockwell Graphic Sys., Inc. v. Dev Indus., Inc., No. 84 C 6740, 1992 WL 162241, at *3-5 (N.D. Ill. July 12, 1992) (excluding allegedly secret drawings raised after discovery closed).

[101] *See* Compuware Corp. v. Health Care Serv. Corp., No. 01 C 0873, 2002 WL 485710, at *7 (N.D. Ill. Apr. 1, 2002) (the court issued sanctions where defendant won motion to compel regarding interrogatory requesting identification of alleged secrets but plaintiff "dragged its feet" in responding and merely listed functions of allegedly secret software); Computer Econ., Inc. v. Gartner Group, Inc., No. 98-CV-0312 TW (CGA), 1999 WL 33178020, at *6 (S.D. Cal. Dec. 14, 1999) (awarding defendant attorneys' fees for many reasons, including plaintiff's claims of "trade secret protection over several vague classes of unprotectable information"); Multimedia Cablevision, Inc. v. Cal. Sec. Co-op, Inc., No. 94-1130-MLB, 1996 WL 447815, at *1-2 (D. Kan. July 30, 1996) (sanctions issued against plaintiff where defendant's motion to compel better interrogatory answer on documents containing alleged secrets granted); Diversified Tech., Inc. v. Dubin, 156 F.R.D. 132 (S.D. Miss. 1994) (depublished) (issue preclusion sanctions for plaintiff's repeated refusal to identify alleged secrets; "With trial of this matter set for less than a week from today, the prejudice to defendants is immeasurable."); Automated Packaging Sys., Inc. v. Sharp Packaging, Inc., No. 88-C-0656, 1989 WL 223755, at *3 (E.D. Wis. Mar. 17, 1989) (fees awarded for meritless request for preliminary injunction where "[t]he plaintiff's case fails because of its inability to establish any sort of identifiable trade secret which could lend itself to an injunctive proceeding."); Cromaglass Corp. v. Ferm, 344 F. Supp. 924, 927 (M.D. Penn. 1972) (awarding discovery sanctions where defendant moved to compel over inadequate interrogatory responses on identification of alleged secrets).

[102] *See* Clearwater Sys. Corp. v. Evapco, Inc., No. Civ.A 305CV507SRU, 2006 WL 726684, at *2 (D. Conn. Mar. 20, 2006) (refusing to award UTSA attorneys' fees despite baseless lawsuit; "Clearwater's ineffective identification of the trade secrets pursued in this case left much to be desired and doubtless

require that a plaintiff understand precisely the alleged secrets that it accuses the defendant of misappropriating, and there is no reason the plaintiff should be unable to share this understanding – essential to the plaintiff's core case—with the defendant. Because non-identification is a lawyers' tactic used to gain an unfair litigation advantage, we believe that sanctions should be readily awarded where a trade secret plaintiff tries to supply as little information as possible and hopes that the court will not require more.

V. CONCLUSION

¶93 Disputes regarding identification of alleged trade secrets are common in trade secret litigation around the country. Courts thus far have not articulated a uniform set of standards and guidelines to address the problem. But such rules are needed, because trade secret plaintiffs generally refuse to precisely identify their trade secret claims unless the court forces them to do so. Our proposals would ensure that the many policy grounds supporting a precise identification of alleged secrets would be satisfied in any given case.

increased EVAPCO's costs in defending the litigation. Still, I am not convinced that Clearwater's problems with trade secret identification reflect a calculated strategy to gain an advantage in the litigation or to unfairly compete with EVAPCO.").

EXHIBIT D

C Only the Westlaw citation is currently available.

NOTE: UNPUBLISHED OPINION, SEE RCWA 2.06.040

Court of Appeals of Washington,
Division 1.
FLUKE CORPORATION, a Washington corporation, Danaher Corporation, a Delaware corporation, Respondents,
v.
MILWAUKEE ELECTRIC TOOL CORPORATION, a Delaware corporation, Jon Morrow, an individual, Petitioners,
Evans Nguyen, an individual, Defendant.
No. 61928-4-I.

Feb. 17, 2009.

West KeySummary
Contracts 95 202(2)

95 Contracts
95II Construction and Operation
95II(C) Subject-Matter
95k202 Trade and Business
95k202(2) k. Restriction of Competition. Most Cited Cases
A parent corporation and subsidiary had no legal rights in an employee's non-competition agreement that was formed with a different subsidiary of the corporation. The non-competition agreement named only the subsidiary corporation in the agreement and did not reference the parent corporation. The non-competition agreement ended 12 months after the employee was transferred to the parent corporation and it was not assigned as the parent never replaced the subsidiary in the original agreement and a new non-competition agreement was never formed.

Appeal from King County Superior Court; Hon. Michael J. Trickey, J.
Bradley S. Keller, Attorney at Law, Keith David Petrak, Byrnes & Keller LLP, Steven Walter Fogg, Michael A. Moore, Corr Cronin Michelson Baumgardner & Pree, Seattle, WA, for Petitioners.
Kevin J. Hamilton, James Sanders, Brian Matthew Flock, Perkins Coie LLP, Seattle, WA, for Respondents.

LEACH, J.

*1 Jonathan Morrow and the Milwaukee Electric Tool Corporation challenge a preliminary injunction that prohibits Morrow from working for Milwaukee Electric Tool Company in the Test and Measurement field. The Fluke Corporation and its parent, the Danaher Corporation, sought and were granted a preliminary injunction to prevent harm from Morrow's alleged breach of a noncompetition agreement (the Agreement). Because Fluke and Danaher have no clear legal or equitable right under the Agreement, we reverse.[FN1]

FN1. Respondents Fluke and Danaher also filed an "Objection to Petitioners' Notice of Filing Deposition Testimony and Documents Submitted to Trial Court But Omitted From Court Docket" on December 29, 2008, which we considered as a motion to strike. It is undisputed that these materials were presented to the trial court for its consideration. We therefore deny the motion.

Background

In 2002 Jon Morrow began working for the Jacobs Chuck Manufacturing Company, a subsidiary of the Danaher Corporation. Jacobs Chuck manufactures and markets parts for electric drills. In June of 2004, Morrow signed a noncompetition agreement. The Agreement provides in pertinent part:

DANAHER

NONCOMPETITION AGREEMENT

Danaher Corporation, an "at will" employer, believes that recruiting and retaining the very best people to work in its highly competitive businesses means treating them fairly, rewarding their contributions, and thereby establishing a strong partnership for our collective well-being and continued success. Employment at Danaher and its divisions *typically provides associates with specialized and unique knowledge and confidential information, which, if used in competition with Danaher, would cause harm to Danaher As such, it is reasonable to expect a commitment from our associates that protects Danaher's interests and therefore their own interests....*

The Jacobs Chuck Manufacturing Company, Clemson, SC, a division of Danaher Corporation, ("the Company") and Jonathan Morrow ... ("the Associate") agree as follows:

...

2. *Noncompetition and nonsolicitation.*

...

(b) For a 12-month period following the termination of the Associate's employment with the Company, whether the termination is voluntary or involuntary, the Associate will not, directly or indirectly, on behalf of himself or herself or for any entity, business or person other than, the Company, Danaher or any other subsidiary of Danaher:

(A) compete with the Company (for purposes of this Section 2(b)(A), the term "Company" shall be deemed to include, in addition to the Company, all affiliates of the Company with whom the Associate was employed at any time during the 12 month period preceding termination of the Associate's employment with the Company) in North America, Asia, Europe (the "Restricted Area"), or

(i) accept employment ... with a business, entity ... or person that competes directly or indirectly with any product or service of the Company within the Restricted Area,

(ii) provide any services similar to the services the Associate provided to or on behalf of the Company, or any other advice or consulting services, to a business, entity ... or person that competes directly or indirectly with any product or service of the Company within the Restricted Area....

***2** ...

The businesses, entities and persons referred to in this Section 2(b)(A) shall include, without limitation, those business, entities and persons referred to on Exhibit A attached hereto.

...

3. *Nonpiracy.* During the Associate's employment and for a 12-month period following the termination of the Associate's employment with the Company, whether the termination is voluntary or involuntary, the Associate will not directly or indirectly, on behalf of himself or herself, or for any other entity, business, or person:

(1) hire, entice, induce, solicit or attempt to hire, entice, induce or solicit any employee of the Company to leave the Company's employ (or the employ of Danaher or another subsidiary of Danaher, as applicable) or cause any employee of the Company to become employed in any business that is directly or indirectly competitive with the Company for any reason whatsoever.

A list of Jacobs Chuck's competitors is attached to the Agreement as Exhibit A. The Agreement permits "the Company" to "assign any and all of its rights and/or duties herein to Danaher and/or any other subsidiary or subsidiaries." The Agreement provides that South Carolina law controls its interpretation and construction.

On November 1, 2004, Morrow transferred to a marketing manager position at the Fluke Corporation, another Danaher subsidiary. In October of 2006, Morrow became Business Unit Manager for Amprobe, a division of Fluke that manufactures testing and measurement devices. He did not enter into a new noncompetition agreement with Fluke.

On February 19, 2008, Morrow resigned from Fluke and joined Milwaukee Electric Tool Company's new Test and Measurement business. There, Morrow worked on products designed to compete with Fluke's products. He has also encouraged at least one other Fluke employee to join him at Milwaukee Electric Tool.

On March 10, 2008, Fluke and Danaher filed suit, alleging that Morrow breached the Agreement, misappropriated trade secrets, and breached his fiduciary duties. Plaintiffs also obtained a temporary restraining order prohibiting Morrow from working in the same area at Milwaukee Electric Tool as he worked at Fluke and from using Fluke's confidential information or trade secrets.

On June 3, 2008, after having heard several days of testimony, the superior court granted Fluke's motion for preliminary injunction. The court found that the noncompete provision in the Agreement was enforceable and prohibited Morrow from working for Milwaukee Electric Tool's Test and Measurement Group.[FN2] The court entered written findings of fact and conclusions of law, and issued the following order:

> FN2. The court found one provision of the Agreement, Paragraph 2(b)(A)(i), which barred Morrow from accepting employment with a business that competed directly or indirectly with any product or service of the "Company," was overbroad and unenforceable.

1. Plaintiffs' Motion for Preliminary Injunction is GRANTED, and Defendant Morrow is HEREBY ENJOINED from:

(a) Working in any capacity for or with MET's Test and Measurement Group.

(b) Providing any services similar to the services Mr. Morrow provided to or on behalf of Fluke, or providing any other advice or consulting services, to MET's T & M Group or any company directly or indirectly competing with any products or services of Fluke within North America, Asia and Europe.

***3** (c) Directly or indirectly soliciting, assisting or encouraging others to solicit, or suggesting or recommending in any manner that MET or its personnel hire or solicit any current Fluke employee to leave Fluke's employ.

(d) Directly or indirectly, using, disclosing or publishing, or knowingly negligently permitting others not so authorized to use, disclose, or publish Fluke's confidential and proprietary information.

The order remains in full force and effect until February 19, 2009.

Morrow and Milwaukee Electric Tool Corporation petitioned this court for discretionary review of the trial court's order granting the preliminary injunction and the findings of fact and conclusions of law entered in conjunction with that order. Discretionary review was granted on August 18, 2008.

Standard of Review

A trial court's decision to grant injunctive relief is reviewed for an abuse of discretion.[FN3] A trial court abuses its discretion if the decision is based on untenable grounds or if the decision is manifestly unreasonable or arbitrary.[FN4] A party seeking injunctive relief must show (1) a clear legal or equitable right, (2) a well-grounded fear of immediate invasion of that right, and (3) actual or substantial harm to the party has resulted from or will result from the acts complained of.[FN5] The moving party must show that it is likely to prevail on the merits, and a court will not issue an injunction in a doubtful case.[FN6] However, where a purely legal issue is involved, the court must necessarily reach the merits of the purely legal issue in order to decide whether to grant or deny the preliminary injunction. [FN7] The interpretation of an unambiguous contract is an issue of law we review de novo.[FN8]

> FN3. *Kucera v. Dep't of Transp.,* 140 Wash.2d 200, 209, 995 P.2d 63 (2000).
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> FN4. *Kucera,* 140 Wash.2d at 209, 995 P.2d 63.
>
> FN5. *Kucera,* 140 Wash.2d at 209, 995 P.2d 63.
>
> FN6. *Rabon v. City of Seattle,* 135 Wash.2d 278, 285-86, 957 P.2d 621 (1998).
>
> FN7. *Rabon,* 135 Wash.2d at 286, 957 P.2d 621.
>
> FN8. *Quality Food Centers v. Mary Jewell T, LLC.,* 134 Wash.App. 814, 817, 142 P.3d 206 (2006).

Discussion

The Agreement provides that it will be governed by the laws of South Carolina. Under South Carolina law, the interpretation of an unambiguous contract is an issue of law.[FN9] A contract is ambiguous only when its terms are reasonably susceptible to more than one interpretation, and ambiguity is determined as a matter of law.[FN10] Here, neither party claims that the Agreement is ambiguous.

FN9. *South Carolina Dep't of Transp. v. M & T Enterprises of Mt. Pleasant,* 379 S.C. 645, 655, 667 S.E.2d 7 (Ct.App.2008).

FN10. *S. Atl. Fin. Servs., Inc. v. Middleton,* 349 S.C. 77, 81, 562 S.E.2d 482, 484 (Ct.App.2002).

The terms of an unambiguous contract are determined by the plain language of the contract, and "a court must construe its provisions according to the terms the parties used; understood in their plain, ordinary, and popular sense." [FN11] Only where a contract is ambiguous will extrinsic evidence be admitted to show the intent of the parties.[FN12] Furthermore, covenants not to compete are critically examined and construed against the employer. [FN13]

FN11. *Schulmeyer v. State Farm Fire & Cas. Co.,* 353 S.C. 491, 495, 579 S.E.2d 132 (2003).

FN12. *Ecclesi astes Prod. Ministries v. Outparcel Assoc.,* LLC, 374 S.C. 483, 500, 649 S.E.2d 494 (Ct.App.2007).

FN13. *Poole v. Incentives Unlimited, Inc.,* 345 S.C. 378, 381, 548 S.E.2d 207 (2001).

The superior court based its decision on the express terms of the Agreement. In its written decision, the trial court concluded that, "[b]y its express terms, and viewing the Agreement as a whole, Mr. Morrow's obligations under the Agreement contemplated movement between Danaher subsidiaries and the rights and obligations of the Agreement transferred from Jacobs Chuck to Fluke along with Mr. Morrow's employment." In its oral ruling, the trial court stated that while the evidentiary hearing was helpful for background, "[i]n the end it seems to me to come down to essentially a legal analysis of Exhibit 38, which is the non-competition agreement signed on June 17, 2004 by Mr. Morrow." The trial court also stated that the Agreement "is not ambiguous. It is quite clear." We agree that the Agreement is unambiguous. However, we disagree with the court's interpretation of the Agreement.

*4 When Morrow's counsel asked the court how it concluded that the noncompetition provision's reference to "the Company" included Fluke, the court responded: "I struggled with that. I concluded in the agreement as a whole, reading it, that quite clearly that the intent was to apply when somebody moved from [one] Danaher subsidiary to another." In its findings of facts, the trial court stated: "The rights and obligations of the Agreement transferred from Jacobs Chuck to Fluke along with Mr. Morrow's employment." Although the trial court erroneously described this determination as a finding of fact, it is a conclusion of law because it requires interpretation of the Agreement, and it is therefore subject to this court's review.[FN14]

FN14. *Woodruff v. McClellan,* 95 Wash.2d 394, 396-97, 622 P.2d 1268 (1980).

A careful reading of plain language of the Agreement reveals that the meaning of "the Company" does not include Fluke. Furthermore, although the Agreement contemplates the possibility that an employee transfer to another Danaher subsidiary, it does not provide that the Agreement is assigned automatically to the new employer upon the employee's transfer.

The Agreement expressly defines the term "Company" as "[t]he Jacobs Chuck Manufacturing Company, Clemson, SC, a division of Danaher Corporation, ("the Company")...." When the parties intended provisions of the Agreement to apply to more entities than just Jacobs Chuck, they so stated. For example, the Agreement is replete with references to "the Company, Danaher, or any other subsidiary of Danaher." Additionally, in section 2(b)(A), the Agreement expressly broadens the term "Company" to include "all affiliates of the Company with whom the Associate was employed at any time during the 12 month period preceding termination of the Associate's employment with the Company." But this broadened definition is expressly limited to section 2(b)(A), which describes entities with whom competition is prohibited. However, in the remainder of section 2, which addresses noncompetition and nonsolicitation, the Agreement's definition of "Company" is not modified and means only Jacobs Chuck.

The noncompetition and nonsolicitation provisions apply "[f]or a 12-month period following the termination of the Associate's employment with the Company." Therefore, because Morrow's employment with Jacobs Chuck terminated in 2004, the prohibitions in the agreement expired 12 months later, in 2005.

Fluke argues that Morrow's transfer did not constitute a "termination" under the agreement for purposes of the noncompetition and nonsolicitation provisions. While a transfer between subsidiaries of a parent corporation is not a termination per se, Morrow's transfer was a termination for purposes of the noncompetition provisions of this contract.

The Agreement states that "a transfer to Danaher or another subsidiary of Danaher shall in no event constitute a 'termination' of any kind for purposes of Sections 6 or 7 hereof." The Agreement's limitation of the application of this qualified definition of a termination to only two sections of the Agreement means that for purposes of the remaining sections of the Agreement this transfer constitutes a termination. If the parties had intended this definition to apply to all sections of the Agreement, it makes no sense for them to have expressly limited its application as they did. Thus, Morrow's transfer to Fluke was a termination for purposes of the noncompetition provisions of the Agreement contained in Section 2.

*5 In addition to contemplating the possibility of an Associate's transfer to another Danaher subsidiary, the Agreement also contemplates the possibility of an assignment of the Agreement. However, the Agreement does not provide for automatic assignment of the Agreement to the subsidiary in the case of a transfer. Rather, the Agreement provides that it will remain in effect unless the Company, Jacobs Chuck, terminates the Agreement and the Associate is offered a new agreement in connection with a promotion or transfer. Here, Morrow was not offered a new agreement, and so the Agreement remained in effect. However, by its plain terms, it remains in effect only as to "the Company," which is Jacobs Chuck, and expired 12 months after Morrow's termination from Jacobs Chuck.

Apparently recognizing that no actual assignment of the Agreement took place, Fluke argues that the Agreement was "equitably assigned" to it. Although Fluke argued this position to the trial court, it made no finding of an equitable assignment. "The absence of a finding of fact in favor of the party with the burden of proof about a disputed issue is the equivalent of a finding against that party on that issue." [FN15] Fluke did not seek review of the trial court's decision and has not assigned error to its failure to find an equitable assignment. Additionally, this argument fails because there is insufficient evidence of an equitable assignment

FN15. *Wallace Real Estate Inv., Inc. v. Groves*, 72 Wash.App. 759, 773, n. 9, 868 P.2d 149 (1994), *aff'd*, 124 Wash.2d 881, 881 P.2d 1010 (1994).

"An equitable assignment is such an assignment as gives the assignee a title which, though not cognizable at law, will be recognized and protected in equity." [FN16] The concept of equitable assignment has been rarely discussed in South Carolina appellate decisions over the past 50 years. The doctrine of equitable assignment is typically used to enforce an attempted assignment of rights that is technically defective.[FN17] Evidence of an equitable assignment must be clear and specific; it is implied from the conduct of the parties rather than established by express words of formal assignment. [FN18] A court may find an equitable assignment where necessary to effectuate the parties' plain intent or to avoid injustice.[FN19]

FN16. *Player v. Player*, 240 S.C. 274, 125 S.E.2d 636, 638 (1962).

FN17. *Recorded Picture Co. v. Nelson Entm't, Inc.*, 53 Cal.App.4th 350, 368, 61 Cal.Rptr.2d 742 (Ct.App.1997).

FN18. *Recorded Picture Co.*, 53 Cal.App.4th at 368, 61 Cal.Rptr.2d 742.

FN19. *SourceTrack, LLC v. Ariba, Inc.*, 32 Fla. L. Weekly D1419, 958 So.2d 523, 526 (Dist.Ct.App.2007).

Fluke argues that the Agreement was equitably assigned and the evidence of equitable assignment is the fact that Jacobs Chuck sent Fluke Morrow's personnel file, which included the Agreement. However, the fact that Jacobs Chuck physically sent Morrow's entire file, which happened to contain the Agreement, does not constitute clear and specific evidence of an equitable assignment. The Agreement was never moved to Morrow's Fluke personnel file with Morrow's Fluke documents, but remained in a separate folder with the rest of the Jacobs Chuck file.

Fluke also points to the fact that Morrow represented himself as a Danaher employee on his resume,[FN20] to prove that "he believed the Agreement had been transferred and remained in effect." However, Morrow's representation of himself as a Danaher employee, rather than simply an employee of Fluke or Jacobs Chuck, does not show that Jacobs Chuck assigned the Agreement to Fluke.

FN20. Morrow's resume stated:

DANAHER CORPORATION

National Sales Manager, Jacobs Chuck Manufacturing

***6** In conclusion, the Agreement provided for a 12-month period of noncompetition and nonsolicitation following Morrow's termination from Jacobs Chuck. The 12-month period began upon Morrow's termination from Jacobs Chuck and expired long before Milwaukee Electric Tool Company employed Morrow. Fluke has no legal rights under the Agreement.

We reverse.

WE CONCUR: DWYER, A.C.J. and SCHINDLER, C.J.
Wash.App. Div. 1,2009.
Fluke Corp. v. Milwaukee Electric Tool Corp.
Not Reported in P.3d, 148 Wash.App. 1041, 2009 WL 376801 (Wash.App. Div. 1)

END OF DOCUMENT

EXHIBIT E

1. ~~Information regarding Fluke's near and long term future business plans, such as the information fount in~~ Portions of Fluke's 2008 Strategic Plan, ~~both the final and earlier drafts~~ specifically the portion addressing Fluke's value brands, including Amprobe, *e.g.,* Fluke ~~006679-6767, 006965-7016;~~ 6721-6726 and 7017-7025; and the portion identifying the "white space" market, specifically Fluke 6707-6719 and 6999-7008;

2. ~~and the information found in t~~The Amprobe Policy Deployment Plan, Fluke 5512-13;

~~2~~3. ~~Information regarding Fluke's recent sales performance, such as the information found in~~ Fluke's daily FY 2008 Bookings Performance Reports, *e.g.,* Fluke 5775-76;

4. ~~and the information found in~~ Fluke's IG New Product Vitality Reports, *e.g.,* Fluke 4694;

~~3~~5. ~~Market and competitive product information compiled by Fluke, such as the information contained in t~~The Cross Market Analysis prepared by Mr. Morrow, Fluke 7107-7166 (and in native format);

6. ~~and in t~~The Competitive Landscape Report, Fluke 4547-4620 (and in native format).

~~4~~7. ~~Information about actual and prospective new products and new product ideas, such as the information contained in t~~The Updated New Product Initiative Spreadsheet, Fluke 4421-4484 (and in native format);

8. ~~the information contained in t~~The Amprobe Engineering 2008 Projects document; Fluke 5729-32;

9. ~~the information contained in t~~The Asia New Products 2007 Report, Fluke 7527-29 (and in native format);

10. ~~and the~~ Nonpublic information relating to the relative strengths and weaknesses of the Ultrasonic Distance Meter developed by Mr. Morrow during his employment with Fluke; and

~~5~~11. Voice of the Customer information gathered by Mr. Morrow in December 2007 and analyzed in the Amprobe Rep Performance Market Research Report; Fluke 4710-17.

No. 64408-4

IN THE COURT OF APPEALS
OF THE STATE OF WASHINGTON, DIVISION I

FLUKE CORPORATION and DANAHER CORPORATION,
Appellants and Cross Respondents,

v.

JONATHAN MORROW, EVANS NGUYEN and
MILWAUKEE ELECTRIC TOOL CORPORATION,
Respondents and Cross Appellants.

APPENDIX OF KEY OUT-OF-STATE CASES CITED IN RESPONDENTS' BRIEF

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PROOF OF SERVICE

The undersigned certifies that on the 5th day of May, 2010, he caused to be served, in the manner noted below, a copy of the Appendix to Respondents' Brief on the following counsel of record:

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DATED this 5th day of May, 2010.

APPENDIX TO KEY OUT-OF-STATE CASES

1. *Automated Concepts, Inc. v. Weaver*, No. 99 C 7599, 2000 WL 1134541 (N.D. Ill. Aug. 9, 2000)

2. *Boise Tower Associates v. Washington Capital Joint Master Trust Mortgage Income Fund*, No. 03-141-S-MHW, 2007 WL 4355815 (D. Idaho Dec. 10, 2007)

3. *FLIR Systems, Inc. v. Parrish*, 174 Cal. App. 4th 1270, 95 Cal. Rptr. 3d 307 (2009)

4. *Glynn Interactive, Inc. v. iTelehealth, Inc.*, No. Civ.A. DKC 2003-0449, 2004 WL 439236 (D. Md. Mar. 9, 2004)

5. *Heuser v. Kephart*, 215 F.3d 1186 (10th Cir. 2000)

6. *IDX System Corp. v. Epic System Corp.*, 285 F.3d 581 (7th Cir. 2002)

7. *Lazer, Inc. v. Kesselring*, 823 N.Y.S.2d 834 (2005)

8. *Lucht's Concrete Pumping, Inc. v. Horner*, 224 P.3d 355 (Colo. App. 2009) *cert. granted,* No. 09SC627, 2010 WL 341383 (Colo. Feb. 1, 2010)

9. *MSC Industrial Direct Co. v. Steele,* No. COA08-418, 2009 WL 2501762 (N.C. App. Aug. 18, 2009)

10. *Mextel, Inc. v. Air-Shields, Inc.*, No. Civ. A.01-CV-7308, 2005 WL 226112 (E.D. Pa. Jan. 31, 2005)

11. *Savor, Inc. v. FMR Corp.*, No. Civ.A 00C-10-149JRS, 2004 WL 1965869 (Del. Super. July 15, 2004)

12. *Schmersahl, Treloar & Co. v. McHugh*, 28 S.W.3d 345 (Mo. App. 2000)

13. *StonCor Group, Inc. v. Campton*, No. C05-1225JLR, 2006 WL 314336 (W.D. Wash. Feb. 7, 2006)

14. *Unisource Worldwide, Inc. v. Carrara*, 244 F. Supp. 2d 977 (C.D. Ill. 2003)

15. *Wilmar, Inc. v. Liles*, 185 S.E.2d 278 (N.C. App. 1971)

TAB 1

Only the Westlaw citation is currently available.

United States District Court, N.D. Illinois, Eastern Division.
AUTOMATED CONCEPTS INCORPORATED, Plaintiff,
v.
Ted WEAVER and Answerthink, Consulting Group, Inc., Defendants.
No. 99 C 7599.

Aug. 9, 2000.

MEMORANDUM OPINION AND ORDER

GUZMAN, J.

***1** Plaintiff Automated Concepts Incorporated ("ACI") has sued defendants Ted Weaver ("Weaver") and AnswerThink for breach of contract, breach of the duty of loyalty, tortious interference with contract, and tortious interference with economic advantage. Defendants have moved to dismiss the Complaint for failure to state a claim upon which relief can be granted pursuant to Fed.R.Civ.P. ("Rule") 12(b)(6). For the reasons set forth below, the Court grants in part and denies in part the motion.

Facts

ACI operates a computer and information systems and consulting firm that builds high technology business information management systems. (Compl.¶ 6.) ACI's principal place of business and state of incorporation is New York. (*Id.* ¶ 4.) ACI operates offices located in New York, New Jersey, and Illinois. (*Id.* ¶ 1.) In November 1998, ACI hired defendant Weaver as the Practice Manager of ACI's Knowledge Management practice at its Illinois office. (*Id.* ¶ 7.) When ACI hired Weaver, ACI and Weaver entered into an employment agreement containing a restrictive covenant, which included a non-solicitation clause. (Compl., Ex. 1, Agreement ("Agreement") ¶ 7.) The terms of the agreement highlight the confidential nature of ACI's affairs and specifically refer to "confidential information, trade secrets ... [and] copyright-protected information." (*Id.* ¶ 6.1.) ACI also alleges that "the goodwill and competitive ability of ACI depends, among other things, upon its keeping such services and information confidential ... [and that] disclosure of such confidential information would irreparably damage ACI and its Clients." (*Id.* ¶ 6.2.) The specific provision at issue reads as follows:

RESTRICTIVE COVENANT

> 7.1 *During the term of this Agreement and for one year following termination of EMPLOYEE'S employment for any reason:* (i) Employee shall not, directly or indirectly, either as an individual, as an employee or member of a partnership, or as an employee, officer, director or stockholder of any corporation, solicit or accept, or advise anyone else to solicit or accept, any business for data processing services, computer software development, and related activities from any Client of ACI, or from the personnel of any Client of ACI with whom EMPLOYEE transacted any business or from whom EMPLOYEE solicited any business during the term EMPLOYEE was employed by ACI; *(ii) EMPLOYEE shall not offer employment to or advise anyone else to offer employment to, any employee of ACI, or any former employee of ACI during such period:*
> (*Id.* ¶ 7 (emphasis added).)

As director of ACI's Knowledge Management practice group, thirteen highly-skilled employees directly reported to Weaver. (Compl.¶¶ 10, 18.) Both Weaver and the members of the Knowledge Management group have and used task-specific expertise in the area of business information management technology. (*Id.* ¶¶ 10, 18.) ACI alleges that both during and after his employment with ACI, Weaver solicited the employees of ACI or former employees of ACI, and successfully solicited three key employees-Jon Mika, Ofer Gal, and David Veith-to work for AnswerThink. (*Id.* ¶¶ 15, 16.) Further, ACI claims that AnswerThink urged Weaver's solicitation of ACI employees. (*Id.* ¶ 15.)

***2** Subsequent to his resignation in July of 1990, Weaver began working for defendant AnswerThink. (*Id.* ¶ 12.) ACI claims that Weaver's solicitation and AnswerThink's inducement of that solicitation was intentional, wrongful, malicious, and intended to destroy the viability of ACI's Knowledge Management practice. (*Id.* ¶ 15.) As a result of Weaver and AnswerThink's conduct, ACI's Knowledge Management practice has been deprived of the valuable services of key employees, which in turn has seriously impaired ACI's ability to honor its existing commitments to its clients. (*Id.* ¶¶ 19, 22.)

ACI filed a complaint against defendants on November 22, 1999. In Count I, ACI alleges that Weaver "wrongfully solicited the employment of employees of ACI ... and/or advised AnswerThink to offer employment to employees of ACI or former employees of ACI." (*Id.* ¶ 21). Furthermore, as a result of Weaver's conduct, ACI alleges that it "has been deprived of the valuable services of key employees comprising approximately one-third of ACI's Knowledge Management practice." (*Id.* ¶ 22.) ACI asserts that Weaver has accordingly breached the employment agreement. (*Id.* ¶ 23.)

In Count II, ACI alleges nearly identical facts and adds that Weaver breached a fiduciary duty when he engaged in "intentional, wrongful, and malicious conduct designed to destroy the viability of ACI's Knowledge Management practice." (*Id.* ¶ 26.) ACI alleges that Weaver's breach of fiduciary duty deprived ACI of the one-third of its Knowledge Management practice. (*Id.* ¶ 28.)

In Count III, ACI alleges AnswerThink tortiously interfered with Weaver's employment agreement. ACI alleges that "while Weaver was still employed by ACI, and at times within a year since his resignation, AnswerThink, required, requested, advised, provided incentives or otherwise encouraged Weaver to wrongfully solicit the employment of employees of ACI or former employees of ACI ...." (*Id.* ¶ 32.)

In Count IV, ACI brings forth a claim for tortious interference with economic advantage. ACI asserts that "[a]s a result of ... [the] acts of AnswerThink and Weaver, ACI has been deprived of the valuable services of key employees... tortiously interfer[ing] with ACI's ability to conduct its business and honor its commitments to its clients. (*Id.* ¶¶ 38, 39.)

Finally, ACI demands relief in the form of punitive damages under each of the four counts and requests attorney's fees. (*Id.* ¶¶ 30, 35, 40(a)-(d), (f).)

Discussion

In deciding a motion to dismiss, a district court must accept as true all well-pleaded allegations set forth in the complaint. *See* *Los Angeles v. Preferred Communications, Inc.*, 476 U.S. 488, 493 (1986); *Marmon Group, Inc. v. Rexnord, Inc.*, 822 F.2d 31, 34 (7th Cir.1987). All reasonable inferences to be drawn from those allegations are also accepted as true. *See* *Nelson v. Monroe Regional Med. Ctr.*, 925 F.2d 1555, 1558 (7th Cir.1991). Dismissal is only justified when the allegations of the complaint itself clearly indicate that plaintiff does not have a claim upon which relief can be granted. *See* *American Nurses' Ass'n v. Illinois*, 783 F.2d 716, 724 (7th Cir.1986). Furthermore, "a complaint should not be dismissed for failure to state a claim unless it appears beyond a doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley v.. Gibson*, 355 U.S. 41, 45-46 (1957).

*3 Plaintiff submitted an affidavit in support of its memorandum in opposition to defendants' motion to dismiss. When examining pleadings, a court may take into consideration "certain extraneous materials, such as the terms of a written agreement and other exhibits attached to the complaint, Fed.R.Civ.P. 10(c), as well as the memoranda in support of and in opposition to the motion." *Three D Depts., Inc. v. K Mart Corp.*, 670 F.Supp. 1404, 1406 (N .D. Ill.1987). However, the "court may not ... rely upon affidavits or other materials addressed to the truth or falsity of plaintiff's factual assertions. *Id.* Thus, the Court will only consider the Complaint, the employment agreement attached to the Complaint, and the memoranda. The Court excludes from its analysis the affidavit of Gary Markham.

I. Breach of Contract (Count I)

Defendants argue that Count I fails to state a claim for breach of contract because the restrictive covenant in Weaver's employment agreement is unenforceable. Defendants contend that the provision is unenforceable because ACI fails to demonstrate a legitimate interest as required by New York law. [FN1]

> FN1. Federal courts exercising diversity jurisdiction employ the conflict of law rules of the forum state. *Klaxon Co. v. Stentor Elec-*

> *tric Mfg. Co.,* 313 U.S. 487, 496-97 (1941). When, as here, a contract has a choice of law provision and the cause of action is premised on contract, "Illinois courts look to the law established by that provision unless the chosen state has no substantial relationship to the parties or the transaction, or the public policy of Illinois would be violated." *Ludgate v. Becker,* 906 F.Supp. 1233, 1240 (N.D.Ill.1995). In this case the parties executed an agreement with a choice of law clause that provides that New York law would govern the agreement. Further, the Court does not find, and neither party argues, that New York lacks a substantial relationship to the parties or transaction or that an application of New York law would infringe upon Illinois public policy. Thus, New York law applies to the breach of contract claim.

Unlike some states, New York has not enacted statutes to govern the enforceability of restrictive covenants in the employment context. Instead, New York relies upon a developing body of case law to determine the enforceability of each covenant. New York courts consider the interests of the employer, the employee, and the public. *See, e.g., Karpinski v. Ingraci,* 28 N.Y.2d 45, 48, 268 N.E.2d 751, 752, 320 N.Y.S.2d 1, 3, (N.Y.1971); *Services Sys. Corp. v. Harris,* 41 A.D.2d 20, 22-24, 341 N.Y.S.2d 702, 704-05 (N.Y.App.Div.1973). In *Service Systems v. Harris,* the New York Appellate court intimated five factors necessary to determine the enforceability of a restrictive covenant within an employment contract:

(1) the time of the restriction must be reasonable;

(2) the geographical restraint must be reasonable;

(3) the burden on the employee must not be unreasonable;

(4) the general public must not incur harm as a result of enforcement; and

(5) the restriction must be necessary for the employer's protection.

Service Sys., 41 A.D.2d at 23, 341 N.Y.S.2d at 705-06. When considering these five elements, New York courts have consistently noted that rather than applying a fixed test, that "[e]ach case must, of course, depend, to a great extent, upon its own facts." *Karpinski,* 28 N.Y.2d at 49, 268 N.E.2d at 753, 320 N.Y.S.2d at 4; *see also Lynch v. Bailey,* 275 A.D. 527, 530-531, 90 N.Y.S.2d 359, 362, *aff'd,* 300 N.Y. 615, 90 N.E.2d 484 (1949) (noting that the crux of the problem is "whether ... [a] particular agreement in light of its extent, scope and purpose and all the facts and circumstances presented, is invalid and void.")

With regard to the time and geographic constraints, the Agreement does not restrict Weaver from seeking employment anywhere he may wish to work, and it only restricts him from soliciting associates during his employment and one year thereafter. Thus, the Court finds these aspects of the restrictive covenant are reasonable. *See Innovative Networks, Inc. v. Satellite Airlines Ticketing Ctrs., Inc .,* 871 F.Supp. 709, 728 (S.D.N.Y.1995) (holding restrictive covenant enforceable where provision placed a twelve-month time restraint on former employee); *Ecolab, Inc. v. K.P. Laundry Mach., Inc.,* 656 F.Supp. 894, 898-99 (S.D.N.Y.1984) (finding restrictive covenant reasonable where former employees were able to pursue livelihood, and were not subjected to geographic limitations). In addition, the restrictive covenant not to solicit employees does not place an unreasonable burden on Weaver's capacity to make full use of his talents and abilities and to pursue his livelihood. Because the restrictive covenant is narrowly drawn, it has only a *de minimis* effect on the public. Here, the public's right to utilize the talents and abilities of Weaver is hardly burdened-Weaver is only prohibited from raiding ACI and taking its employees. Thus, ACI's restrictive covenant is reasonable with respect to the scope of the time and geographic restriction and the burden on Weaver and the public.

*4 Defendants argue that ACI's non-solicitation provision is merely an attempt to insulate itself from fair competition rather than protecting a legitimate interest. The cases on which defendants rely with regard to legitimate interests are inapposite because they concern covenants not to compete, not covenants not to solicit employees of a former employer. Unlike a covenant not to compete, which has the potential of threatening a person's livelihood, a covenant not to solicit employees merely prohibits a person from pirating employees of the former employer and inducing them to work for another entity. Contrary to defendants' contention, a covenant not to solicit employees does not prevent any employee from seeking better work opportunities because he or she is free to find another job on his or her own. Thus, the Court finds that an employer's interest in preventing a current or former employee from raiding its employee rosters is reasonable. Moreover, it is clear that New York law recognizes the enforceability of covenants not to solicit employees. *Veraldi v. American Analytical Labs., Inc.,* 706 N.Y.S .2d 158, 159-60 (N.Y.App.Div.2000). As with all restrictive covenants, the overarching concern is that an employer "is entitled to protection from unfair or illegal conduct that causes economic injury." *American Broad. Cos., Inc. v. Wolf,* 52 N.Y.2d 394, 403-04, 420 N.E.2d 363, 366-68, 438 N.Y.S.2d 482, 486-87 (N.Y.1981). ACI has alleged that Weaver raided its Knowledge Management practice by successfully soliciting several key employees, including Jon Mika, Ofer Gal, and David Veith, with the intent to destroy its practice's viability. (Compl.¶ 16.) ACI further alleges that Weaver's solicitation of these employees, in essence, gutted its Knowledge Management practice and seriously impaired its ability to service its existing clients. (*Id.* ¶¶ 15, 19.) Therefore, ACI has alleged a legitimate interest in preventing unfair competition that resulted in economic injury. Because the Court finds that, as alleged, the covenant not to solicit employees is reasonable in all aspects and furthers a legitimate interest. Thus, the Court denies defendants' motion to dismiss Count I.

II. Breach of Duty of Loyalty (Count II)

As an initial matter, ACI entitled Count II as "Breach of Contract and Duty of Loyalty by Weaver." Defendants argue, and the Court agrees, that the breach of contract claim in Count II is the same as that in Count I. Thus, to the extent that the breach of contract claim in Count II is redundant, defendants' motion to dismiss is granted.

Next, defendants argue that ACI's breach of duty of loyalty claim in Count II must be dismissed because ACI fails to state a claim under New York law. ACI argues that Illinois law applies and that it has pleaded its claim sufficiently.

Illinois has adopted the internal affairs doctrine, which provides that "[w]hen the subject is liability of officers and directors for their stewardship of the corporation, the law presumptively applicable is the law of the place of incorporation." *Resolution Trust Corp. v. Chapman,* 29 F.3d 1120, 1122 (7th Cir.1994). This doctrine "recognizes the benefits of using one rule of law to determine the duties and liabilities of directors and officers whose firm may do business in many states." *Id.* "[O]therwise a corporation could be faced with conflicting demands." *Edgar v. MITE Corp.,* 457 U.S. 624, 645 (1982).

*5 At least one court has applied the doctrine to an employer's breach of fiduciary duty claims against employees regardless of whether they hold a director or officer position. *Regal-Beloit Corp. v. Drecoll,* 955 F.Supp. 849, 857-58 (N.D.Ill.1996). The Court finds no plausible reason for distinguishing between an officer or director and an employee, and ACI provides none. After all, the application of a predictable rule of law with regard to mid-level employees is equally beneficial-especially where, as here, the employer does business in different states, *i.e.,* Illinois, New Jersey, and New York. Thus, the Court applies the internal affairs doctrine, and finds that the law of incorporation, New York, governs.

"Fundamental to ... [the employer-employee] relationship is the proposition that an employee is to be loyal to his employer and is 'prohibited from acting in any manner inconsistent with his agency or trust and is at all times bound to exercise the utmost good faith and loyalty in the performance of his duties." ' *Western Elec. Co. v. Brenner,* 41 N.Y.2d 291, 295, 360 N.E.2d 1091, 1094, 392 N.Y.S.2d 409, 411 (N.Y.App.Div.1977) (quoting *Lamdin v. Broadway Surface Adver. Corp.,* 272 N.Y. 133, 138, 5 N.E.2d 66, 67 (N.Y.1936)). An employee breaches his duty of loyalty where he induces other employees to join a competitor by using dishonest means or by designing a scheme with the sole purpose of causing damage. *Headquarters Buick-Nissan, Inc. v. Michael Oldsmobile,* 149 A.D.2d 302, 304, 539 N.Y.S.2d 355, 355 (N.Y.App.Div.1989).

ACI alleges that Weaver solicited the employment of employees or former ACI employees with the purpose of destroying ACI's Knowledge Management unit's viability. (Compl.¶ 15.) ACI contends that Weaver's conduct was intentional, wrongful, and malicious. (*Id.* ¶ 26.) Further, ACI maintains that, Weaver deprived ACI of three of its key employees, or one third of the employees in its practice, and as a result, ACI is unable to honor its commitments to existing clients. (*Id.* ¶¶ 19, 28.) Accordingly, ACI states a claim for breach of the duty of loyalty.

III. Tortious Interference with Contract (Count III)

Defendants next argue that in Count III, ACI fails to state a claim that AnswerThink tortiously interfered with ACI's employment agreement with Weaver. ACI disagrees.

Conforming with Illinois' choice-of-law rules, the court must employ the substantive law of the state with the most significant relationship to the tort at issue. *See* *Ingersoll v. Klein,* 46 Ill.2d 42, 44, 262 N.E.2d 593, 595 (1970). "This test requires us to consider: (a) the place where the injury occurred; (b) the place where the conduct causing the injury occurred; (c) the parties' domiciles and places of business; and (d) the place where the parties' relationship is centered." *Rohlfing v. Manor Care, Inc.,* 172 F.R.D. 330, 340-41 (N.D.Ill.1997).

Given the facts of this case, Illinois has the most significant relationship to the tort alleged in Count III (tortious interference with contract against AnswerThink), as well as that alleged in Count IV (tortious interference with economic advantage against AnswerThink and Weaver) despite the fact that ACI is incorporated in New York. The injury-or interference with the contract or economic advantage-occurred in Illinois; the conduct causing the injury-AnswerThink's inducing Weaver to breach his contract and Weaver and AnswerThink's interference with ACI's ability to serve its clients-occurred in Illinois; and the parties' relationship is centered in Illinois. Therefore, the Court applies Illinois law to ACI's tort claims.

***6** To state a claim for tortious interference with contract, a plaintiff must plead: (1) the existence of a valid contract, (2) defendant's knowledge of the existence of the contract, (3) defendant's intentional and malicious inducement of the breach of the contract, (4) breach of the contract caused by defendant's wrongful conduct and resultant damage to the plaintiff. *See* *Fieldcrest Builders, Inc. v. Antonucci,* 34 Ill.App.3d 597, 611, 724 N.E.2d 49, 61, 243 Ill.Dec. 740, 752 (1st Dist.1999); *Swager v. Couri,* 60 Ill.App. 192, 193-94, 376 N.E.2d 456, 459, 17 Ill.Dec. 457, 459 (3rd Dist.1978), *aff'd,* 77 Ill.2d 173, 395 N.E.2d 921, 32 Ill.Dec. 540 (1979).

ACI alleges that AnswerThink "required, requested advised, provided incentives or otherwise encouraged Weaver to wrongfully solicit the employment of employees of ACI or former employees of ACI" (Compl.¶ 32.) ACI submits that AnswerThink engaged in this conduct "while Weaver was still employed by ACI, and at times within a year since his resignation." (*Id.* ¶ 32.) Furthermore, ACI alleges that the acts of both AnswerThink and Weaver "were intentional, wrongful, malicious and intended to destroy the viability of ACI's Knowledge Management practice." (*Id.* ¶ 15.) Finally, ACI alleges that Weaver's breach of the contract caused by AnswerThink's wrongful conduct, resulted in damage to ACI. (*Id.* ¶¶ 15, 32-35.)

Defendants mainly argue that because no valid contract exists between ACI and Weaver, there can be no tortious interference with an unenforceable contract. However, as discussed above, the Court has already determined that ACI states a claim for breach of contract because as alleged, the restrictive covenant is enforceable.

Defendants further argue that even if the covenant is enforceable, ACI's tortious interference with contract claim fails because ACI alleges that AnswerThink induced Weaver to breach his contract in a "conclusory and generic fashion." (Defs.' Reply at 11.) Contrary to defendants' argument, a plaintiff need not allege elaborate factual allegations. Federal courts require notice pleading, which provides a short plain statement of the claim upon which plaintiff rests its cause of action. *See* *Perkins v. Silverstein,* 939 F.2d 463, 467 (7th Cir.1991). Moreover, in addition to the allegations supporting its breach of contract claim discussed above, ACI alleges that "while Weaver was still employed by ACI, and at times within a year since his resignation, AnswerThink, required, requested, advised, provided incentives or otherwise encouraged Weaver to wrongfully solicit the employment of employees of ACI or former employees of ACI and/or offer employment to employees of ACI or former employees of ACI." (Compl.¶ 37.) This is sufficient to provide AnswerThink with notice of the claims against it. Accordingly, the Court denies defendants' motion to dismiss ACI's tortious interference with contract claim.

IV. Tortious Interference with Prospective Economic Advantage

*7 Defendants argue that ACI's allegations in Count IV fail to state a claim for tortious interference with prospective economic advantage. The Court agrees. To state a claim for tortious interference with economic advantage plaintiff must demonstrate: (1) "plaintiff's reasonable expectancy of entering into a valid business relationship"; (2) "the defendant's knowledge of this expectancy"; (3) "an intentional interference by the defendant which prevents the expectancy from ripening into a valid business relationship"; and "damages to the plaintiff from such interference." *Crinkley v. Dow Jones & Co.*, 67 Ill.App.3d 869, 878, 385 N.E.2d 714, 720, 24 Ill.Dec. 573, 579 (1st Dist.1979). Under Illinois law, "[t]he tort requires that the defendant have taken some action toward a third party which caused the third party not to do business with the plaintiff." *Young v. Connecticut Mut. Life Ins. Co.*, No. 90 C 254, 1990 WL 125496, at *4 (N.D.Ill. Aug. 17, 1990). "The action toward the third party must be some sort of direct interference with the relationship between the plaintiff and the third party, such as disparagement or other wrongful conduct." *Id.*

ACI alleges that because defendants deprived ACI of the services of key employees, defendants interfered with ACI's ability to conduct its business and honor its commitments to its clients. (Compl.¶¶ 38-39.) Plainly ACI has not alleged and cannot allege that defendants took direct action toward ACI's clients. Further, ACI clearly fails to allege that the defendants' conduct caused ACI's clients not to do business with ACI.

Moreover, ACI has not alleged a reasonable business expectancy. The fact that ACI has a "track record" of receiving work from a particular customer in the past, in and of itself, does not establish a reasonable expectation of ACI's entering into any particular future business relationship with such a customer. *See International Serv. Assocs., Inc. v. Arco Management*, No. 94 C 1807, 1994 WL 583302, at *7 (N.D.Ill. Oct. 21, 1994).

In sum, ACI has not alleged the elements to state a claim for tortious interference with prospective economic advantage. Accordingly, the Court dismisses Count IV with prejudice.

V. Punitive Damages

Defendants have moved to strike plaintiff's request for punitive damages and attorney's fees. ACI has failed to respond to defendants' argument regarding attorney's fees and therefore it does not dispute that it has not stated a claim for such fees. Thus, the Court grants defendants' motion to dismiss ACI's request for attorney's fees in each count of the Complaint.

With regard to ACI's request for punitive damages in its breach of contract claim, under New York law, punitive damages have been awarded in breach of contract cases where plaintiff's claim satisfies a two part test: (1) the conduct constituting, accompanying, or associated with the breach contract must be actionable as an independent tort for which compensatory damages are ordinarily available; and (2) the conduct must be sufficiently egregious-tortious conduct aimed at the public in general-to warrant the additional imposition of exemplary damages. *Rocanova v. Equitable Life Assurance Soc'y*, 83 N.Y.2d 603, 613, 634 N.E.2d 940, 943-44, 612 N.Y.S.2d 339, 342-43 (N.Y.1994). "Punitive or exemplary damages have been allowed in cases where the wrong complained of is morally culpable, or is actuated by evil and reprehensible motives, not only to punish the defendant but to deter him, as well as others who might otherwise be so prompted, from indulging in similar conduct in the future." *Walker v. Sheldon*, 10 N.Y.2d 401, 404, 179 N.E.2d 497, 497, 223 N.Y.S.2d 488, 488 (N.Y.1961).

*8 With regard to the first prong of the test, as discussed above, ACI's breach of contract claim does not support an independent tort claim against Weaver for tortious interference with economic advantage. Because New York law requires that a plaintiff satisfy both prongs of the punitive damages test for contract claims, it is clear that the Court must strike ACI's request for punitive damages in Count I.

Next, defendants argue that ACI cannot recover punitive damages for its breach of fiduciary duty and remaining tort claims because it has failed to allege that defendants' conduct warranted punitive damages. With regard to ACI's remaining tort claims, Illinois courts will allow punitive damages in the presence of aggravated circumstances, *i.e.*, fraud, willfulness, wantonness, or malice appearing with a wrongful act. *See* Beaton & Assocs., Ltd. v. Joslyn Mfg. & Supply Co., 159 Ill.App.3d 834, 845-47, 512 N.E.2d 1286, 1293, 111 Ill.Dec. 649, 656 (1st Dist.1987). With regard to ACI's breach of duty of loyalty claim, under New York law, punitive damages are available for a breach of fiduciary duty where there is evidence of malicious or reckless misconduct on the part of the defendant. *See* Guardian Mortgage Acceptance Corp. v. Bankers Trust Co., 259 A.D.2d 358, 359, 687 N.Y.S.2d 56, 56 (N.Y.App.Div.1999).

In this case, plaintiff alleges that Weaver willfully breached his employment agreement and that Weaver and ACI willfully interfered with employment agreements between ACI and its employees. (Compl.¶¶ 15, 20, 23, 26, 27, 29, 32, 34.) ACI's complaint further suggests the presence of aggravated circumstances in the form of wrongful conduct and a malicious motive. ACI alleges that the "acts were intentional, wrongful, malicious, and intended to destroy the viability of ACI's Knowledge Management practice." (*Id.* ¶ 15.) If, as plaintiff alleges, defendants acted with malicious intent to destroy its Knowledge Management practice, such a motive would support a claim for punitive damages for ACI's remaining tort claims and breach of duty claim.

Conclusion

For the foregoing reasons, defendants' motion to dismiss is granted as to ACI's: (1) request for punitive damages for breach of contract in Count I; (2) breach of contract claim in Count II because that claim is redundant; (3) tortious interference with prospective economic advantage claim (Count IV); and (4) request for attorney's fees in all counts. In all other respects, defendants' motion is denied.

SO ORDERED

N.D.Ill.,2000.
Automated Concepts Inc. v. Weaver
Not Reported in F.Supp.2d, 2000 WL 1134541 (N.D.Ill.)

END OF DOCUMENT

TAB 2

Only the Westlaw citation is currently available.

United States District Court,
D. Idaho.
BOISE TOWER ASSOCIATES, LLC, a Washington Limited Liability Company, Plaintiff,
v.
WASHINGTON CAPITAL JOINT MASTER TRUST MORTGAGE INCOME FUND, et al., Defendants.
No. 03-141-S-MHW.

Dec. 10, 2007.

Christopher C. Burke, Jon T. Simmons, Richard H. Greener, Greener Banducci Shoemaker P.A., Eric S. Rossman, Rossman Law Group PLLC, Boise, ID, for Plaintiff.

James L. Martin, Randall A. Peterman, Moffatt Thomas Barrett Rock & Fields, Boise, ID, Bernard William McHugh, Ford Elsaesser, Elsaesser Jarzabek Anderson Marks Elliott & McHugh, Sandpoint, ID, for Defendants.

MEMORANDUM DECISION AND ORDER

MIKEL H. WILLIAMS, United States Chief Magistrate Judge.

***1** Currently pending before the Court are the Motion for Attorney Fees, Docket No. 317, and Motion for Taxation of Costs, Docket No. 319, filed by Defendants Washington Capital Joint Master Trust, Washington Capital Management, Inc., and BNY Western Trust Company (collectively, "WCM"). Pursuant to the Court's Order, Docket No. 313, WCM has elected to address its entitlement to attorney fees prior to submitting a memorandum and affidavits regarding the amount and reasonableness of claimed attorney fees. The Court heard oral argument on November 7, 2007, and took the matters under advisement. After careful consideration of the parties' arguments and written submissions, the Court will deny WCM's motions for the reasons discussed below.

I.

Background

On April 2, 2007, the Court issued its Memorandum Decision and Order finding that WCM was entitled to summary judgment on counts one and two of Boise Tower Associates, LLC's ("BTA") complaint alleging breach of contract and breach of the covenant of good faith and fair dealing. Docket No. 307.[FN1] Thereafter, the parties stipulated to dismiss WCM's counterclaim, and the Court entered final judgment in favor of WCM on July 6, 2007. Docket No. 315.

FN1. The Court also denied BTA's second motion for partial summary judgment, Docket No. 249.

WCM filed a motion under Fed.R.Civ.P. 54(d)(2) and Dist. Idaho Loc. Civ. R. 54.2 seeking attorney fees pursuant to Idaho Code § 12-120(3) as the prevailing party.[FN2] WCM also filed a motion seeking non-taxable costs under Dist. Idaho Loc. Civ. R. 54.1(c)(8), requesting $207,838.43. Docket No. 319.[FN3]

FN2. WCM also claims fees are owed under Idaho Code § 12-121. For fees to be awarded under Idaho Code § 12-121, BTA's claims must be frivolous, unreasonable, or without foundation. *Thomas v. Madsen,* 132 P.3d 392, 396 (Idaho 2006). If there is a legitimate triable issue of fact or issue of law, attorney fees may not be awarded under Idaho Code § 12-121 even if the losing party asserted factual or legal claims that were frivolous, unreasonable, or without foundation. *Thomas,* 132 P.3d at 396. WCM presented no argument or supporting facts in its memorandums, Docket Nos. 317, 330, that BTA pursued its claims frivolously or unreasonably. Accordingly, the Court finds that WCM waived any right it may have had to assert fees under that statute.

FN3. These discretionary costs are in addition to the costs outlined in WCM's Bill of Costs, Docket No. 318, requesting

$33,613.16. BTA did not file an objection to WCM's Bill of Costs and there is no overlap between the two requests.

II.

Discussion

A. WCM's Motion for Attorney Fees.

WCM argues it is entitled to attorney fees under Idaho law and cites *Alyeska Pipeline Serv. Co. v. Wilderness Soc'y,* 421, U.S. 240 (1975) for support.FN4 In that case, the Supreme Court held that a court sitting in diversity must apply the forum state's attorney fee law if it does not conflict with any federal law, and it represents the "substantial policy" of the state. *Alyeska Pipeline Serv. Co.,* 421 U.S. at 260, n. 31. WCM argues that Idaho Code § 12-120(3) applies, which provides that the prevailing party "shall" be allowed a reasonable attorney fee if the action is one to recover in any "commercial transaction." An award under § 12-120(3) is mandatory. *Nelson v. Anderson Lumber Co.,* 99 P.3d 1092, 1106 (Idaho Ct.App.2004). WCM further contends that a conflict of law analysis is not required under *Alyeska,* and that even if it is required, Idaho has the most significant relationship to the issue of attorney fees, citing *Arno v. Club Med Boutique, Inc.,* 134 F.3d 1424 (9th Cir.1998).

FN4. At oral argument, WCM directed the Court to *Ward v. Puregro Co.,* 913 P.2d 582 (Idaho 1996). The Court finds that case inapplicable here. *Ward* involved a contract with an explicit choice of law provision, which the court honored as part of the parties' agreement. *Ward,* 913 P.2d at 584. The parties in this case had no such provision in their contract. *See* First Am. Compl., Ex. A, Docket No 67.

While BTA agrees state law applies, it argues that the Court's choice of law analysis utilized in its Memorandum Decision and Order, Docket No. 248, applies with equal force to the issue of attorney fees. Accordingly, BTA contends that Washington state law applies. Not surprisingly, under Washington law the prevailing party is not automatically entitled to attorney fees. Washington courts may not award attorney fees unless there is a contract, statute, or recognized equitable exception. *City of Seattle v. McCready,* 931 P.2d 156, 160 (Wash.1997). There is no corresponding statute applicable in Washington that would award attorney fees to the prevailing parties in this case, and thus BTA asserts each party must bear its own costs and fees. FN5

FN5. Wash. Rev.Code § 4.84.330 allows the prevailing party in any action on a contract to be awarded reasonable attorney fees if the "contract or lease specifically provides that attorney's fees and costs, which are incurred to enforce the provisions of such contract or lease," are recoverable. The Loan Commitment Letter BTA alleged WCM breached had no such provision, and so this statute is inapplicable. *See* First Am. Compl., Docket No 67, Exhibit A.

***2** The Court finds that the *Alyeska* criteria are met. There is no conflict between state law and federal law concerning entitlement to attorney fees. And, it has been previously held that Idaho's fee statutes represent a substantial policy of the state of Idaho. *Lockheed Martin Idaho Technologies Co. v. Lockheed Martin Advanced Environ. Sys., Inc.,* 2006 WL 2095876 *2, Case No. CV 98-316-BLW (D.Idaho July 27, 2006). However, a choice of law analysis is required, because Idaho courts have determined that Idaho Code § 12-120(3) is a substantive law that enlarges the rights of litigants in a commercial transaction. *Griggs v. Nash,* 775 P .2d 120, 127 (Idaho 1989); *Myers v. Vermaas,* 753 P.2d 296, 298 (Idaho Ct.App.1988). Consequently, the Court is directed to turn to the substantive law of the forum state, including its choice-of-law rules, to ascertain the applicable state law governing the parties' entitlement to attorney fees.FN6 *See* Sims Snowboards, Inc. v. Kelly, 863 F.2d 643, 645 (9th Cir.1988) ("If the issue is 'substantive'-concerned with the legal rights of the parties-then a choice of law analysis must be made.").

FN6. WCM would have the Court ignore the choice-of-law issue in its entirety, relying upon *Alyeska* and *Lockheed.* Neither *Lockheed* or *Alyeska,* however, presented a choice-of-law issue affecting entitlement to attorney fees. The Court in *Lockheed* noted that if a conflict-of-law issue was present, the Court would have to consider it. *Lockheed,* 2006 WL 2095876 at *2 n. 1

(considering a conflict-of-laws analysis, but declining to apply it because there was no conflict present in that case). The same conflict-of-law analysis is required in this case when the litigants are arguing whether Idaho or Washington law applies to determine entitlement to attorney fees in a breach of contract matter. *See* McMahan v. Toto, 256 F.3d 1120, 1131-32 (11th Cir.2001) (explaining that if the matter is substantive, the law of the state, including its choice-of-law rules, applies and considering *Alyeska* only in the context of whether the state law conflicted with a federal statute or rule).

Idaho's and Washington's attorney fee statutes are different, and so a choice must be made. As the Court discussed in its July 22, 2006 Memorandum Decision and Order, Docket No. 248, Idaho applies the most significant relationship test in resolving conflict of law issues as set forth in RESTATEMENT (SECOND) CONFLICTS OF LAWS, although it has not adopted the Restatement formulation in full. *Barber v. State Farm Mut. Ins.*, 931 P.2d, 1195, 1199 (Idaho 1997). *See also* *Grover v. Isom*, 53 P.3d 821 (Idaho 2002); *Rungee v. Allied Van Lines, Inc.*, 449 P.2d 378 (Idaho 1968); *DeMeyer v. Maxwell*, 647 P.2d 783 (Idaho Ct.App.1982). "The goal of this test is to identify the state most significantly related to a particular issue and to apply its law to resolve that issue." *Suebert Excavators Inc. v. Anderson Logging Co.*, 889 P .2d. 82, 85 (Idaho 1995).

Both the underlying action upon which WCM sought summary judgment and the agreement between them and their Idaho attorneys are contracts, requiring the Court to examine: 1) the domicile, residence, nationality, place of incorporation, and place of business of the parties; 2) the place of negotiations of the contract; 3) the place of contracting; and 4) the place of performance; and 5) the location of the subject matter of the contract. RESTATEMENT (SECOND) CONFLICTS OF LAWS § 188 (1971).

Once the factual contacts between the parties are identified, the court then conducts an analysis to determine which state has the most significant relationship to the transaction by considering the following policies:

(a) the needs of the interstate and international systems,

(b) the relevant policies of the forum,

(c) the relevant policies of other interested states and the relative interests of those states in the determination of the particular issue,

***3** (d) the protection of justified expectations,

(e) the basic policies underlying the particular field of law,

(f) certainty, predictability and uniformity of result, and

(g) ease in the determination and application of the law to be applied.

RESTATEMENT (SECOND) CONFLICT OF LAWS § 6 (1971). *See also* *Rungee v. Allied Van Lines, Inc.*, 449 P .2d 378, 383 (Idaho 1968) (citing the Restatement).

In support of its argument that Idaho law applies to the issue of attorney fees, WCM argues that an issue by issue analysis is required and that the Courts previous decision applying Washington law to the contract does not necessarily drive the conclusion that Washington law applies to the question of an award of attorney fees. WCM contends that Idaho has the most significant relationship because the attorney fees were generated in Idaho, the parties contracted with Idaho lawyers, and BTA chose the forum. BTA counters that this Court's prior determination that Washington law applies to the contract is conclusive on this issue. Under Idaho law, BTA argues that Idaho Code § 12-120 is "adjunct" to the contract between the parties and cites *Myers v. Vermaas*, 753 P.2d 296 (Idaho Ct.App.1988) for the proposition that § 12-120 becomes a part of any commercial transaction in Idaho whether the parties intended to or not. BTA therefore contends it is improper to apply an Idaho substantive fee provision as an adjunct to another state's contract.

The Court agrees with BTA's analysis on this point. Contracts negotiated in Idaho would be governed by the holding in *Myers* that, in commercial litigation, Idaho Code § 12-120(3) would be adjunct to the underlying contractual agreement. In *Myers,* the Idaho Court of Appeals noted:

> Unlike I.C. § § 12-121 and 61-617A, I.C. § 12-120 provides for a *mandatory,* not discretionary, award of attorney fees to the prevailing party in commercial litigation. The automatic nature of an award under I.C. § 12-120 makes it, in effect, an adjunct to the underlying commercial agreement between the parties. It establishes an entitlement. In this respect, an award under the statute is closely akin to other "contractual or vested" rights contained in the agreement itself.

Id. at 298. While parties to a contract executed in Idaho and governed by Idaho law can avail themselves of § 12-120, the converse is not true. A contract entered into between parties in another state would not automatically have a substantive Idaho statutory fee component in their commercial agreements. It would be unreasonable to conclude otherwise.

With that said, the law governing liability for the underlying cause of action, *e.g.* breach of contract, does not automatically control the fee issue. For example, in *Rungee v. Allied Van Lines, Inc.,* 449 P.2d 378 (Idaho 1968), the court was presented with a choice between Florida and Idaho law involving enforcement of an insurance contract and an award of attorney fees under the contract to the prevailing party. In that case, although the insurance contract was executed in Florida, the prevailing party sought fees under Idaho's insurance enforcement statute. *Rungee,* 449 P.2d at 381. Florida had no statute under which attorney fees would be awarded. The court viewed the issue involved in that case as which state-Florida or Idaho-had the greater concern for the protection of an insured's contractual rights when the insurance contract applied to the interstate transfer of goods delivered to Idaho. *Id.* at 383-84. The court determined that Idaho had the more significant relationship to the transaction and the parties involved in that case, and therefore permitted the plaintiff to seek fees under the Idaho insurance enforcement statute at issue. *Id.* at 384. *See also* *MRO Communications, Inc. v. Am. Tel. & Tel. Co.,* 197 F.3d 1276, 1282 (9th Cir.1999) (applying the law of the forum state to determine whether a party was entitled to attorney fees in an action involving a choice between Nevada and New Jersey law); *Barber v. State Farm Mut. Auto. Ins. Co.,* 931 P .2d 1195 (Idaho 1997) (following *Rungee,* and reasoning under the same insurance statute considered in *Rungee* that Washington law applied to determine the issue of attorney fees).

*4 In *Arno v. Club Med Boutique Inc.,* 134 F.3d 1424 (9th Cir.1998), the Ninth Circuit considered a tort action brought by a California resident injured while working at a resort in a territory governed by French law. In its previous decision, the court determined that the law of the place where the tort occurred, in this case a French territory, rather than the law of California, the forum state, governed the substantive issues in the case. *Arno,* 22 F.3d at1468. However, when the plaintiff sought attorney fees, the court concluded that the law governing liability for the tort action did not control the fee issue, independently considered the choice-of-law issue, and held that California had the most significant interest in the manner in which the Plaintiff's attorney was compensated. *Id.* at 1426. *See also* *McMahan v. Toto,* 256 F.3d 1120, 1135 (11th Cir.2001) (deciding attorney fee issue independently of underlying tort claim under Florida's choice of law rules).

Accordingly, the Court must undertake an independent choice-of-law analysis. Applied to the issue of attorney fees in the present case, the Court previously considered that, as to the underlying contract action, the majority of the factors favored applying Washington law. All of the parties resided in Washington, although Mr. Peterson maintained residences both in Idaho and Washington, and BTA had a business office in Boise. The loan agreement was negotiated in Washington, executed in Washington, and was to be performed in Washington. BTA, however, availed itself of an Idaho forum under the principles of diversity. BTA's choice of forum required the parties to either hire Idaho counsel or out-of-state counsel to associate with local Idaho counsel.

As to the agreements between WCM and Idaho counsel, these contracts on their face would appear to favor application of Idaho law. WCM argued that *Arno* favored such a result, because the employment contracts were negotiated, executed, and performed in Idaho, and the fees were generated in Idaho. However that argument has only superficial appeal if the Court were inclined to constrain itself to considering the place where the fee agreement was entered into as the controlling the issue.

But the Court is not being asked to enforce the contract between WCM and Idaho counsel.FN7 Rather, the Court determined the litigants' rights under a Washington contract that Idaho lawyers were hired to enforce. Considering the matter in that context, the law favors application of Washington law to the issue of entitlement to attorney fees because of the policies articulated in § 6 of the Restatement. *See* Grover v. Isom, 53 P.3d at 825 (looking at the underlying policies to support its determination that Oregon law applied in a tort action). Although WCM hired Idaho counsel and litigated in the District of Idaho, counsel represented WCM in a suit alleging breach of a contract formed in Washington.

> FN7. *Arno* is distinguishable, because the plaintiff and her lawyer had entered into a contingent fee agreement. Despite the contingent fee agreement, Arno filed a fee application seeking reimbursement of attorney fees from the defendant rather than pay her attorney from the settlement proceeds. *Arno,* 134 F.3d at 1425. Although the Ninth Circuit did not elaborate, it noted that contingent fee arrangements were not honored under French law, the law governing the tort action. *Arno,* 134 F.3d at 1426. Thus, the court was being asked to enforce an employment agreement between Arno and her attorney, and it found California law governing contingent fee agreements applied. *Arno,* 134 F.3d at 1426.

While the parties should certainly be free to avail themselves of Idaho's courts and to hire counsel of their choice, it would not be proper for that decision to ultimately dictate the application of an Idaho substantive statute providing for attorney fees based upon that choice, when the substantive law of Washington governs the underlying contract. In other words, the parties are not entitled to attorney fees under an Idaho substantive statute that enlarges the rights of litigants to a commercial dispute when the law governing the contract denies litigants that right. Washington's fee statute would not award attorney fees to a litigant in a contract dispute unless the contract specifically provided for such an award. Wash. Rev.Code § 4.84.330. Nor can parties litigating breach of contract actions in Washington courts avail themselves of Idaho Code § 12-120(3), and thus neither should these litigants. If the Court were to hold otherwise, the decision would impact the important policies concerning attorney fees articulated by the state of Washington in its statutes.

*5 Litigants in an Idaho forum should also not be subjected to potentially uncertain results. In cases where it is clear that another state's substantive law applies to the contract governing the parties, they should expect that the other state's substantive law concerning entitlement to attorney fees applies. Attorney fee statutes, especially when they enlarge the rights of litigants to a commercial contract dispute, should not be applied based upon the choice of forum or the choice of attorney. To do so would promote forum shopping among those litigants that could avail themselves of diversity jurisdiction in Idaho when their particular agreement did not contain a provision awarding attorney fees to a prevailing party and further assuming that under the law of their state, fees would not be otherwise recoverable. Prevailing litigants seeking fees in a contract dispute governed by Washington law that would otherwise be litigated in a Washington court but for invocation of diversity jurisdiction should be limited to Washington substantive statutes governing availability of attorney fees as well. To hold otherwise would interject uncertainty, unpredictability, and non-uniform results.

Accordingly, WCM's motion regarding its entitlement to attorney fees under Idaho Code § 12-120(3) will be denied.

B. WCM's Motion for Non-Taxable Costs.

In addition to attorney fees, WCM also seeks non-taxable costs in the amount of $207,838.43 as the prevailing party under Fed.R.Civ.P. 54(d)(1) and Dist. Idaho Loc. Civ. R. 54.1(c)(8). 18 U.S.C. §§ 1920 and 1821 grant the Court authority to assess costs in cases before it. Fed.R.Civ.P. 54(d)(1) implements those statutes and provides that "[e]xcept when express provision is made either in a statute of the United States or in these rules, costs other than attorney fees shall be allowed as of course to the prevailing party unless the court otherwise directs[.]" The corresponding local rule defines a prevailing party as "the one who successfully prosecutes the action or successfully defends against it, prevails on the merits of the main issue, and the one in whose favor the decision or verdict is rendered and judgment entered." Dist. Idaho Loc. Civ. R. 54.1(b). As a threshold issue, BTA does not dispute that WCM prevailed in the litigation.

WCM seeks costs in addition to those enumerated in the local rule under subsection (c)(8), which allows recovery of "other items" not listed in the rule with prior court approval. Dist. Idaho Loc. Civ. R. 54.1(c)(8). The local rule does not define appropriate "other" costs. BTA objects overall to the costs claimed, asserting WCM has no legal authority explaining what constitutes appropriate "other costs" under Dist. Idaho Loc. Civ. R. 54.1(c)(8) and relying upon Idaho R. Civ. P. 54(d)(1)(D) for guidance. Idaho R. Civ. P. 54(d)(1)(D) allows for a party to recover discretionary costs when that party proves the costs are "necessary and exceptional costs reasonably incurred, and should in the interest of justice be assessed against the adverse party." BTA claims that these costs were not "exceptional," and so should not be awarded. WCM argues if state law applies for guidance, Washington law should be used.

***6** Despite the absence of federal guidance concerning "other" costs, federal procedural law, not state law, governs the award of costs even though the issues, including attorney fees, were decided under Washington state law. *Aceves v. Allstate Ins. Co.,* 68 F.3d 1160, 1167 (9th Cir.1995) (deciding the issue of costs under federal law although California law governed the substantive issues). This premise has been followed for over a century. *Dodge v. Tulleys,* 144 U.S. 451, 457 (1892) (noting that state law "does not determine the procedure of courts of the United States ... or the costs which are taxable there[.]"). Contrary to the arguments advanced by both parties, there is no need to look to either Washington or Idaho procedural statutes governing the award of costs.

The non-taxable costs WCM seeks consist of the following: (1) computerized research, $8,981.85; (2) out of town travel, $9,844.64; (3) expert witness fees, $164,383.53; (4) outside printing costs, $8,724.84; (5) digital discovery, $3,776.82; (6) in-house printing costs, $10,354.04; (7) long distance telephone charges, $1,592.03; and (8) PACER access fees, $180.68. FN8

FN8. WCM has reduced the actual amounts of costs claimed for all costs except expert witness fees by fifty percent. Defs.' Pet. at 2-3. The costs stated represent the amounts claimed after the reduction.

1. Expert Witness Fees.

At the hearing, WCM stated that it was withdrawing the claim for reimbursement of expert witness fees. It appears WCM has already asked for the statutory witness fees in the Bill of Costs, Docket No. 318, and so the request for additional expert witness fees will be denied.

2. Printing Costs.

WCM seeks outside and in-house printing costs in addition to those costs outlined in the Bill of Costs, Docket No. 318, arguing that the Court may interpret 28 U.S.C. § 1920 as encompassing those costs. *See Alflex Corp. v. Underwriters Laboratories, Inc.,* 914 F.2d 175, 177 (9th Cir.1990) (holding that *Crawford Fitting Co. v. J.T. Gibbons, Inc.,* 482 U.S. 437 (1987) "does not prevent courts from interpreting [28 U.S.C.] § 1920."); *Haagen-Dazs Co., Inc. v. Double Rainbow Gourmet Ice Creams, Inc.,* 920 F.2d 587, 588 (9th Cir.1990) (allowing printing costs at 50% of total costs under California local rules). 28 U.S.C. § 1920(3) permits the Court to award "fees" for "printing" with no limitation as to what those costs must relate to, while 28 U.S.C. § 1920(4) allows "fees" for copies of papers necessarily obtained for use in the case. BTA argues that such costs were not "exceptional," and so should be disallowed.

While the Court agrees *Alflex* and *Haagen-Dazs* held that the court has some leeway in interpreting what costs would be allowed under 28 U.S.C. § 1920, in those cases the court's local rules allowed for the costs claimed. For example, in *Haagen-Dazs,* the court upheld the award of costs for fifty percent of the plaintiff's cost of reproducing documents even though they were not introduced in support of the plaintiff's motion for summary judgment because the local rules allowed "the cost of reproducing documents obtained [in discovery] and used for any purpose in the case[.]" *Haagen-Dazs Co., Inc.,* 920 F.2d at 588. Similarly, in *Alflex,* the court upheld an award of costs for the cost of the original and one copy of all depositions because the local rule allowed it. *Alflex Corp.,* 914 F.2d at 176.

*7 In this district, the Court has chosen to limit costs for copies to those attached to a document required to be filed and served. Dist. Idaho Loc. Civ. R. 54.1(c)(5). "The cost of reproducing copies of motions, pleadings, notices, and other routine case papers is not taxable." *Id.* The cost of visual aids is taxable "if they are admitted into evidence." Dist. Idaho Loc. Civ. R. 54.1(c)(6). Also, the court is expressly limited to tax costs in conformity with 28 U.S.C. §§ 1920-1923. Dist. Idaho Loc. Civ. R. 54 .1(c). In the absence of an award of attorney fees such that these costs could be included in the award, the Court finds that the local rule expressly limits an award of such costs, and WCM is not entitled to claim costs for excess copying and printing other than what is enumerated in the local rule. Since WCM has already included those costs in their Bill of Costs, Docket No. 318, additional copy and printing charges are disallowed.

3. Miscellaneous Other Costs.

WCM argues that other costs claimed for computerized research, out of town travel, digital discovery, long distance telephone charges, and PACER access fees were reasonably and necessarily incurred. WCM contends that these costs are properly awarded as part of an attorney fee award. Defendant disagrees, arguing that since attorney fees are not recoverable under Washington law, these discretionary costs may not be awarded because they are not properly taxed as part of attorney fees.

This Court considers computer-aided research, like any other form of legal research, a component of attorney fees that should not always be independently taxed as an item of cost. *See Goff v. Washington County, et al.,* Case No. CV 03-268-MHW (April 10, 2006), *cited in Gomez v. Mastec North Am., Inc.,* Case No. CV 03-421-MHW (Dec. 13, 2006). The Court determined that attorney fees are not recoverable under Washington law, and so costs for computerized research may not be taxed. Nor could the Court find authority for the taxing as costs for out of town travel, long distance telephone charges, PACER fees, or digital discovery in an instance where attorney fees were not recoverable, and so finds that those costs are not appropriate.

ORDER

Based on the foregoing, the Court being otherwise fully advised in the premises, **IT IS HEREBY ORDERED that:**

1) Defendants' Motion for Attorney Fees (Docket No. 317) is DENIED.

2) Defendants' Petition for Non-Taxable Costs (Docket No. 319) is DENIED.

D.Idaho,2007.
Boise Tower Associates, LLC v. Washington Capital Joint Master Trust Mortg. Income Fund
Not Reported in F.Supp.2d, 2007 WL 4355815 (D.Idaho)

END OF DOCUMENT

TAB 3

H

Court of Appeal, Second District, Division 6, California.

FLIR SYSTEMS, INC., et al., Plaintiffs and Appellants,

v.

William PARRISH et al., Defendants and Respondents.

No. B209964.

June 15, 2009.
Review Denied Sept. 23, 2009.

Background: Employer brought action against former employees for misappropriation of trade secrets, seeking injunction. The Superior Court, Santa Barbara County, No. B8154145,James W. Brown, J., entered judgment for former employees after court trial, awarding attorney fees and costs. Employer appealed.

Holdings: The Court of Appeal, Yegan, P.J., held that:
(1) misappropriation claim was objectively specious;
(2) employer acted with subjective bad faith in bringing or maintaining the action;
(3) employee's act of bringing files home was not a threatened misappropriation of trade secrets;
(4) employee's statements that two of employer's patent applications were not valid was not a threatened misappropriation of trade secrets;
(5) trial court's earlier rulings for employer did not preclude bad faith sanctions;
(6) finding in trial court's tentative statement of decision did not preclude bad faith sanctions; and
(7) declining to hold post-trial hearing to address issue of bad faith was proper.

Affirmed.

West Headnotes

[1] Costs 102 ⚿194.44

102 Costs
102VIII Attorney Fees
102k194.44 k. Bad Faith or Meritless Litigation. Most Cited Cases
Statute authorizing award of reasonable attorney fees and costs when a claim of trade secret misappropriation is made in bad faith authorizes the trial court to award attorney fees as a deterrent to specious trade secret claims. West's Ann.Cal.Civ.Code § 3426.4.

[2] Costs 102 ⚿2

102 Costs
102I Nature, Grounds, and Extent of Right in General
102k1 Nature and Grounds of Right
102k2 k. In General. Most Cited Cases

Costs 102 ⚿194.44

102 Costs
102VIII Attorney Fees
102k194.44 k. Bad Faith or Meritless Litigation. Most Cited Cases
Because the award is a sanction, a trial court has broad discretion in awarding fees under statute authorizing award of reasonable attorney fees and costs when a claim of trade secret misappropriation is made in bad faith. West's Ann.Cal.Civ.Code § 3426.4.

[3] Appeal and Error 30 ⚿984(5)

30 Appeal and Error
30XVI Review
30XVI(H) Discretion of Lower Court
30k984 Costs and Allowances
30k984(5) k. Attorney Fees. Most Cited Cases

Appeal and Error 30 ⚿1024.1

30 Appeal and Error
30XVI Review

30XVI(I) Questions of Fact, Verdicts, and Findings
30XVI(I)6 Questions of Fact on Motions or Other Interlocutory or Special Proceedings
30k1024.1 k. In General. Most Cited Cases
On appeal from an order awarding attorney fees and costs based on a claim of trade secret misappropriation made in bad faith, the appellant has an uphill battle, and must overcome both the "sufficiency of evidence" rule and the "abuse of discretion" rule. West's Ann.Cal.Civ.Code § 3426.4.

[4] Costs 102 ⚷194.44

102 Costs
102VIII Attorney Fees
102k194.44 k. Bad Faith or Meritless Litigation. Most Cited Cases
"Objective speciousness," as required for bad faith in a claim of trade secret misappropriation supporting an award of reasonable attorney fees and costs, exists where the action superficially appears to have merit but there is a complete lack of evidence to support the claim. West's Ann.Cal.Civ.Code § 3426.4.

[5] Antitrust and Trade Regulation 29T ⚷438

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk438 k. Costs and Attorney Fees. Most Cited Cases
Trial court's finding that employer's trade secret misappropriation claim against former employees was objectively specious, in awarding attorney fees and costs, was supported by substantial evidence, including chief executive officer's (CEO) testimony that the lawsuit was filed because employer could not "tolerate a direct competitive threat" from the former employees, and employer's failure to prove its complaint's allegations that employees misappropriated secrets, that employees stated an intention to misappropriate trade secrets, and that employees caused employer to suffer actual damage. West's Ann.Cal.Civ.Code § 3426.4.
See Cal. Civil Practice (Thomson Reuters 2009) Business Litigation, §§ 66:2, 66:19; Cal. Transactions Forms, Business Transactions, § 9:43 (Thomson Reuters 2009); Chin et al., Cal. Practice Guide: Employment Litigation (The Rutter Group 2009) ¶ 14:216 (CAEMPL Ch. 14-C); 13 Witkin, Summary of Cal. Law (10th ed. 2005) Equity, § 91.

[6] Antitrust and Trade Regulation 29T ⚷438

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk438 k. Costs and Attorney Fees. Most Cited Cases
Statute authorizing award of reasonable attorney fees and costs when a claim of trade secret misappropriation is made in bad faith requires objective speciousness of the plaintiff's claim, as opposed to frivolousness. West's Ann.Cal.Civ.Code § 3426.4; West's Ann.Cal.C.C.P. § 128.5.

[7] Antitrust and Trade Regulation 29T ⚷414

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(A) In General
29Tk414 k. Elements of Misappropriation. Most Cited Cases
The doctrine of inevitable disclosure, which would allow a plaintiff to prove a claim of trade secret misappropriation by demonstrating that the defendant's new employment will inevitably lead him to rely on the plaintiff's trade secrets, is not the law in California. West's Ann.Cal.Bus. & Prof.Code § 16600.

[8] Injunction 212 ⚷56

212 Injunction
212II Subjects of Protection and Relief
212II(B) Matters Relating to Property
212k56 k. Disclosure or Use of Trade

Secrets. Most Cited Cases
Speculation that a departing employee may misappropriate and use a trade secret in a startup business will not support an injunction. West's Ann.Cal.Civ.Code § 3426.2.

[9] Antitrust and Trade Regulation 29T 414

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(A) In General
29Tk414 k. Elements of Misappropriation. Most Cited Cases
A misappropriation of trade secrets plaintiff must show an actual use or an actual threat. West's Ann.Cal.Civ.Code § 3426.2.

[10] Antitrust and Trade Regulation 29T 438

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk438 k. Costs and Attorney Fees. Most Cited Cases
Subjective bad faith, as required for bad faith in a claim of trade secret misappropriation supporting an award of reasonable attorney fees and costs, may be inferred by evidence that the plaintiff intended to cause unnecessary delay, filed the action to harass the defendant, or harbored an improper motive. West's Ann.Cal.Civ.Code § 3426.4.

[11] Antitrust and Trade Regulation 29T 438

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk438 k. Costs and Attorney Fees. Most Cited Cases
The timing of a trade secret misappropriation action may raise an inference of bad faith supporting a sanctions award of reasonable attorney fees and costs. West's Ann.Cal.Civ.Code § 3426.4.

[12] Antitrust and Trade Regulation 29T 438

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk438 k. Costs and Attorney Fees. Most Cited Cases
Trial court's finding that employer acted with subjective bad faith in bringing or maintaining a misappropriation of trade secrets action against former employees, in awarding attorney fees and costs to employees, was supported by substantial evidence, including contradictory testimony of employer's executives who did not want to take responsibility for initiating and maintaining the action, employer's failure to seek an order compelling employees to return anything in requesting a permanent injunction, employer's failure to identify what trade secrets would be subject to permanent injunction, and employer's settlement demands which were inflammatory and contrary to public policy. West's Ann.Cal.Civ.Code § 3426.4.

[13] Antitrust and Trade Regulation 29T 420

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(A) In General
29Tk420 k. Particular Cases, in General. Most Cited Cases

Injunction 212 56

212 Injunction
212II Subjects of Protection and Relief
212II(B) Matters Relating to Property
212k56 k. Disclosure or Use of Trade Secrets. Most Cited Cases
Employee's act of copying employer's commodity

code database onto a hard drive was not a "threatened misappropriation" of trade secrets subject to injunction under California Uniform Trade Secrets Act, even though employee later stopped working for employer and planned to start a competing business, where employee notified employer that he had copied the files in an attempt to work on them at home and that he later destroyed the hard drive; employee did not threaten to misuse trade secrets, by words or conduct. West's Ann.Cal.Civ.Code § 3426.2.

[14] Antitrust and Trade Regulation 29T 413

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(A) In General
29Tk413 k. What Are "Trade Secrets" or Other Protected Proprietary Information, in General. Most Cited Cases

A "threatened misappropriation" of trade secrets, as would support injunction under California Uniform Trade Secrets Act, means a threat by a defendant to misuse trade secrets, manifested by words or conduct, where the evidence indicates imminent misuse. West's Ann.Cal.Civ.Code § 3426.2.

[15] Injunction 212 56

212 Injunction
212II Subjects of Protection and Relief
212II(B) Matters Relating to Property
212k56 k. Disclosure or Use of Trade Secrets. Most Cited Cases

Mere possession of trade secrets by a departing employee is not enough for an injunction under California Uniform Trade Secrets Act. West's Ann.Cal.Civ.Code § 3426.2.

[16] Injunction 212 56

212 Injunction
212II Subjects of Protection and Relief
212II(B) Matters Relating to Property
212k56 k. Disclosure or Use of Trade Secrets. Most Cited Cases

Under California Uniform Trade Secrets Act, a trade secret will not be protected by the extraordinary remedy of an injunction on mere suspicion or apprehension of injury; there must be a substantial threat of impending injury before an injunction will issue. West's Ann.Cal.Civ.Code § 3426.2.

[17] Injunction 212 56

212 Injunction
212II Subjects of Protection and Relief
212II(B) Matters Relating to Property
212k56 k. Disclosure or Use of Trade Secrets. Most Cited Cases

Provision of California Uniform Trade Secrets Act stating that affirmative acts to protect a trade secret may be compelled by court order authorizes mandatory, not prohibitory injunctions. West's Ann.Cal.Civ.Code § 3426.2(c).

[18] Injunction 212 56

212 Injunction
212II Subjects of Protection and Relief
212II(B) Matters Relating to Property
212k56 k. Disclosure or Use of Trade Secrets. Most Cited Cases

Provision of California Uniform Trade Secrets Act stating that affirmative acts to protect a trade secret may be compelled by court order does not authorize an order enjoining a remote threat or misuse or disclosure, since such an order is prohibitory and does not necessarily compel affirmative acts. West's Ann.Cal.Civ.Code § 3426.2(c).

[19] Antitrust and Trade Regulation 29T 420

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(A) In General
29Tk420 k. Particular Cases, in General. Most Cited Cases

Injunction 212 🔑56

212 Injunction
212II Subjects of Protection and Relief
212II(B) Matters Relating to Property
212k56 k. Disclosure or Use of Trade Secrets. Most Cited Cases
Trial court acted within its discretion in finding that former employee's statements that two of employer's patent applications based on a process employee had worked on were not valid was not a threatened misappropriation of trade secrets subject to injunction under California Uniform Trade Secrets Act, where employer's Chief Intellectual Property Officer opined that the United States Patent & Trademark Office could go either way on the validity of the applications, and where employer's officers and managers stated that the former employee was trustworthy and that an inventor's disagreement about a patent application did not signal a plot to steal trade secrets. West's Ann.Cal.Civ.Code § 3426.2.

[20] Injunction 212 🔑189

212 Injunction
212V Permanent Injunction and Other Relief
212k189 k. Nature and Scope of Relief. Most Cited Cases
Employer's proposed injunction against former employees under California Uniform Trade Secrets Act, barring employees from developing certain products for a 12 month period even if employees did not use employer's technology or trade secrets, would be an unlawful restraint on trade. West's Ann.Cal.Civ.Code § 3426.2; West's Ann.Cal.Bus. & Prof.Code § 16600.

[21] Compromise and Settlement 89 🔑9

89 Compromise and Settlement
89I In General
89k7 Validity
89k9 k. Legality of Consideration. Most Cited Cases
A condition in employer's proposed settlement of a misappropriation of trade secrets action against former employees, barring employees from working with certain third party foundries, was an unlawful trade restraint. West's Ann.Cal.Bus. & Prof.Code § 16600; West's Ann.Cal.Civ.Code § 3426 et seq.

[22] Compromise and Settlement 89 🔑9

89 Compromise and Settlement
89I In General
89k7 Validity
89k9 k. Legality of Consideration. Most Cited Cases
A condition in employer's proposed settlement of a misappropriation of trade secrets action against former employees, barring the former employees from hiring employer's other employees, violated public policy. West's Ann.Cal.Bus. & Prof.Code § 16600; West's Ann.Cal.Civ.Code § 3426 et seq.

[23] Compromise and Settlement 89 🔑9

89 Compromise and Settlement
89I In General
89k7 Validity
89k9 k. Legality of Consideration. Most Cited Cases
A condition in employer's proposed settlement of a misappropriation of trade secrets action against former employees, barring the former employees from challenging employer's patent applications, violated public policy. 37 C.F.R. § 1.56; West's Ann.Cal.Civ.Code § 3426 et seq.

[24] Antitrust and Trade Regulation 29T 🔑438

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk438 k. Costs and Attorney Fees. Most Cited Cases
A trial court may consider a party's dilatory tactics and bad faith settlement demands in maintaining

the action, in awarding attorney fees and costs for bad faith in bringing or maintaining a misappropriation of trade secrets action. West's Ann.Cal.Civ.Code § 3426.4.

[25] Costs 102 ⚷194.44

102 Costs
102VIII Attorney Fees
102k194.44 k. Bad Faith or Meritless Litigation. Most Cited Cases

Malicious Prosecution 249 ⚷77

249 Malicious Prosecution
249V Actions
249k77 k. Costs. Most Cited Cases
In certain tort actions, such as malicious prosecution, the denial of summary judgment normally precludes the trial court from finding that the lawsuit was frivolous.

[26] Judgment 228 ⚷190

228 Judgment
228V On Motion or Summary Proceeding
228k190 k. Construction and Operation. Most Cited Cases
Trial court's denial of a motion for summary judgment, a motion in limine, and two nonsuit motions did not preclude trial court from awarding attorney fees and costs to former employees for employer's bad faith in bringing or maintaining misappropriation of trade secrets action, where employer opposed summary judgment motion with expert declarations suggesting there was a scientific methodology to predict the likelihood of trade secret misuse, but at trial employer's experts admitted there was no valid scientific methodology to predict trade secret misuse and agreed that no trade secrets were misappropriated. West's Ann.Cal.Civ.Code § 3426.4.

[27] Antitrust and Trade Regulation 29T ⚷438

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk438 k. Costs and Attorney Fees. Most Cited Cases
Under the California Uniform Trade Secret Act, sanctions may be awarded for the bad faith filing or maintenance of a groundless action. West's Ann.Cal.Civ.Code § 3426.4.

[28] Antitrust and Trade Regulation 29T ⚷438

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk438 k. Costs and Attorney Fees. Most Cited Cases
Under the California Uniform Trade Secret Act, a trade secrets claim brought in good faith could warrant an award of attorney fees if the claim is pursued beyond a point where the plaintiff no longer believes the case has merit. West's Ann.Cal.Civ.Code § 3426.4.

[29] Antitrust and Trade Regulation 29T ⚷438

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk438 k. Costs and Attorney Fees. Most Cited Cases
For purposes of an award of attorney fees and costs for bad faith in bringing or maintaining a misappropriation of trade secrets action, bad faith may be inferred where the specific shortcomings of the case are identified by opposing counsel, and the decision is made to go forward despite the inability to respond to the arguments raised. West's Ann.Cal.Civ.Code § 3426.4.

[30] Judges 227 ⚷24

227 Judges
227III Rights, Powers, Duties, and Liabilities
227k24 k. Judicial Powers and Functions in General. Most Cited Cases
A finding in trial court's tentative statement of decision, that former employees did not prevail on an unclean hands defense in employer's misappropriation of trade secrets action against former employees, did not preclude trial court from awarding attorney fees and costs to employees for employer's bad faith in bringing or maintaining the action, since the tentative statement of decision was not binding on the trial court, and the doctrine of unclean hands did not relate to the filing or maintenance of the action. West's Ann.Cal.Civ.Code § 3426.4; Cal.Rules of Court, Rule 3.1590(b).

[31] Appeal and Error 30 ⚷717

30 Appeal and Error
30X Record
30X(N) Matters Not Apparent of Record
30k717 k. Opinion of Lower Court. Most Cited Cases
A tentative decision cannot be relied on to impeach the judgment on appeal. Cal.Rules of Court, Rule 3.1590(b).

[32] Equity 150 ⚷65(1)

150 Equity
150I Jurisdiction, Principles, and Maxims
150I(C) Principles and Maxims of Equity
150k65 He Who Comes Into Equity Must Come with Clean Hands
150k65(1) k. In General. Most Cited Cases
The doctrine of unclean hands relates to misconduct occurring before the lawsuit was filed, not the bad faith filing or maintenance of an action.

[33] Antitrust and Trade Regulation 29T ⚷427

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk427 k. Defenses in General. Most Cited Cases

Equity 150 ⚷65(1)

150 Equity
150I Jurisdiction, Principles, and Maxims
150I(C) Principles and Maxims of Equity
150k65 He Who Comes Into Equity Must Come with Clean Hands
150k65(1) k. In General. Most Cited Cases
The doctrine of unclean hands does not apply to an action for unfair competition. West's Ann.Cal.Bus. & Prof.Code § 17200 et seq.

[34] Antitrust and Trade Regulation 29T ⚷438

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk438 k. Costs and Attorney Fees. Most Cited Cases

Constitutional Law 92 ⚷4018

92 Constitutional Law
92XXVII Due Process
92XXVII(E) Civil Actions and Proceedings
92k4017 Costs and Fees
92k4018 k. In General. Most Cited Cases

Costs 102 ⚷208

102 Costs
102IX Taxation
102k208 k. Duties and Proceedings of Taxing Officer. Most Cited Cases
Trial court acted within its discretion in declining to hold a post-trial hearing to address the issue of bad faith, before awarding attorney fees and costs to employees for employer's bad faith in bringing or

maintaining misappropriation of trade secrets action, where trial court did not exclude evidence before ruling on question of bad faith, trial court had already found objective speciousness and subjective bad faith and calendared the matter to determine reasonable attorney fees, and employer did not object to the briefing schedule or make an offer of proof that it had new evidence; employer had no due process right to retry the issue of bad faith. U.S.C.A. Const.Amend. 14; West's Ann.Cal.Civ.Code § 3426.4.

[35] Antitrust and Trade Regulation 29T 438

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk438 k. Costs and Attorney Fees. Most Cited Cases

Costs 102 2

102 Costs
102I Nature, Grounds, and Extent of Right in General
102k1 Nature and Grounds of Right
102k2 k. In General. Most Cited Cases

Costs 102 208

102 Costs
102IX Taxation
102k208 k. Duties and Proceedings of Taxing Officer. Most Cited Cases

Employer was not denied a meaningful opportunity to address sanctions, before trial court awarded attorney fees and costs to former employees for employer's bad faith in bringing or maintaining misappropriation of trade secrets action, where sanctions were discussed a few days after the action was filed, in the answer to the complaint, in opening statement, in closing statement, and in the post-trial briefs, and the trial court asked counsel to brief sanctions on the next-to-last day of trial. West's Ann.Cal.Civ.Code § 3426.4.

****311** Latham & Watkins; Daniel Scott Schecter, Charles Courtenay, Los Angeles, and Svetlana M. Berman, San Francisco; Bickel Brewer; William A. Brewer III and James S. Renard, Dallas, TX, for Appellants.

Wilson, Sonsini, Goodrich & Rosati; James A. DiBoise and Charles Tait Graves, San Francisco, for Respondents.

****312** YEGAN, P.J.

***1273** Appellants FLIR Systems, Inc. (FLIR) and Indigo Systems Corporation (Indigo) appeal from a judgment and post-judgment order awarding respondents William Parrish and Timothy Fitzgibbons $1,641,216.78 attorney fees and costs in a trade secret action. (Civ.Code, § 3426 et seq.) FN1 ***1274** THE TRIAL COURT FOUND THAT THE ACTION WAS FILED AND maintained in bad faith within the meaning of section 3426.4 of the California Uniform Trade Secrets Act. We affirm.

> FN1. Unless otherwise stated, all statutory references are to the Civil Code. The California Uniform Trade Secrets Act states: " 'Trade secret' means information, including a formula, pattern, compilation, program, device, method, technique, or process, that: [¶] (1) Derives independent economic value, actual or potential, from not being generally known to the public or to other persons who can obtain economic value from its disclosure or use; and [¶] (2) Is the subject of efforts that are reasonable under the circumstances to maintain its secrecy." (§ 3426.1, subd. (d).)

Facts

Indigo manufactures and sells microbolometers. A microbolometer is a device used in connection with infrared cameras, night vision, and thermal imaging. A significant portion of Indigo's technology was created by respondent William Parrish. FLIR manufactures and sells infrared cameras, night vision, and thermal imaging systems that use microbolometers. In 2004, FLIR purchased Indigo for approximately $185 million, acquiring Indigo's patents, technology, and intellectual property. Parish and Fitzgibbons were shareholders and officers of Indigo before the company was sold. After the sale, they continued working at Indigo.

In 2005, respondents decided to start a new company to mass produce bolometers and gave notice that they would quit Indigo on or about January 6, 2006. The new company was based on a business plan (Thermicon) developed by Fitzgibbons in 1998 and 1999 when he was self-employed.

Before leaving Indigo, respondents discussed allowing appellants to participate in Thermicon. Respondents proposed outsourcing bolometer production to a third party. The production startup time would be quick, assuming respondents could acquire technology licenses and intellectual property from a third party. Respondents offered FLIR a non-controlling interest in Thermicon. FLIR rejected the offer and wished respondents success in the new endeavor.

In early 2006, respondents entered into negotiations with Raytheon Company to acquire licensing, technology, and manufacturing facilities for Thermicon. Respondents assured appellants they would not misappropriate Indigo's trade secrets and that the new company would use an intellectual property filter similar to the one used at Indigo to prevent the misuse of trade secrets.

Fearful that the new business would undermine FLIR's market, appellants sued for injunctive relief and damages on June 15, 2006. The action was premised on the theory that respondents could not mass produce low-cost microbolometers based on the Thermicon time line without misappropriating trade secrets.

Upon learning of the lawsuit, Raytheon Company terminated business discussions with respondents. On August 15, 2006, respondents advised appellants that they were not going forward with the new business.

**1275 The Permanent Injunction Trial*

Appellants dismissed the damage causes of action and proceeded to trial for a permanent**313 injunction to enjoin respondents from: (1) making use of appellants' trade secrets in the design, manufacture, and high-volume production of uncooled Vanadium Oxide microbolometers; (2) selling uncooled Vanadium Oxide microbolometers in commercial markets less than 12 months after respondents entered into a license with Raytheon Company or any other third party to purchase intellectual property; or (3) using, disclosing or misappropriating the contents of an Indigo commodity code database that Parrish attempted to download while an employee at Indigo.

After eight days of testimony, the trial court found no misappropriation or threatened misappropriation of trade secrets. It was uncontroverted that respondents received no funding for Thermicon, did not start a new business, had no employees or customers, did not lease a facility or develop technology, and did not design, produce, sell, or offer to sell infrared products.

In a 25-page well-reasoned statement of decision, the trial court found that the action was brought in bad faith based on a theory of "inevitable disclosure," a doctrine not recognized by California courts because it contravenes a strong public policy of employee mobility that permits ex-employees to start new entrepreneurial endeavors. (See *Continental Car-Na-Var v. Moseley* (1944) 24 Cal.2d 104, 110, 148 P.2d 9; *Whyte v. Schlage Lock Co.* (2002) 101 Cal.App.4th 1443, 1462, 125 Cal.Rptr.2d 277.) Appellants were ordered to pay $1,352,000 attorney fees and $289,216.78 costs. (§ 3426.4.)

Section 3426.4 Fees: Trial Rules, and Appellate

Rules

[1][2] Section 3426.4 of the California Uniform Trade Secrets Act provides: "If a claim of misappropriation is made in bad faith, ... the [trial] court may award reasonable attorney's fees and costs to the prevailing party." Although the Legislature has not defined "bad faith," our courts have developed a two-prong standard: (1) objective speciousness of the claim, and (2) subjective bad faith in bringing or maintaining the action, i.e., for an improper purpose. (*Gemini Aluminum Corp. v. California Custom Shapes, Inc.* (2002) 95 Cal.App.4th 1249, 1262, 116 Cal.Rptr.2d 358 (*Gemini*).) Section 3426.4 authorizes the trial court to award attorney fees as a deterrent to specious trade secret claims. (*Id.,* at p. 1261, 116 Cal.Rptr.2d 358.) Because the award is a sanction, a trial court has broad discretion in awarding fees. (*Id.,* at p. 1262, 116 Cal.Rptr.2d 358.)

[3] On appeal from such an order, the appellant has an "uphill battle" and must overcome both the "sufficiency of evidence" rule and the "abuse of discretion" rule. We need not repeat these well-settled rules. (See ***1276***Estate of Gilkison* (1998) 65 Cal.App.4th 1443, 1448-1450, 77 Cal.Rptr.2d 463.) As we shall explain, appellant does not appear to appreciate the trial court's fact-finding power and its discretionary power to award attorney fees and costs to curtail a bad faith claim of trade secret misappropriation. We do not retry cases on appeal and we do not substitute our discretion for that of the trial court.

Objectively Specious

[4] Appellant argues that the first prong, i.e. objective speciousness, was not satisfied. Objective speciousness exists where the action superficially appears to have merit but there is a complete lack of evidence to support the claim. (*Gemini, supra,* 95 Cal.App.4th at p. 1261, 116 Cal.Rptr.2d 358; *CRST Van Expedited, Inc. v. Werner Enterprises* (9th Cir.2007) 479 F.3d 1099, 1112.)

****314** The trial court found that the action was objectively specious because appellants suffered no economic harm and there was no misappropriation or threatened misappropriation of trade secrets. It also found that respondents did not misappropriate the idea of outsourcing bolometer production to a third party and that the Thermicon business plan, which included a business forecast chart, did not misappropriate confidential information from appellants.

[5] Objective speciousness was established by evidence that appellants had an anticompetitive motive in filing the lawsuit. When asked why the action was filed, FLIR CEO Earl Lewis testified that "we can't tolerate a direct competitive threat by Bill [Parrish] and Tim [Fitzgibbons]." Lewis had no evidence of wrongdoing but was bothered that respondents planned to compete with FLIR in the future.

[6] Appellants argue that attorney fees may not be awarded unless the action is "frivolous," an objective standard used to impose Code of Civil Procedure section 128.5 sanctions. But the word "frivolous" does not appear in section 3426.4. "[S]ection 3426.4 requires objective speciousness of the plaintiff's claim, as opposed to frivolousness...." (*Gemini, supra,* 95 Cal.App.4th at p. 1262, 116 Cal.Rptr.2d 358.)

The evidence here supports the finding that appellants filed a specious action as a preemptive strike and for an anticompetitive purpose. The complaint alleges that appellants suffered "actual damages" and that respondents willfully and maliciously converted appellants' trade secrets "with the deliberate intent to injure [appellants'] business...." FN2 The evidence, ***1277** however, showed no "actual damages," misappropriation, or threatened misappropriation of trade secrets, and no threat of imminent harm.

FN2. The complaint alleges that Fitzgibbons, at a July 2004 board presentation to partner with FLIR, "effectively claimed

> ownership of FLIR's trade secrets" and "stated his intentions to proceed with a competing business based on such ideas, plans and information...." The complaint states that appellants were concerned about respondents' "brazen plan to use FLIR's confidential trade secrets" and that respondents willfully and deliberately breached non-compete agreements and proprietary agreements. None of these allegations were proven.

[7] The trial court ruled that the action was based on the doctrine of "inevitable disclosure" and violated public policy favoring employee mobility. (Bus. & Prof.Code § 16600; *Metro Traffic Control, Inc. v. Shadow Traffic Network* (1994) 22 Cal.App.4th 853, 859, 27 Cal.Rptr.2d 573; *Bayer Corp. v. Roche Molecular Systems, Inc.* (N.D.Cal.1999) 72 F.Supp.2d 1111, 1119-1120.) FN3 The doctrine of inevitable disclosure is not the law in California. (*Whyte v. Schlage Lock Co., supra,* 101 Cal.App.4th at p. 1447, 125 Cal.Rptr.2d 277 [inevitable disclosure injunction not permitted].) Sixty years ago our Supreme Court in *Continental Car-Na-Var Corp. v. Moseley, supra,* 24 Cal.2d at page 110, 148 P.2d 9, stated: "A former employee has ****315** the right to engage in a competitive business for himself and to enter into competition with his former employer, even for the business of those who had formerly been the customers of his former employer, provided such competition is fairly and legally conducted. [Citation.]"

> FN3. "Under the doctrine of inevitable disclosure, 'a plaintiff may prove a claim of trade secret misappropriation by demonstrating that defendant's new employment will inevitably lead him to rely on the plaintiff's trade secrets.' (*PepsiCo, Inc. v. Redmond* (7th Cir.1995) 54 F.3d 1262, 1269 (*PepsiCo*).) The inevitable disclosure doctrine results in an injunction prohibiting employment, not just use of trade secrets. The doctrine's justification is that unless the employee has 'an uncanny ability to compartmentalize information' the employee will necessarily rely-consciously or subconsciously-upon knowledge of the former employer's trade secrets in performing his or her new job duties. (Citation.)" (*Whyte v. Schlage Lock Co., supra,* 101 Cal.App.4th at pp. 1458-1459, 125 Cal.Rptr.2d 277.)

[8][9] Appellants admitted that respondents had the right leave to Indigo but claimed that respondents would misappropriate trade secrets if they started a new company. But speculation that a departing employee may misappropriate and use a trade secret in a startup business will not support an injunction. (*Continental Car-Na-Var v. Moseley, supra,* 24 Cal.2d at pp. 107-108, 148 P.2d 9 [injunction may not issue based on employer's speculation]; *GlobeSpan, Inc. v. O'Neill* (C.D.Cal.2001) 151 F.Supp.2d 1229, 1235 [same].) "A trade secrets plaintiff must show an actual use or an actual threat." (*Bayer Corp. v. Roche Molecular Systems, Inc., supra,* 72 F.Supp.2d at p. 1120.)

Missing here is evidence of misappropriation, threatened misappropriation, imminent harm, or on-going wrongdoing. William Sundermeier, president of a FLIR division, voted with FLIR CEO Lewis to file the lawsuit but had no ***1278** personal knowledge that respondents had committed a wrongful act. At trial, Sundermeier could not say why the lawsuit was still on-going a year and a half later.

Subjective Bad Faith

[10][11] Subjective bad faith may be inferred by evidence that appellants intended to cause unnecessary delay, filed the action to harass respondents, or harbored an improper motive. (*Gemini, supra,* 95 Cal.App.4th at p. 1263, 116 Cal.Rptr.2d 358.) The timing of the action may raise an inference of bad faith. (*Id.,* at pp. 1263-1264, 116 Cal.Rptr.2d 358.) Similar inferences may be made where the plaintiff proceeds to trial after the action's fatal shortcom-

ings are revealed by opposing counsel. (*Id.*, at p. 1264, 116 Cal.Rptr.2d 358.)

[12] Appellants suspected that trade secrets would be misappropriated and claim that a reasonable suspicion is evidence of good faith.[FN4] The trial court did not credit this theory, instead finding that appellants' reasons for bringing and maintaining the action were "inevitable disclosure" arguments. "In reviewing the facts which led the trial court to impose sanctions, we must accept the version thereof which supports the trial court's determination, and must indulge in the inferences which favor its findings. [Citations.]' [Citation.]" (*Gemini, supra,* 95 Cal.App.4th at pp. 1262-1263, 116 Cal.Rptr.2d 358.)

FN4. The statement of decision states that respondents, by their words or conduct, did not threaten imminent misuse of appellant's trade secrets or threaten immediate harm, "although the conduct of both of them raised a reasonable suspicion that they might misuse [appellants'] trade secrets." Appellants argue that "reasonable suspicion" bars a finding of subjective bad faith. The trial court correctly ruled that "reasonable suspicion" was not enough and that appellants were suing on an inevitable disclosure theory to prevent respondents from competing with FLIR.

Hard Drive Download

[13] Appellants contend there was a threatened misappropriation of trade secrets because Parrish downloaded technological data onto a portable hard drive before leaving Indigo. The information was stored on Indigo's computer network in a commodity code database for employee access.

Working on a project at Indigo, Parrish was frustrated about the slow computer network and copied the database to work ****316** at home. Parrish tried to use the hard drive but discovered that the database hyperlinks were broken and the data was not readable. Parrish left the hard drive at home and destroyed it in the spring of 2006 before the lawsuit was filed.

Parrish told Jim Woolaway, FLIR's Chief Intellectual Property Officer, about the download several months after the lawsuit was filed. Woolaway reported ***1279** the incident to his superiors. Thomas Surran, an Indigo executive, thereafter attempted to download the database on a hard drive and confirmed the hyperlinks did not work.

The hard drive download was not a consideration in bringing the action because appellants first learned of it after the complaint was filed. The trial court found that the download was not a threatened misappropriation because there was no evidence that the contents of the hard drive, "if such contents existed, were improperly accessed, used, or copied before the drive was destroyed."

[14] Appellants claim that the hard drive download is a "threatened" misappropriation under the California Uniform Trade Secrets Act. This is a restatement of the inevitable disclosure doctrine which is not the law in California. (*Whyte v. Schlage Lock Co., supra,* 101 Cal.App.4th at pp. 1463-1464, 125 Cal.Rptr.2d 277; Trade Secrets Practice in California (Cont.Ed.Bar 2d ed.2008) § 12.13, p. 486.) The trial court, in construing section 3426.2, properly found that a "threatened misappropriation" means a threat by a defendant to misuse trade secrets, manifested by words or conduct, where the evidence indicates imminent misuse. (See e.g., *Central Valley General Hosp. v. Smith* (2008) 162 Cal.App.4th 501, 527, 75 Cal.Rptr.3d 771 [imminent threat of misuse based on defendant's possession of trade secrets and prior misuse].)

Under appellants' construction of the law, an employer could bring a trade secret action after an employee downloads a company document and deletes the document from his or her laptop computer at home. A similar action could be brought where company messages are left on the employee's email or phone answering machine and deleted after the employee changes jobs.

[15][16] The California Uniform Trade Secrets Act requires an "[a]ctual or threatened misappropriation ...." (§ 3426.2, subd. (a).) Mere possession of trade secrets by a departing employee is not enough for an injunction. (*Central Valley General Hosp. v. Smith, supra,* 162 Cal.App.4th at pp. 528-529, 75 Cal.Rptr.3d 771; Trade Secrets Practice in California, *supra,* § 12.13, pp. 484-485.) " 'A trade secret will not be protected by the extraordinary remedy of an injunction on mere suspicion or apprehension of injury. There must be a substantial threat of impending injury before an injunction will issue....' [Citations.]" (*Del Monte Fresh Produce Co. v. Dole Food Co., Inc.* (S.D.Fla.2001) 148 F.Supp.2d 1326, 1328 [discussing California and Florida law].)

[17][18] Where the trade secrets plaintiff seeks a permanent injunction, section 3426.2, subdivision (c) "authorizes only injunctions that compel 'affirmative acts.' " It authorizes mandatory, not prohibitory injunctions, i.e., "mandatory injunctions requiring that a misappropriator return the fruits of misappropriation to an aggrieved person ... [Citation.] An order enjoining a remote threat or misuse or disclosure is prohibitory and does not necessarily compel affirmative acts. Thus such an injunction is not authorized by subdivision (c) of section 3426.2." ***1280**(*Central Valley General Hospital v. Smith, supra,* 162 Cal.App.4th at p. 530, 75 Cal.Rptr.3d 771; see Trade ****317** Secrets Practice in Calif., *supra,* § 12.13, p. 485.)

Although the complaint was for a permanent injunction, appellants did not seek an order compelling respondents to return anything. The hard drive was destroyed prior to trial. Respondents could not return anything because no trade secrets were misappropriated. "All that is alleged, at bottom, is that defendants could misuse plaintiff's secrets, and plaintiffs fear they will. That is not enough." (*Teradyne, Inc. v. Clear Communications Corp.* (N.D.Ill.1989) 707 F.Supp. 353, 357.)

Subjective bad faith was established by the contradictory testimony of appellants' executives who did not want to take responsibility for initiating and maintaining the action. Appellants' managers and employees testified that respondents were trustworthy, would not do anything wrong, and should have been allowed to start a new company.

Patent Applications

[19] Appellants argue that Parrish's objections to two Indigo patent applications created a reasonable suspicion that he would misappropriate trade secrets. Parrish held 25 patents and was the inventor of 11 or 12 patents while employed at Indigo.

After quitting Indigo, Parrish learned that appellants were submitting patent applications on a packaging and manufacturing process that he had worked on. Parrish told Woolaway, FLIR's Chief Intellectual Property Officer, that the patent applications were not valid. At trial, appellants claimed that Parrish's objection to the patent applications caused them to believe that trade secrets might be misappropriated.

Woolaway, who authored the patent applications, stated that the United States Patent & Trademark Office could go either way on the validity of the applications. Woolaway was concerned about Parrish's remarks but did not believe Parish would steal or misuse appellants' intellectual property. This testimony was echoed by appellants' officers and managers who stated that respondents were trustworthy and that an inventor's disagreement about a patent application did not signal a plot to steal trade secrets. The trial court ***1281** reasonably concluded that Parrish's objections to the patent applications was not a threatened misappropriation of a trade secret.

Trade Secret Experts

The trial court factually found that appellants maintained the action in bad faith with expert testimony that lacked a scientific basis and failed to address the possibility that respondents could lawfully acquire technology from Raytheon Company. Appellants claimed that respondents' plan to work with Raytheon Company was a contrivance and that Raytheon did not have the technology for mass-producing microbolometers. The trial court found that respondents' testimony, the testimony of a Raytheon official, and the Raytheon negotiation documents were credible and unrebutted. It concluded that the "contrivance" argument was asserted in bad faith to bolster a groundless action.

[20] Subjective bad faith was also established by appellants' failure to identify what trade secrets would be subject to the permanent injunction. Appellants' experts testified that appellants had a mix of trade secrets and non-secret information and that no list was prepared to identify the trade secrets. The trial court found that the proposed injunction was overbroad, did not give notice as to what was forbidden, and would harm respondents' reputation in the business community. (See e.g., ****318***MAI Systems Corp. v. Peak Computer, Inc.* (9th Cir.1993) 991 F.2d 511, 522-523 [permanent injunction failed to identify trade secrets with reasonable specificity]; *Advanced Modular Sputtering, Inc. v. Superior Court* (2005) 132 Cal.App.4th 826, 836, 33 Cal.Rptr.3d 901 [more particularity required in describing trade secrets in highly specialized technical field]; Trade Secrets Practice in California, *supra,* § 12.8, p. 476.) Among other things, the proposed injunction barred respondents from developing certain products for a 12 month period even if respondents did not use appellants' technology or trade secrets. It was an unlawful restraint on trade (Bus. & Prof.Code, § 16600) and strong evidence of subjective bad faith.

Bad Faith Settlement Tactics

The trial court further found that appellants maintained the action in bad faith by imposing unnecessary settlement conditions. In a July 14, 2005 settlement letter, respondents described their plan to acquire technology from a third party, restated that they would not misappropriate appellants' trade secrets, attached copies of Fitzgibbons' Thermicon business plan, and agreed to have a third party monitor and review the technology that respondents would develop. Appellants responded with the demand for $75,000, a non-competition agreement, an agreement that respondents would not hire appellants' employees, or challenge Indigo patent applications.

[21][22][23] ***1282** Woolaway, FLIR's Chief Intellectual Property Officer, was privy to the settlement discussions and testified that the $75,000 demand was "inflammatory." The trial court found that the other settlement terms were not related to the trade secret action and were made for an anticompetitive purpose. The condition that respondents not work with certain third party foundries was an unlawful trade restraint. (Bus. & Prof.Code, § 16600.) The condition that respondents not hire appellants' employees violated public policy (*ibid.*) as did the demand that Parrish not communicate relevant information to the federal government about the patent applications. (See 37 C.F.R. § 1.56; *Honeywell Intern., Inc. v. Universal Avionics Systems* (Fed.Cir.2007) 488 F.3d 982, 999 [applicants for patents have duty to prosecute patent applications with candor, good faith, and honesty].)

[24] A trial court, in awarding sanctions, may consider a party's dilatory tactics and bad faith settlement demands in maintaining the action. (§ 3426.4; *Gemini, supra,* 95 Cal.App.4th at p. 1263, 116 Cal.Rptr.2d 358; see e.g., *In re Marriage of Norton* (1988) 206 Cal.App.3d 53, 58-60, 253 Cal.Rptr. 354.) Here the settlement terms were inflammatory, violated public policy, and were made in bad faith.

Pre-Trial Motions

[25][26] Appellants argue that the trial court was estopped from finding bad faith because the court denied a motion for summary judgment, a motion in limine, and two nonsuit motions. In certain tort

actions, such as malicious prosecution, the denial of summary judgment normally precludes the trial court from finding that the lawsuit was frivolous. (See *Zamos v. Stroud* (2004) 32 Cal.4th 958, 973, fn. 10, 12 Cal.Rptr.3d 54, 87 P.3d 802.) "We say 'normally' rather than 'conclusively' because there may be situations where denial of summary judgment should not irrefutably establish probable cause. For example, if denial of summary judgment was induced by materially false facts submitted in opposition, equating denial with probable cause might be wrong. Summary judgment might have been granted but for the false evidence." ****319**(*Roberts v. Sentry Life Insurance* (1999) 76 Cal.App.4th 375, 384, 90 Cal.Rptr.2d 408.)

Appellants opposed the summary judgment motion with expert declarations suggesting there was a scientific methodology to predict the likelihood of trade secret misuse. The trial court found that respondents made a compelling argument for summary judgment but "the concepts involved in this action are highly technical." Erring on the side of caution, the trial court denied the summary judgment motion to see what would develop.

At trial, appellants' experts admitted there was no valid scientific methodology to predict trade secret misuse and agreed that no trade secrets were misappropriated. Both experts failed to address the possibility that respondents might lawfully acquire Raytheon's internal technology for the startup ***1283** business. One expert, Daniel Murphy, assumed that respondents would not innovate at the new company and incorrectly assumed that respondents planned to manufacture and sell bolometers in one year.

The trial court, in awarding sanctions, ruled: "The denial of the motion [for summary judgment] was not a ruling on whether [appellants] initiated or maintained the lawsuit in bad faith." The court denied the motion because it had not heard all the evidence or considered witness credibility.

Appellants cite no California authority that the denial of a summary judgment motion in a trade secret case precludes the trial court from finding, after it has heard all the evidence, that the action was brought or maintained in bad faith. (See *Waller v. TJD, Inc.* (1993) 12 Cal.App.4th 830, 836, 16 Cal.Rptr.2d 38 [order denying summary judgment is not a basis to reverse a judgment entered after trial on the merits]; Weil & Brown, Cal. Practice Guide, Civil Procedure Before Trial (The Rutter Group 2008) ¶ 10:364, p. 10-129.) If the rule was otherwise, a trade secrets plaintiff could file sham declarations to successfully oppose a summary judgment motion and immunize itself from sanctions.

[27][28][29] Under the California Uniform Trade Secret Act, sanctions may be awarded for the bad faith filing *or* maintenance of a groundless action. (*Gemini, supra,* 95 Cal.App.4th at pp. 1261-1262, 116 Cal.Rptr.2d 358.) A trade secrets claim could be brought in good faith but warrant attorney fees were the claim is pursued beyond a point where the plaintiff no longer believes the case has merit. (See *Yield Dynamics, Inc. v. TEA Systems Corp.* (2007) 154 Cal.App.4th 547, 579, fn. 20, 66 Cal.Rptr.3d 1 [discussed but not decided].) " 'Bad faith may be inferred where the specific shortcomings of the case are identified by opposing counsel, and the decision is made to go forward despite the inability to respond to the arguments raised.' [Citation.]" (*Gemini, supra,* 95 Cal.App.4th at p. 1264, 116 Cal.Rptr.2d 358.) The trial court reasonably inferred that appellants knew there was no misappropriation or threatened misappropriation of trade secrets before the summary judgment motion was argued.

In *Gemini,* the Court of Appeal rejected the argument that lack of bad faith was established by the denial of a nonsuit motion. (*Gemini, supra,* 95 Cal.App.4th at p. 1264, fn. 6, 116 Cal.Rptr.2d 358.) The same principle applies here. At trial, appellants' experts conceded there was no accepted scientific methodology for predicting the misuse of trade secrets and made false assumptions that respondents would not innovate new technology or acquire technology from a third party. The trial court found that appellants used expert testimony to "unreasonably discount[ ] ways in which Defendants could **320 have proceeded with the new company lawfully." The award for sanctions was proper. It is well settled that "[n]o one can take advantage of his own wrong." (§ 3517.)

[30][31][32][33] *1284 Appellants assert that the tentative statement of decision includes a finding that respondents did not prevail on an unclean hands defense, thus precluding the trial court from finding the action was brought in bad faith. The argument fails for several reasons. First, a tentative statement of decision is not binding on the trial court and can be modified or changed as the judge sees fit before entry of judgment. (Cal. Rules of Court, rule 3.1590(b); *Horning v. Shilberg* (2005) 130 Cal.App.4th 197, 203, 29 Cal.Rptr.3d 717.) A tentative decision cannot be relied on to impeach the judgment on appeal. (*In re Marriage of Ditto* (1988) 206 Cal.App.3d 643, 646-647, 253 Cal.Rptr. 770.) Second, the doctrine of unclean hands relates to misconduct occurring before the lawsuit was filed, not the bad faith filing or maintenance of an action. (See e.g., *Smoketree-Lake Murray, Ltd. v. Mills Concrete Construction Co.* (1991) 234 Cal.App.3d 1724, 1743-1744, 286 Cal.Rptr. 435.) Moreover, the doctrine of unclean hands does not apply to an action for unfair competition, alleged here as an alternative theory for injunctive relief. (See *Cortez v. Purolator Air Filtration Products Co.* (2000) 23 Cal.4th 163, 179-180, 96 Cal.Rptr.2d 518, 999 P.2d 706.) "Courts have long held that the equitable defense of unclean hands is not a defense to an unfair trade or business practices claim based on violation of a statute." (*Ticconi v. Blue Shield* (2008) 160 Cal.App.4th 528, 543, 72 Cal.Rptr.3d 888.)

Post-Trial Bad Faith Hearing

[34] Appellants contend that the trial court erred in not conducting a post-trial hearing to address the issue of bad faith. In *Yield Dynamics, Inc. v. TEA Systems Corp., supra,* 154 Cal.App.4th 547, 66 Cal.Rptr.3d 1, the trial court excluded evidence, proffered after trial, that the trade secrets action was filed in good faith. The Court of Appeal held that it was error because "[t]he subjective element of bad faith ... might be proved or refuted by evidence that would have been wholly irrelevant at trial." (*Id.*, at p. 579, 66 Cal.Rptr.3d 1.)

Unlike *Yield Dynamics Inc. v. TEA Systems Corp., supra,* here the trial court did not exclude evidence before ruling on the question of bad faith. Appellants' request for a post-trial hearing was denied because the court had received voluminous briefing and had already found objective and subjective bad faith. Appellants did not object to the briefing schedule or make an offer of proof that they had new evidence.

[35] The assertion that appellants were denied a meaningful opportunity to address sanctions is equally without merit. Sanctions were discussed a few days after the action was filed, in the answer to the complaint, in opening *1285 statement, in closing statement, and in the post-trial briefs. On the next-to-last day of trial, the trial court asked counsel to brief sanctions and the inevitable disclosure doctrine which was "the heart of the case." Appellants' post-trial brief devoted 10 pages to sanctions and stated: " Throughout trial, Defendants consistently claimed that they would prove that Plaintiffs brought this action in bad faith."

A fair reading of the 25 page judgment and statement of decision with citations to the pleadings, to discovery, to the settlement discussions, to the pretrial motions, and to the trial evidence obviated any need for a further hearing. The complaint states that appellants were entitled to a **321 permanent injunction and punitive damages yet FLIR's CEO, Earl Lewis, had no evidence that respondents had engaged in wrongdoing.

Lewis's testimony is remarkable and clearly shows that the action was brought for an anti-competitive purpose. Lewis did not "think it would be good, healthy for them [respondents] to go and directly compete with us." Lewis stated that FLIR "couldn't tolerate a direct competitive threat by [respondents] because it would fly in the face of everything that we spent 200 million dollars to buy." Lewis's statements were corroborated by FLIR Senior Vice President Tony Trunzo who testified that respondents' "vision for the industry will take place someday" but FLIR "wanted that competition to take place as far out in the future as possible."

The trial court reasonably concluded that further briefing or post-trial testimony on the question of bad faith would be repetitive and unnecessary. It had already found objective speciousness and subjective bad faith and calendared the matter to determine reasonable attorney fees.[FN5] Appellants did not file a motion for new trial and had no due process right to retry the issue of bad faith.

> FN5. Respondents moved for $2,399,650.55 attorney fees and were awarded $1,352,000 fees plus $289,216.78 costs. The order granting fees and costs recites the following bad faith findings which were previously made in the statement of decision: "Plaintiffs initiated and continued to pursue this action against Defendants in bad faith and primarily for the anticompetitive motive of preventing Defendants from attempting to create a new business in competition with Plaintiffs.... Plaintiffs engaged in subjective and objective bad faith.... Plaintiffs' suspicions regarding Defendants were not sufficient to justify the filing of the lawsuit on June 15, 2006, or the maintenance of the lawsuit through trial in December 2007.... Plaintiffs initiated and maintained the lawsuit in bad faith in that Plaintiffs proceeded on a legal theory that Defendants would misuse trade secret[s] in the future, and that 'inevitable disclosure' type of theory is not supported by California law.... The Court finds that plaintiffs' theory for initiating the lawsuit, as described in Mr. Lewis's testimony is not consistent with California law ... [and] Plaintiffs continued the lawsuit in bad faith [after] Defendants notified Plaintiffs of problems in Plaintiffs' case...."

***1286** *Conclusion*

Appellants' remaining arguments merit no further discussion.

The judgment and order awarding respondents $1,641.216.78 attorney fees and costs are affirmed. (§ 3426.4.) Respondents are awarded costs and attorney fees on appeal, in an amount to be determined by the trial court on noticed motion. (*Gemini, supra,* 95 Cal.App.4th at pp. 1264-1265, 116 Cal.Rptr.2d 358.)

We concur: COFFEE and PERREN, JJ.
Cal.App. 2 Dist.,2009.
FLIR Systems, Inc. v. Parrish
174 Cal.App.4th 1270, 95 Cal.Rptr.3d 307, 29 IER Cases 441, 09 Cal. Daily Op. Serv. 7448, 2009 Daily Journal D.A.R. 8599

END OF DOCUMENT

TAB 4

Only the Westlaw citation is currently available.

United States District Court,
D. Maryland.
GLYNN INTERACTIVE, INC.
v.
ITELEHEALTH, INC.
No. Civ.A. DKC2003-0449.

March 9, 2004.

Vernon W Johnson, III, Jackson and Campbell PC, Washington, DC, for Plaintiff.

Craig Benson Young, William C Bergmann, Connolly Bove Lodge and Hutz LLP, Washington, DC, for Defendant.

MEMORANDUM OPINION

CHASANOW, J.

*1 Presently pending and ready for resolution in this breach of contract and tort case are the motions (1) by Defendant iTelehealth, Inc. for partial summary judgment and (2) by Plaintiff Glynn Interactive, Inc. to seal the exhibits in its opposition to Defendant's partial summary judgment motion. The issues have been fully briefed and the court now rules, no hearing being deemed necessary. Local Rule 105.6. For the reasons that follow, the court will grant in part the motion for partial summary judgment and will deny the motion to seal.

I. Background

A. Factual Background

The following are facts either uncontroverted or viewed in the light most favorable to Plaintiff Glynn Interactive, Inc. On May 7, 2002, Plaintiff and Defendant iTelehealth, Inc. entered into a Prime/Subcontractor Teaming Agreement (Teaming Agreement) to submit a proposal in response to a grant solicitation issued by the National Institutes of Mental Health (NIMH). Under the Teaming Agreement, Defendant was designated as the prime contractor responsible for preparing and submitting the proposal to NIMH, while Plaintiff was designated as the subcontractor to assist Defendant in the work.

Defendant submitted the proposal for the grant to NIMH, which subsequently accepted the proposal. Defendant entered into a contract with NIMH on September 26, 2002. During October and November 2002, Plaintiff and Defendant attempted to negotiate a subcontract in order to perform the web design work under the NIMH contract awarded to Defendant, but these efforts failed. On November 17, 2002, Defendant notified Plaintiff by certified mail to cease all performance of work in connection with the NIMH contract. Following the failure to execute a subcontract, Defendant then hired another web designer to replace Plaintiff.

B. Procedural Background

On January 15, 2003, Plaintiff filed a complaint in the Circuit Court for Montgomery County, alleging: (1) breach of contract, (2) unjust enrichment, (3) account stated, (4) copyright infringement, and (5) misappropriation of trade secrets. Defendant subsequently removed the case to this court. On July 24, 2003, Defendant moved for partial summary judgment, pursuant to Fed.R.Civ.P. 56(b), on all claims except unjust enrichment.

II. Standard of Review

It is well established that a motion for summary judgment will be granted only if there exists no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. *See* Fed.R.Civ.P. 56(c); *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 250, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986); *Celotex Corp. v. Catrett,* 477 U.S. 317, 322, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986). In other words, if there clearly exist factual issues "that properly can be resolved only by a finder of fact because they may reasonably be resolved in favor of either party," then summary judgment is inappropriate. *Anderson,* 477 U.S. at 250; *see also* Pulliam Inv. Co. v. *Cameo Properties,* 810 F.2d 1282, 1286 (4th

Cir.1987); *Morrison v. Nissan Motor Co.,* 601 F.2d 139, 141 (4th Cir.1987). The moving party bears the burden of showing that there is no genuine issue as to any material fact and that he is entitled to judgment as a matter of law. *See* Fed.R.Civ.P. 56(c); *Catawba Indian Tribe of South Carolina v. State of S.C.,* 978 F.2d 1334, 1339 (4th Cir.1992), *cert. denied,* 507 U.S. 972, 113 S.Ct. 1415, 122 L.Ed.2d 785 (1993).

*2 When ruling on a motion for summary judgment, the court must construe the facts alleged in the light most favorable to the party opposing the motion. *See U.S. v. Diebold,* 369 U.S. 654, 655, 82 S.Ct. 993, 8 L.Ed.2d 176 (1962); *Gill v. Rollins Protective Servs. Co.,* 773 F.2d 592, 595 (4th Cir.1985). A party who bears the burden of proof on a particular claim must factually support each element of his or her claim. "[A] complete failure of proof concerning an essential element ... necessarily renders all other facts immaterial." *Celotex Corp.,* 477 U.S. at 323. Thus, on those issues on which the nonmoving party will have the burden of proof, it is his or her responsibility to confront the motion for summary judgment with an affidavit or other similar evidence in order to show the existence of a genuine issue for trial. *See Anderson,* 477 U.S. at 256; *Celotex Corp.,* 477 U.S. at 324. However, "[a] mere scintilla of evidence in support of the nonmovant's position will not defeat a motion for summary judgment." *Detrick v. Panalpina, Inc.,* 108 F.3d 529, 536 (4th Cir.), *cert. denied sub nom., Gold v. Panalpina, Inc.,* 522 U.S. 810, 118 S.Ct. 52, 139 L.Ed.2d 17 (1997). There must be "sufficient evidence favoring the nonmoving party for a jury to return a verdict for that party. If the evidence is merely colorable, or is not significantly probative, summary judgment may be granted." *Anderson,* 477 U.S. at 249-50 (citations omitted).

III. Analysis

A. Breach of Contract

The Teaming Agreement appears to serve as the basis for this claim.[FN1] Plaintiff claims that Defendant's decisions not to pay it the purported amount due and to hire another subcontractor after negotiations stalled constitute a breach of contract. Defendant, on the other hand, contends that the Teaming Agreement was merely a letter of intent to form a subcontract if and when Defendant received the NIMH grant.

FN1. Count I, entitled breach of contract, seeks $500,000 in damages and asserts that "Glynn entered into an agreement with iTelehealth, whereby defendant agreed to pay Glynn for services rendered, including labor and materials furnished, on various endeavors, and iTelehealth agreed to use Glynn as subcontractor on those and other endeavors." Paper 1 at ¶ 13. The only written contract attached to the complaint is the Teaming Agreement.

The language of the Teaming Agreement makes clear, in numerous provisions, that the document is not contractually binding beyond the proposal submission phase and contemplates future negotiations between the parties. For instance, the Teaming Agreement states that Plaintiff and Defendant will enter into a subcontract "subject to mutual agreement on prices and other terms and conditions." Paper 27, Ex. 4 at ¶ 2.1. Another paragraph provides that the Teaming Agreement shall terminate upon, *inter alia,* the "[i]nability of the Parties negotiating in good faith to reach agreement on the terms of a subcontract in accordance with this Agreement." Paper 27, Ex. 4 at ¶ 3.1.d. Finally, the Teaming Agreement is explicit that in the event it should be terminated, "either party shall be free to pursue its individual technical approach in association with the successful contractor or a third party for work which is the subject of this Agreement." Paper 27, Ex. 4 at ¶ 5.3.

Courts generally do not regard letters of intent, such as the portion of the Teaming Agreement at issue here, as binding contracts and thus do not enforce them "because traditionally, the purpose and function of a preliminary letter of intent has been to merely provide the initial framework from which the parties might later negotiate a final binding agreement." *Burbach Broad. Co. of Delaware v. Elkins Radio Corp.,* 278 F.3d 401, 406 (4th Cir.2002).[FN2] For a letter of intent to bind the parties, "it must expressly indicate the parties' intention to be bound by the document." *Abt Assoc., Inc. v. JHPIEGO Corp.,* 104 F.Supp.2d 523, 532 (D.Md.2000), *aff'd,* 9 Fed.Appx. 172 (4th Cir.2001) (unpublished disposition). Plaintiff cannot, and does not, point to any such indication of intent in the Teaming Agreement.

FN2. In support of its position, Plaintiff asserts that "the term 'letter of intent' does not even appear in the document." Paper 30 at 20. Although perhaps helpful signals of the parties' intentions, "[l]abels such as 'letter of intent' or 'commitment letter' are not necessarily controlling." Burbach Broad., 278 F.3d at 406.

*3 Moreover, the Teaming Agreement contains a host of open terms to the subcontract, most notably the amount Defendant was to pay Plaintiff for the services to be rendered. *See* Paramount Brokers, Inc. v. Digital River, Inc., 126 F.Supp.2d 939, 947 (D.Md.2000) (no binding contract where express condition of letter of intent "was that the parties' understanding was 'subject to reaching an agreement ... in regards to pricing and commissions" '); *Phoenix Mut. Life Ins. Co. v. Shady Grove Plaza Ltd. P'ship,* 734 F.Supp. 1181, 1187 (D.Md.1990), *aff'd,* 937 F.2d 603 (4th Cir.1991) (Table). That the parties could not agree on the terms and conditions of the subcontract during their negotiations after Defendant's receipt of the NIMH grant "is significant evidence that there was no prior binding contractual relationship between them." *Abt Assoc.,* 104 F.Supp.2d at 532.[FN3]

FN3. Plaintiff mistakenly relies on a Third Circuit case, *ATACS Corp. v. Trans World Communications, Inc.,* 155 F.3d 659 (3d Cir.1998), in its argument that Defendant should be bound by the Teaming Agreement. Although the *ATACS* court noted that courts generally permit a breach of contract action based solely on a teaming agreement, it cautioned that the party relying on the teaming agreement, as Plaintiff here, must overcome "two major obstacles: (1) the intent of the parties to enter into a binding contractual relationship; and (2) the existence of sufficiently objective criteria to enforce." *Id.* at 666 (noting that parties often "may reach an understanding to team, but fail to execute a subcontract as anticipated in the teaming agreement").

Plaintiff's complaint does not allege a breach of the Teaming Agreement by bad faith negotiations concerning the terms of a subcontract. Rather, Plaintiff claims that the Teaming Agreement itself constitutes a binding contract. Plaintiff's mere assertion, without more, that there exists "a factual dispute as to what the parties intended in entering into the Teaming Agreement" is not sufficient to withstand summary judgment. Paper 30 at 20. Indeed, the explicit, unequivocal language of the Teaming Agreement eliminates any dispute here; a breach of contract action cannot lie based on the parties' failure to agree on a mutually satisfactory subcontract. The only agreement here, the Teaming Agreement, contained no binding terms governing the work performed by Plaintiff after the bid proposal phase and while the parties attempted to negotiate the subcontract. Accordingly, Defendant's motion for summary judgment on the breach of contract claim will be granted.

B. Account Stated

Under Maryland law, "[a]n account stated is an agreement between the parties who have had previous transactions of a monetary character that all the items of the account representing such transactions, and the balance struck, are correct, together with a promise, express or implied, for the payment of such a balance." *Radio Parts Co. v. Lowry,* 125 B.R. 932, 944 (D.Md.1991) (quoting *Wathen v. Pearce,* 175 Md. 651, 661, 3 A.2d 486, 491 (1939)). An "indispensable ingredient" of an account stated is "an assent on the part of the person sought to be charged that the balance struck is the true measure of his indebtedness to the plaintiff." *Wathen,* 3 A.2d at 491. Absent such assent, "there can be no account stated." *Radio Parts,* 125 B.R. at 944.

Plaintiff bases its account stated claim on multiple invoices for purported work it performed in connection with the NIMH grant, claiming that Defendant is liable for a balance of $248,894.04 as a result of its delay in responding to "the stated balance within a reasonable time." Paper 2 at ¶ 29. Plaintiff does not offer any evidence to support its allegation. In fact, upon failure to execute a subcontract, Defendant offered to pay half of the first invoice of $6,898 to help "reach an equitable conclusion" between the parties. Paper 27, Ex. 12. This compromise offer demonstrates that Defendant never agreed to pay the total of the invoices, so as to hold it liable for an account stated. [FN4] Accordingly, Defendant's motion for summary judgment on the account stated claim will be granted.

FN4. Plaintiff contends that the settlement offer is inadmissible under Fed.R.Evid. 408. However, Rule 408 permits introduction of

> such evidence in order to "negativ[e] a contention of undue delay." Fed.R.Evid. 408. Thus, Defendant may proffer this evidence to contravene Plaintiff's argument that the two-month lapse between delivery of the invoice and settlement offer is sufficient to establish an account stated. *See Bituminous Constr., Inc. v. Rucker Enter., Inc.,* 816 F.2d 965, 968 (4th Cir.1987) (exclusion of evidence under Rule 408 required "only if the evidence is offered to prove either liability for or invalidity of a claim or its amount").

C. Copyright Infringement

***4** Plaintiff alleges that Defendant infringed on the copyright for its web design mock-ups constructed for the anticipated subcontracting relationship between the parties. In Count IV, Plaintiff states that it "has complied in all respects with the Copyright Act of 1976" and seeks injunctive relief, statutory damages up to $150,000.00, other damages, attorney's fees and costs. The Copyright Act requires the registration of a copyright before filing an action for copyright infringement. *See* 17 U.S.C. § 411(a); *Xoom, Inc. v. Imagineline, Inc.,* 323 F.3d 279, 283 (4th Cir.) ("Copyright registration is a jurisdictional prerequisite to bringing an action for infringement under the Copyright Act"), *cert. denied,* 540 U.S. 879, 124 S.Ct. 303, 157 L.Ed.2d 143 (2003). A certificate of copyright registration is "prima facie evidence of the validity of the copyright and [of] the facts stated in the certificate." *Serv. & Training, Inc. v. Data Gen. Corp.,* 963 F.2d 680, 688 (4th Cir.1992) (quoting 17 U.S.C. § 410(c)). *See also Lowery Reports, Inc. v. Legg Mason, Inc.,* 271 F.Supp.2d 737, 744 (D.Md.2003) ("As proof of ownership, [plaintiff] submits the certificates of copyright registration for all of the *Reports* at issue").

Plaintiff has not produced a certificate of copyright registration for any of the alleged copyrighted works in this action, so as to demonstrate ownership of a valid copyright. Instead, Laura Glynn, president of Plaintiff, states in a declaration that Plaintiff has filed "the necessary registration" for the copyright. Paper 30, Ex. A at ¶ 18. While some courts have held that submission of registration materials suffices to maintain a copyright infringement claim, others require either the issuance of a registration or an official refusal to do so. *See Strategy Source, Inc. v. Lee,* 203 F.Supp.2d 1, 2 (D.D.C.2002) (collecting cases). Plaintiff does not allege that the Copyright Office has issued a certificate of registration. Indeed, the record here is unclear as to exactly what Plaintiff has done with regard to registering its purported copyright.

Even if Plaintiff submitted sufficient evidence of copyright registration, it still would be precluded from recovering the statutory damages and attorney's fees that it seeks. The Copyright Act bars the award of statutory damages and attorney's fees where the alleged infringement of the copyright on an unpublished work "commenced before the effective date of its registration." 17 U.S.C. § 412(1). *See also Bouchat v. Baltimore Ravens Football Club, Inc.,* 346 F.3d 514, 517 n. 2 (4th Cir.2003) (plaintiff "not entitled to pursue statutory damages because the infringement was of an unpublished work and preceded copyright registration," citing § 412(1)); *Berlyn, Inc. v. The Gazette Newspapers, Inc.,* 157 F.Supp.2d 609, 623-24 (D.Md.2001). In this case, Plaintiff admits that it filed for copyright registration only after commencement of this litigation-and thus, necessarily, after any alleged infringement by Defendant. *See* Paper 30, Ex. A at ¶ 18 .[FN5] Defendant has indicated that it will not be making use of Plaintiff's designs in connection with the NIMH grant, as it already has executed an agreement with another subcontractor, and in fact "offer[ed] to sign any paperwork to that effect." Paper 27, Ex. 12.

> FN5. Laura Glynn also states in the declaration that Plaintiff discovered its failure to register a copyright "after this Motion was filed." Paper 30, Ex. A at ¶ 18. The court will presume that the "Motion" referred to by Ms. Glynn is the Plaintiff's opposition to Defendant's partial summary judgment motion, to which Plaintiff attached the declaration and filed on August 11, 2003. Thus, Plaintiff theoretically would not have a valid copyright infringement claim, at the earliest, until after that date. This acknowledgment by Plaintiff contravenes its assertion in the complaint that it had fully complied with the Copyright Act at the time it filed suit.

***5** For the reasons articulated, *supra,* Plaintiff cannot seek statutory damages or attorney's fees. Accordingly, Defendant's motion for summary judgment on the copyright infringement claim will be granted in part. If Plaintiff indeed has any evidence of actual damages (assuming proper registration), it may pursue its claim of copyright infringement in that vein. The court will direct Plaintiff to provide an update on the copyright registration process at the status conference, discussed *infra.*

D. Misappropriation of Trade Secrets

Plaintiff alleges that Defendant misappropriated its web design mock-ups, as trade secrets, in violation of the Maryland Uniform Trade Secrets Act (MUTSA), Md.Com.Law II Code Ann. §§ 11-1201 *et seq.* As an initial matter, Plaintiff bears the burden "of producing *some* evidence that these items met the definition of a trade secret." Trandes Corp. v. Guy F. Atkinson Co., 996 F.2d 655, 661 (4th Cir.) (emphasis in original), *cert. denied,* 510 U.S. 965, 114 S.Ct. 443, 126 L.Ed.2d 377 (1993). To do so, Plaintiff must "describe the subject matter of its alleged trade secrets in sufficient detail to establish each element of a trade secret." *Id.* (plaintiff "had to do more than merely allege that it had a secret").[FN6] Plaintiff's claim, without more, that "[t]he trade secrets involved include the type of expertise and information provided by Glynn to iTelehealth" lacks such sufficient detail. Paper 30 at 26. Again, Plaintiff's claim devoid of particularity, along with the equally bald assertion that "there are factual disputes on this issue," is not enough to save Plaintiff's trade secret claim from summary judgment.

FN6. Under MUTSA-

(e) "Trade secret" means information, including a formula, pattern, compilation, program, device, method, technique, or process, that:

(1) Derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use; and

(2) Is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

Md.Com.Law II Code Ann. § 11-1201(e).

Even assuming that it could prove the existence of a trade secret, Plaintiff still must show that Defendant misappropriated the secret information pursuant to MUTSA, by demonstrating that Defendant "used improper means to acquire from [Plaintiff] the information currently in [Defendant's] possession." *DTM Research, L.L.C. v. AT & T Corp.,* 245 F.3d 327, 333 (4th Cir.2001) (citing §§ 11-1201(b),(c)).[FN7] Plaintiff points to Defendant's alleged breach of contract based on the Teaming Agreement-a claim the court already has discussed and dismissed, *supra*-as evidence that Defendant engaged in "a clear abuse of confidence and impropriety." Paper 30 at 26. Moreover, the Teaming Agreement expressly provides that "[d]uring the preparation of the proposal, certain technical and other information deemed proprietary and confidential by the Parties may be disclosed to the other party." Paper 27, Ex. 4 at ¶ 4.1. Therefore, any alleged trade secret information obtained by Defendant while preparing the proposal was knowingly and voluntarily provided by Plaintiff. This evidence falls well short of that necessary to establish misappropriation. Accordingly, Defendant's motion for summary judgment on the misappropriation of trade secrets claim will be granted.

FN7. Under MUTSA-

(c) "Misappropriation" means the:

(1) Acquisition of a trade secret of another by a person who knows or has reason to know that the trade secret was acquired by improper means; or

(2) Disclosure or use of a trade secret of another without express or implied consent by a person who:

(i) Used improper means to acquire knowledge of the trade secret; or

(ii) At the time of disclosure or use, knew or had reason to know that the person's knowledge of the trade secret was:

1. Derived from or through a person who had utilized improper means to acquire it;

2. Acquired under circumstances giving rise to a duty to maintain its secrecy or limit its use; or

3. Derived from or through a person who owed a duty to the person seeking relief to maintain its secrecy or limit its use; or

(iii) Before a material change of the person's position, knew or had reason to know that it was a trade secret and that knowledge of it had been acquired by accident or mistake.

Md.Com.Law II Code Ann. § 11-1201(c).

IV. Plaintiff's Motion to Seal

***6** Plaintiff has moved to seal the 40 exhibits it attached to its opposition to Defendant's partial summary judgment motion, on the principal ground that the many of the exhibits "reflect issues that involve trade secret, confidential, and proprietary information of the parties as well as copyrighted materials not for public dissemination." Paper 31 at ¶ 3. The court already has found that Plaintiff failed to establish that it possessed any trade secrets in this action. Moreover, these exhibits do not appear to contain any such confidential information-and Plaintiff points to none-that warrant placing them under seal. *Cf.* Padco Advisors, Inc. v. *Omdahl,* 179 F.Supp.2d 600, 614-15 (D.Md.2002) (granting parties' motions to seal where action was "based on enforcing a non-compete clause in an employment contract in order to protect these trade secrets"). Accordingly, Plaintiff's motion to seal will be denied.

Along with its motion for partial summary judgment, Defendant attached a notice that it was filing two supporting exhibits under seal. However, Defendant failed to file a motion to seal those exhibits, as required in the Stipulated Order Regarding Confidentiality of Discovery Material. *See* Paper 24 at ¶ 2. Accordingly, these exhibits will be treated as unsealed. Indeed, none of the exhibits filed by Plaintiff or Defendant in this action are sealed.

V. Remaining Claims

Discovery is complete in this case and, as a result, Plaintiff's claim for unjust enrichment appears ready for trial. Additionally, in its answer, Defendant filed counterclaims for (1) breach of contract, (2) unjust enrichment, and (3) theft of trade secrets. To date, Plaintiff has not yet responded substantively to these counterclaims. The court will schedule a telephone conference between the parties to discuss the status of this particular matter, as well as that of Plaintiff's copyright infringement claim with regard to potential actual damages.

VI. Conclusion

For the foregoing reasons, the court will grant in part Defendant's motion for partial summary judgment and will deny Plaintiff's motion to seal the exhibits in its opposition to Defendant's partial summary judgment motion. The court also will schedule a telephone conference between the parties to discuss the status of Defendant's counterclaims and any remaining copyright claim. A separate Order will follow.

ORDER

For the reasons stated in the foregoing Memorandum Opinion, it is this 9th day of March, 2004, by the United States District Court for the District of Maryland, ORDERED that:

1. The motion by Defendant iTelehealth, Inc. for partial summary judgment (Paper 27) BE, and the same hereby IS, GRANTED IN PART and DENIED IN PART;

2. Judgment BE, and the same hereby IS, ENTERED in favor of Defendant iTelehealth, Inc. and against Plaintiff Glynn Interactive, Inc. on the claims for breach of contract, account stated, statutory damages and attorney's fees for copyright infringement, and misappropriation of trade secrets;

***7** 3. The motion by Plaintiff to seal the exhibits in its opposition to Defendant's partial summary judgment motion (Paper 31) BE, and the same hereby IS, DENIED;

4. The parties are directed to file electronically within 10 days a notice attaching the exhibits that each previously sought to have sealed;

5. Plaintiff's claim for unjust enrichment appears ready for trial;

6. A telephone conference will be held on March 22, 2004, at 9:00 a.m. to set a trial date and to discuss the status of Defendant's counterclaims and any remaining copyright claim (counsel should notify chambers of the telephone number where they can be reached at that time); and

7. The Clerk will transmit copies of this Memorandum Opinion and this Order to counsel for the parties.

D.Md.,2004.
Glynn Interactive, Inc. v. iTelehealth, Inc.
Not Reported in F.Supp.2d, 2004 WL 439236 (D.Md.)

END OF DOCUMENT

TAB 5

H

United States Court of Appeals,
Tenth Circuit.
Anthony HEUSER and Nona Heuser, Plaintiffs-Appellants,
v.
Frank KEPHART; Farmington Utility System; Jack McQuitty, Code Compliance Officer; Stephen Hrzich, City Electrical Inspector, City of Farmington; James Cheverie, Roger Lasater, San Juan County Board of County Commissioners, Defendants-Appellees.
No. 98-2233.

June 30, 2000.

Customers of city electrical utility brought § 1983 action against county and city officials alleging constitutional violations in connection with denial of electrical services. The United States District Court for the District of New Mexico, Martha Vasquez, J., dismissed action pursuant to putative settlement agreement. Customers appealed. The Court of Appeals, Holloway, Circuit Judge, held that putative agreement settling action, stating that officials' counsel would recommend that officials pay certain amount to settle action, set forth illusory promise.

Reversed and remanded.

Ebel, Circuit Judge, dissented and filed opinion.

West Headnotes

[1] Federal Courts 170B ⚷813

170B Federal Courts
170BVIII Courts of Appeals
170BVIII(K) Scope, Standards, and Extent
170BVIII(K)4 Discretion of Lower Court
170Bk813 k. Allowance of Remedy and Matters of Procedure in General. Most Cited Cases

A district judge's approval of a settlement agreement is reviewed for an abuse of discretion.

[2] Compromise and Settlement 89 ⚷3

89 Compromise and Settlement
89I In General
89k1 Nature and Requisites
89k3 k. Subject-Matter. Most Cited Cases

Compromise and Settlement 89 ⚷6(1)

89 Compromise and Settlement
89I In General
89k1 Nature and Requisites
89k6 Consideration
89k6(1) k. Necessity and Sufficiency in General. Most Cited Cases

Under federal or New Mexico law, putative agreement settling electrical customers' action alleging constitutional violations by county and city officials in connection with denial of electrical service, stating that officials' counsel would recommend that officials pay certain amount to settle action, but indicating that settlement had to be approved by city and county authorities, set forth illusory promise, and thus was legally insufficient as consideration for customers' promises; officials had unfettered discretion to accept or reject settlement, attorneys promised only to do that which they were separately entitled to do, and, because counsel were officials' agents, their recommendation was not consideration flowing from third party. Restatement (Second) of Contracts §§ 71(4), 77.

[3] Contracts 95 ⚷10(1)

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k10 Mutuality of Obligation
95k10(1) k. In General. Most Cited Cases

Under federal and New Mexico law, a promise by a party in the alternative is not consideration except under limited circumstances.

[4] Contracts 95 ⚷10(1)

95 Contracts

95I Requisites and Validity
95I(A) Nature and Essentials in General
95k10 Mutuality of Obligation
95k10(1) k. In General. Most Cited Cases

Under federal and New Mexico law, a promise or apparent promise is not consideration if by its terms the promisor or purported promisor reserves a choice of alternative performances unless: (1) each of the alternative performances would have been consideration if it alone had been bargained for, or (2) one of the alternative performances would have been consideration and there is or appears to the parties to be a substantial possibility that before the promisor exercises his or her choice events may eliminate the alternatives which would not have been consideration. Restatement (Second) of Contracts § 77.

[5] Contracts 95 ⚷10(1)

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k10 Mutuality of Obligation
95k10(1) k. In General. Most Cited Cases

Under federal and New Mexico law, where a party has an unfettered choice of alternatives, and one alternative would not have been consideration if separately bargained for, the promise in the alternative is not consideration. Restatement (Second) of Contracts § 77.

[6] Contracts 95 ⚷10(1)

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k10 Mutuality of Obligation
95k10(1) k. In General. Most Cited Cases

Under New Mexico law, a valid contract must possess mutuality of obligation, and mutuality means both sides must provide consideration.

[7] Contracts 95 ⚷10(1)

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k10 Mutuality of Obligation
95k10(1) k. In General. Most Cited Cases

Under New Mexico law, a contract which leaves it entirely optional with one of the parties to perform is not founded on mutual promises and thus is not valid.

*1187 Debra D. Poulin, Santa Fe, New Mexico, (Richard Rosenstock, Santa Fe, New Mexico and Jeffrey J. Buckels, Albuquerque, New Mexico on the briefs) for the plaintiffs-appellants.

David G. Reynolds (Wayne E. Bingham with him on the brief), Crider, Bingham & Hurst, P.C., Albuquerque, New Mexico, for the defendants-appellees Hrzich, McQuitty and City of Farmington Utility System.

Robert C. Armijo (Gregory W. MacKenzie with him on the brief), Civerolo, Gralow & Hill, Albuquerque, New Mexico, for defendants-appellees Kephart, Cheverie, Lasater and San Juan County Board of County Commissioners.

Before EBEL, HOLLOWAY and KELLY, Circuit Judges.

HOLLOWAY, Circuit Judge.

Plaintiffs/appellants Anthony and Nona Heuser (plaintiffs) bring this timely appeal from a judgment of the district court dismissing, pursuant to a putative settlement agreement, a suit they brought under 42 U.S.C. § 1983. The Section 1983 action alleged constitutional violations by state, county and city officials in denying electrical services to plaintiffs, *inter alia.* Contending that no enforceable settlement agreement had been reached, the plaintiffs opposed the dismissal below and now ask this court to reverse the judgment of dismissal.

I

A

Because the issues in this appeal are limited to those involving the enforceability of the putative settlement agreement of April 15, 1998, the "Outline of Agreement," we need only provide a brief general sketch of the underlying dispute. Except for findings of the district court noted below, we summarize only the plaintiffs' allegations.

Plaintiffs apparently live near to but not within the city limits of Farmington, New Mexico and before the present controversy, received their electrical service from the Farmington Utility System. Defendant Kephart, a building inspector for the county, allegedly entered plaintiffs' property without a warrant in 1991. As a result of what he saw then, he brought a criminal charge of constructing a building without a permit. Eventually plaintiffs were acquitted of that charge. While that criminal case was pending, however, a search warrant was obtained for some of the outbuildings on plaintiffs' property, and the warrant was executed on March 11, 1992. The actions of some of the defendants in obtaining and executing this search warrant are central events alleged by plaintiffs in the instant case.

The district judge found that the following facts were undisputed.[FN1] Kephart was ***1188** not properly certified as a building inspector. None of the officers who assisted Kephart in presentation of the search warrant application demonstrated their credentials to conduct an administrative inspection. The allegations in the search warrant application were limited to violations of county ordinances regarding proper set back and/or fire separations, failure to obtain building permits, and the existence of five or more structures "that appear to be fire hazards to adjacent buildings and property lines." Aplt.App. 63, 65-66.

FN1. These findings occurred in a rather unusual procedure. Some or all of the defendants had filed a motion for summary judgment raising the defense of qualified immunity. When that motion was denied, the defendants commenced an interlocutory appeal. Plaintiffs then moved the district court to certify that the appeal was frivolous, arguing that the appellate court did not have jurisdiction of the appeal under the doctrine of *Johnson v. Jones,* 515 U.S. 304, 115 S.Ct. 2151, 132 L.Ed.2d 238 (1995). The district court granted the plaintiffs' motion, thus determining that proceedings could continue in the district court during the pendency of the interlocutory appeal. *See Stewart v. Donges,* 915 F.2d 572, 574-79 (10th Cir.1990).

The district judge further found that no allegations of electrical or plumbing code violations were made in the affidavit and Kephart was neither qualified nor authorized to conduct electrical or plumbing inspections. Kephart asked defendant Hrzich to investigate the electrical wiring of the plaintiffs' buildings in spite of the lack of allegations of violations of electrical codes in the search warrant affidavit. No allegations of criminal activity were made in the search warrant affidavit. The district judge found that in the affidavit defendant Deputy Sheriff Cheverie "falsely accused Plaintiffs of committing crimes in violation of a county ordinance and misinformed the magistrate who issued the criminal search warrant that Plaintiffs' refusal to allow Kephart right of entry on their property without a warrant in itself violated the building code." The search warrant authorized a search only by Kephart, but other inspectors or law enforcement officers (ten of them according to plaintiffs' allegations) joined him in executing the warrant. While executing the warrant, two of the defendants entered the plaintiffs' residence, which was expressly excluded from the search warrant. *Id.*

About two months after execution of the search warrant, plaintiffs filed a tort claim with the county. On June 10, 1992, within a week of plaintiffs' filing of the claim, two of the defendants cut off plaintiffs' electrical service. Service was restored on April 2, 1993, but on May 26, 1993, it was again terminated by some of the defendants. Service was then not restored for about five years, under circumstances discussed below. Altogether, the plaintiffs were without electric service from the City for almost six years, relying on electricity from their own generator during that time.

B

About three years after the March 1992 execution of the search warrant, plaintiffs commenced the present Section 1983 action. Plaintiffs, who originally were proceeding *pro se,* sued the Governor and the Attorney General of New Mexico; the City Council of Farmington and the Farmington Utility System (the City); the Board of Commissioners of the County of San Juan (the County); and various county and city officials. Plaintiffs invoked 42 U.S.C. § 1983, *inter alia,* alleging that the defendants had violated plaintiffs' constitutional rights. The district court thus had jurisdiction under 28 U.S.C. §§ 1331 and 1343. The state officials were dismissed during the progress of the case and are not parties to this appeal.

C

On April 15, 1998, about three years after the action had been commenced, a settlement conference was conducted with a court-appointed mediator. At the conference there was agreement on the basic contours of a settlement, which the mediator summarized in a hand written document styled "Outline of Agreement" and which was signed by plaintiffs, their attorney, and attorneys for the Cityand for San ***1189** Juan County. Aplt.App. 106-109. (The attorney for the City also was representing the city employees and officials; similarly the attorneys for the County were also representing the county employees and officials.)

We quote the most pertinent provisions of the Outline:FN2

> FN2. We have a typed "transcript" of the Outline provided by plaintiffs and appended to their brief. Defendants have not contested the accuracy of plaintiffs' typed version of the original hand-written document.

> 1. Counsel for the County and City Defendants agree that they will recommend to their respective clients that said clients jointly pay the total sum of $237,500 in full and complete settlement of all claims in this above-referenced action filed or that could have been filed including attorneys fees and costs.
>
> 2. Plaintiffs agree that if said sum of $237,500 is jointly offered as indicated above by the County & City Defendants that they will accept said offer, if it also includes the terms set out below.
>
> 3. Farmington Utility System agrees that if a full and complete settlement is reached, they will promptly restore electrical service to the Heuser's [sic] property ... and the Heusers will be reinstated as regular customers without need of an inspection, subject to the Heusers[ ] signing a Hold Harmless Agreement.
>
> 4. The Heusers agree to sign a full and complete standard release in a form satisfactory to Defendants which Release shall contain language that Defendants do not admit liability.
>
> Aplt.App. 107-108.

As made clear in an affidavit of counsel later submitted to the district court, the attorney representing the City at the mediation session did not have authority to commit the City to any settlement, which required the approval of the City Council.FN3 Before that body could meet and approve the proposal, plaintiffs communicated their dissatisfaction with it and indicated that they would not accept the payment called for therein. Upon receiving notice that the settlement was being rejected by the plaintiffs, the district judge *sua sponte* scheduled a hearing to determine whether plaintiffs' electricity could be safely restored immediately. Aplt.App. 70-71. Before the day of the scheduled hearing, the service was restored.

> FN3. The New Mexico Supreme Court has noted that it " 'is fundamental that an attorney does not by reason of his employment have authority to compromise his client's cause of action absent an emergency requiring prompt action.' " *See Augustus v. John Williams & Assoc., Inc.,* 92 N.M. 437, 589 P.2d 1028, 1030 (1979) (quoting *Hayes v. Eagle-Picher Industries, Inc.,* 513 F.2d 892, 893 (10th Cir.1975)).

The defendants moved for enforcement of the purported settlement agreement, which the district court granted over plaintiffs' objection. The court entered judgment based on that order, dismissing plaintiffs' action as settled. Plaintiffs then filed a motion under Fed.R.Civ.P. 59(e) asking the court to vacate the order enforcing the settlement. The judge denied that motion, again holding that the Outline constituted an enforceable agreement, and plaintiffs commenced this appeal.

II

In the first of the two orders upholding the settlement agreement, the district judge ruled that the language of the Outline was unambiguous so that there was no need for extrinsic evidence as to the meaning of its terms. The judge found no merit in plaintiffs' contention that the terms of the Outline were not sufficiently definite for creation of a binding contract, and she found that the parties intended to form a final enforceable agreement, as opposed to merely documenting the progress of their negotiations. Her findings stated:

> Since the City Defendants are self insured, the City Council had to give final formal approval of the settlement amounts. Affidavit of Robin D. Strother.***1190** Accordingly, the parties agreed that "Counsel for the County and City Defendants will recommend to their respective clients that said clients jointly pay the total sum of $237,500 in full and complete settlement of all claims in the action filed or that could have been filed including attorneys fees and costs."

Aplt.App. at 76.

The condition of approval of the settlement amount by the City Council was a condition precedent to enforcement of the contract, the district court ruled, but not a condition to formation of the contract. Accordingly, the City had a reasonable time to perform the condition. The judge also rejected the plaintiffs' allegation that they had signed the Outline under duress. The judge opined that the real reason for the plaintiffs' resistance was the belated belief that they were not receiving enough money for their claims and that the court could not relieve the parties of their commitments.

On plaintiffs' motion to amend the judgment, which argued that there was no consideration for their promise to accept the deal if offered, the district judge specifically held that the consideration was sufficient:

> There was a bilateral contract here: *in return for Defendants' agents' promise to recommend that the City pay the negotiated amount, Plaintiffs promised not to back out on the deal that Defendants' attorneys had negotiated* (at great expense to the Defendants) before Defendants could act on that recommendation. New Mexico follows Section 71 of the Restatement (Second) of Contracts (1979). Under that Section, "[t]o constitute consideration, a performance or a return promise must be bargained for.".... The Court finds that the parties bargained for the exchange of promises and that the cessation of litigation was the goal of the bargaining process. .... *Defendants, through their agents, provided adequate consideration for Plaintiffs' promise to accept the monetary settlement if it was offered.* Settlement negotiations between individuals and public entities would be meaningless if Courts allowed individuals to undo days of negotiation (with their underlying expense) by simply changing their minds before the entity can take formal action to complete the bargain.

Aplt.App. 92-93 (emphasis added).

III

[1] We review a district judge's approval of a settlement agreement for an abuse of discretion. *See United States v. Hardage,* 982 F.2d 1491, 1495 (10th Cir.1993). We have held that the enforcement and interpretation of settlement agreements in Title VII cases are governed by federal common law because such settlements are "inextricably linked" to the underlying law of Title VII. *Snider v. Circle K Corp.,* 923 F.2d 1404, 1407 (10th Cir.1991) ("Federal common law governs the enforcement and interpretation of such agreements because 'the right of the litigants and the operative legal policies derive from a federal source.' *Fulgence v. J. Ray McDermott & Co.,* 662 F.2d 1207, 1209 (5th Cir.1981)."). Our later opinion in *Morris v. City of Hobart,* 39 F.3d 1105, 1112 (10th Cir.1994), addressed the issue whether federal or state law governs the interpretation of such settlement agreements in the context of subject matter jurisdiction and said that the "cause of action [for breach of contract arising out of private settlement of a Title VII claim] is a subject traditionally relegated to state law." FN4 Here the district judge said that " 'Construction of a settlement agreement generally is governed by state law.' " Memorandum Opinion and Order, Appellants' App. at 78 (quoting ***1191***Brockman v. Sweetwater County School Dist. No. 1,* 25 F.3d 1055, 1994 WL 170795 (10th Cir.), *cert. denied,* 513 U.S. 951, 115 S.Ct. 368, 130 L.Ed.2d 320 (1994)).

> FN4. The divergence of views of other courts on the applicability of federal or state law is noted in 19 Charles A. Wright, Arthur R. Miller & Edward H. Cooper, *Federal Practice & Procedure: Jurisdiction 2d* § 4541 at p. 394 n. 132 (2d ed.1996) (collecting cases).

In the instant appeal, the parties do not present a controversy over which law governs. In fact the briefs for all the parties say that state law governs interpretation of the settlement contract. Appellants' Brief at 20 n. 6; Response Brief of Appellees Frank Kephart *et al.* at 21; Response Brief of Appellees McQuitty *et al.* at 18. Moreover we feel that the applicable principles of contract law are not different in federal and New Mexico law. Accordingly, we turn to the parties' arguments which we will consider under basic contract rules.

[2] Plaintiffs first argue that the defendants' alleged promise was illusory and thus legally insufficient as consideration for plaintiffs' promises. Therefore, plaintiffs contend, the district court erred in holding that the Outline constituted a legally enforceable contract. We agree. It was apparent from paragraphs 1 and 3 of the Outline's numbered provisions that the $237,500 settlement had to be submitted to, and be given approval by, the City and County authorities. Aplt.App. at 108.

Thus, there was no legally sufficient consideration for the plaintiffs' promise to accept the contemplated settlement offer. The district judge found that the consideration, which she also found had been specifically bargained for, was the attorneys' promise to recommend the terms of the proposed settlement to their clients. The court's ruling notes that the attorneys were acting as agents. Section 147 of the Restatement (Second) of Agency provides: "Unless otherwise agreed, a disclosed or partially disclosed principal is a party to a contract, if not negotiable or sealed, made by his agent within his authority." *See also id.* § 292 & comment *a.* Here, the language of the Outline makes it clear that the parties "otherwise agreed" that the defendants as principals were not parties to the "agreement" but were to be given a recommendation to offer a specific amount of money, plus other consideration, to the plaintiffs if they chose to do so.

[3][4] Under the terms of the Outline, the defendants were not obligated to extend the offer to plaintiffs, and the Outline noted the operative procedure "if said sum of $237,500 is jointly offered ... by the County and City Defendants ..." Outline of Agreement, paragraph 2, Aplt.App. at 107. The defendants were completely free to choose between two alternatives-they could accept the attorneys' recommendation and extend the offer, or they could reject the recommendation. Obviously, if the defendants were to choose the second alternative, plaintiffs would have received nothing in exchange for their agreement. It is well settled that a promise by a party in the alternative is not consideration except under limited circumstances:

> A promise or apparent promise is not consideration if by its terms the promisor or purported promisor reserves a choice of alternative performances unless
>
> (a) each of the alternative performances would have been consideration if it alone had been bargained for; or
>
> (b) one of the alternative performances would have been consideration and there is or appears to the parties to be a substantial possibility that before the promisor exercises his choice events may eliminate the alternatives which would not have been consideration.

Restatement (Second) of Contracts § 77 (1981).

[5] Where, as here, a party "has an unfettered choice of alternatives, and one alternative would not have been consideration if separately bargained for, the promise in the alternative is not consideration." *Id., comment b.* In circumstances very similar to those presented here, it has been held that an apparent promise subject to the "unfettered discretion" of a municipality's governing body to accept or reject is "a classic example of an illusory promise." ***1192** Mastaw v. Naiukow, 105 Mich.App. 25, 306 N.W.2d 378, 380 (1981) ("Since the Detroit Common Council had unfettered discretion to accept or reject the settlement, its options were in no way limited by the supposed settlement."). Similarly in the instant case the defendants made no binding promise but had the unfettered discretion to accept or reject the proposed terms. Hence this is a clear example of an illusory promise.

[6][7] New Mexico cases have applied this principle, holding that where the purported promise to perform actually leaves it to the discretion of the promisor, the alleged promise is illusory and not consideration as a matter of law. *See* Board of Education v. James Hamilton Construction Co., 119 N.M. 415, 891 P.2d 556, 561 (App.1994), *cert. denied,* 119 N.M. 354, 890 P.2d 807 (1995); Acme Cigarette Services, Inc. v.

Gallegos, 91 N.M. 577, 577 P.2d 885, 889 (App.1978). As the court explained in *Hamilton Construction:* "A valid contract must possess mutuality of obligation. Mutuality means both sides must provide consideration. It is also elementary that a contract, which leaves it entirely optional with one of the parties to perform, is not founded on mutual promises." 891 P.2d at 561 (internal citations and quotation marks omitted).

The purported contract in *Hamilton Construction* was for the purchase of real property, but the written agreement provided forty days for the buyer to complete its due diligence work "and to review and approve or reject all matters pertaining to this transaction." *Id.* at 558. The escrow arrangements provided that buyer "may" deposit funds with the escrow agent. The New Mexico court held that there was no contract: "[B]ecause Buyer's promise to perform under the Agreement and [escrow] Instructions was entirely at its discretion, any consideration contained in such a promise would be illusory." *Id.* at 561. Because the purported contract in the instant case likewise left it entirely to the discretion of the defendants whether to accept or reject the proposed terms, we hold that the district court erred in concluding that the parties had entered into a binding contract.

In *Joseph E. Montoya and Associates v. State of New Mexico,* 103 N.M. 224, 704 P.2d 1100 (1985), another ruling similar to that of the Michigan Court in *Mastaw,* 306 N.W.2d at 380, was made. The New Mexico Supreme Court there held:

> Even without consideration of New Mexico law requiring DFA approval of state agency contracts, a contract never came into being under traditional contract principles. Part of the bargain between HSD and Montoya was that the proposed contract would not become effective unless and until DFA approval was obtained ... Because this condition precedent was not satisfied, no contract came into being.

704 P.2d at 1102.

Defendants contend that there was consideration for the plaintiffs' promise to accept the designated sum because the attorneys were bound by their promise to recommend the settlement. Defendants correctly point out that the district judge ruled that this was the promise for which the plaintiffs had specifically bargained, as our quotation *supra* from her order shows. We conclude nevertheless that the Outline is unenforceable, even if we assume that the district judge was correct in her ruling that the plaintiffs specifically bargained for only the attorneys' promise to recommend the settlement to their clients (as opposed to bargaining for the anticipated offer of money and restoration of electrical services from the defendants under the terms of the Outline). The attorneys' promise is not consideration because the attorneys promised only to do that which they were as counsel separately entitled to do-make a recommendation to the City and County. We assume that the attorneys promised to recommend the settlement to their clients because, in the exercise of their independent judgment and adhering to their ethical obligation of loyalty to their clients, the attorneys had ***1193** concluded that it was in their clients' best interests to approve the settlement.

The dissent argues that the recommendation from the attorneys, contemplated in the Outline of Agreement, serves as consideration flowing from a third party supporting the settlement agreement as performance given "by some other person." *See Restatement (Second) Contracts* § 71(4). This contention is premised on a misconception of the City and County counsel as a third party. The misconception runs counter to the parties' and the attorneys' treatment of such counsel not as third parties, but as *agents* of the City and County. The district judge found that "Defendants, through their agents, provided adequate consideration ...". Aplt.App. at 93. In their brief before us, the County defendants recognize that their counsel were acting as their *agents.* Response Brief of Appellees Kephart, et al. at 27 ("Plaintiffs bargained for the Defendants' agents['] promise that they would recommend the settlement to their clients"). The Response Brief of Appellees McQuitty, et al. at 24 and 25, implicitly recognizes their counsel as their agents (the offer had been "accepted by the Appellees, through counsel ..."). Thus the recommendations of counsel to accept the settlement must be treated as coming from the City's and County's agents, and cannot serve as third party performance given "by some other person." *Restatement (Second) Contracts* § 71(4).[FN5]

> FN5. Moreover the wording of the Outline of Agreement refutes the dissent's sugges-

tion that the agreement contained "no such language" as that in Montoya v. State of New Mexico, 704 P.2d at 1101, showing that the agreement in *Montoya* was not to be effective until a given date or approval by a state Department. To the contrary, the Outline of Agreement in the instant case clearly conditioned the duty of the plaintiffs to accept the settlement, saying "*if said sum of $237,500 is jointly offered as indicated above* ... they [plaintiffs] will accept said offer." Aplt.App. at 108.

In sum, the attorneys' promise is not sufficient as a matter of law to serve as consideration *from the defendants* to support this purported contract because the defendants simply made no enforceable promise. Because we have determined that there was no consideration given to the plaintiffs to make their promise enforceable at law, we need not reach other issues raised by the plaintiffs.

IV

The judgment of the district court is **reversed** and the case is remanded for further proceedings.

EBEL, Circuit Judge, dissenting
I disagree with the majority's conclusion that the settlement outline fails for lack of consideration. In my view, the promise of the City and County attorneys to recommend ratification of the settlement constitutes sufficient third-party consideration to support an agreement. I therefore respectfully dissent.

The cases relied upon by the majority are not persuasive under the facts presented by this case. First, the majority notes that the New Mexico Supreme Court has held that, absent emergency circumstances or preauthorization, an attorney may not " 'compromise his client's cause of action.' " *Augustus v. John Williams & Assocs., Inc.*, 92 N.M. 437, 589 P.2d 1028, 1030 (1979) (quoting *Hayes v. Eagle-Picher Indus., Inc.*, 513 F.2d 892, 893 (10th Cir.1975)); *see* Majority Opinion at n. 3. The *Augustus* case, however, does not describe the situation we are presently addressing. In the case at bar, the lawyers merely supplied valid third-party consideration in the form of a promise to recommend the settlement to their clients.[FN1] They did not, ***1194** as the *Augustus* case prohibits, affirmatively bind the City or County or otherwise compromise their interests. Rather, they made a promise that induced the Heusers to agree to the settlement.

FN1. The majority opinion dismisses the possibility that the attorneys supplied third-party consideration because, the opinion states, the parties have chosen to characterize the attorneys as agents of the City and County. However, even assuming that the attorneys did not act both as agents for the City and County and as third parties, the majority's point is misguided. If acting as agents, then the attorneys' promise affirmatively to recommend the settlement is direct consideration flowing from the promisee. The fact remains that the Heusers bargained for this affirmative act by the attorneys, and it was a meaningful restraint on the attorneys' freedom which constitutes adequate consideration, regardless of whether it is viewed as third-party consideration or party consideration.

The majority also cites cases for the proposition that "where the purported promise to perform actually leaves it to the discretion of the promisor, the alleged promise is illusory and not consideration as a matter of law." Majority Opinion at 13 (citing *Board of Educ. v. Hamilton Constr. Co.*, 119 N.M. 415, 891 P.2d 556, 561 (App.1994); *Acme Cigarette Servs., Inc. v. Gallegos*, 91 N.M. 577, 577 P.2d 885, 889 (App.1978)).[FN2] This discussion likewise overlooks the presence of third-party consideration in the present case. Although the City retained the option of either approving or rejecting the proposed settlement, the attorneys obligation to recommend the settlement was firm and definite.

FN2. I also note that the majority's reliance on *Joseph E. Montoya & Assocs. v. State of New Mexico*, 103 N.M. 224, 704 P.2d 1100 (1985) is misplaced because that case is plainly distinguishable from the present facts. The alleged agreement in *Montoya* contained a explicit provision stating that the agreement was not to become effective until "January 1, 1983, or upon approval by the Department of Finance and Administration, whichever is later." *Id.* at 1102. The outline at issue in the case at bar contains no such language, and that case did not involve third-party consideration as is the case here.

I would conclude that the attorneys promise to recommend the settlement was sufficient consideration supporting the settlement agreement. It is well-settled that consideration may flow from a third-party. *See* Restatement (Second) of Contracts § 71(4) ("The performance or return promise may be given to the promisor or to some other person. *It may be given by the promisee or by some other person.*") (emphasis added); 2 Corbin on Contracts § 5.11 (1995 Rev. Ed.) ("[I]n this country it is indisputable that the consideration need not move from the promisee.").

The majority seeks to dismiss the value of the attorneys' promise as consideration "because the attorneys promised to do that which they were as counsel separately entitled to do-make a recommendation to the City and County." Majority Opinion at 15. The majority then explicitly "assume[s] that the attorneys promised to recommend the settlement to their clients because, in the exercise of their independent judgment and adhering to their ethical obligation of loyalty to their clients, the attorneys had concluded that it was in their clients' best interests to approve the settlement." *Id.* This reasoning is misguided. The attorneys had an ethical and professional obligation to *present* the settlement to their clients, but they were under no duty to *affirmatively recommend* it. Furthermore, the assumption that the attorneys must have concluded that it was in their clients' best interest to accept the settlement is unfounded. The attorneys may very well have concluded that this was the best settlement offer that they could negotiate with the Heusers, but that it was perhaps still too generous. Whatever tension might exist between the lawyers' promise to recommend the settlement and their professional obligation not to advise a client to accept an undesirable settlement does not alter the fact that the attorneys are not obligated to affirmatively recommend every settlement offer presented to their clients.

Here the Heusers obtained a clear commitment from the City's and County's attorneys to recommend the settlement for adoption. That commitment was an obvious benefit to the Heusers, as it would greatly facilitate the likelihood that the City and County would approve the settlement. It was similarly a detriment to the attorneys, who thereby diminished their ***1195** own options. Whatever implication this may have had as between the City and County and its attorneys is of no consequence to the Heusers. From the Heusers' perspective, the commitment by the City's and County's attorneys was clear and valuable consideration, and in my opinion, it supports the settlement agreement.

Thus, I would find that the attorneys' promise represented valid third-party consideration supporting the agreement. I respectfully dissent.

C.A.10 (N.M.),2000.
Heuser v. Kephart
215 F.3d 1186, 2000 CJ C.A.R. 4049

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TAB 6

United States Court of Appeals,
Seventh Circuit.
IDX SYSTEMS CORPORATION, Plaintiff-Appellant,
v.
EPIC SYSTEMS CORPORATION, University of Wisconsin Medical Foundation, Mitchell Quade, and Michael Rosencrance, Defendants-Appellees.
Nos. 01-3083, 01-3228.

Argued Jan. 24, 2002.
Decided April 1, 2002.

Provider of medical business management software sued competitor and former customer, claiming trade secret misappropriation and tortious interference with contract. United States District Court for the Western District of Wisconsin, 165 F.Supp.2d 812, John C. Shabaz, J., granted summary judgment for defendants, and appeal was taken. The Court of Appeals, Easterbrook, Circuit Judge, held that: (1) plaintiff failed to adequately identify allegedly misappropriated trade secrets; (2) confidentiality agreement between plaintiff and customer was valid; and (3) Wisconsin law did not preempt plaintiff's claim that competitor tortiously induced customer to breach confidentiality agreement.

Affirmed in part; reversed and remanded in part.

West Headnotes

[1] Antitrust and Trade Regulation 29T 413

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(A) In General
29Tk413 k. What Are "Trade Secrets" or Other Protected Proprietary Information, in General. Most Cited Cases
(Formerly 382k984 Trade Regulation, 379k10(5))
To show that particular information is "trade secret," under Wisconsin law, misappropriation plaintiff must demonstrate that it is valuable, not known to others who might profit by its use, and has been handled by means reasonably designed to maintain secrecy. W.S.A. 134.90.

[2] Antitrust and Trade Regulation 29T 428

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(B) Actions
29Tk428 k. Pleading. Most Cited Cases
(Formerly 382k998 Trade Regulation, 379k26(1), 379k10(5))
Under Wisconsin law, provider of software for medical business management failed to adequately identify trade secrets allegedly misappropriated by competitor; provider tendered complete documentation for software, without identifying exactly which pieces of information were trade secrets. W.S.A. 134.90.

[3] Contracts 95 116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases
Rules limiting extent of no-compete clauses are based on fact that they tie up human capital and, if widely adopted, may have practical effect of preventing horizontal competition in economically significant markets.

[4] Contracts 95 118

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k118 k. Preventing Disclosure of Trade Secrets. Most Cited Cases
Under Wisconsin law, as predicted by circuit court, confidentiality agreement between business man-

agement software provider and customer was not invalidated by its lack of time and place restrictions or fact that it was not restricted just to trade secrets.

[5] Torts 379 ⚷251

379 Torts
379III Tortious Interference
379III(B) Business or Contractual Relations
379III(B)3 Actions in General
379k251 k. Nature and Form of Remedy. Most Cited Cases
(Formerly 379k12)

Wisconsin trade secret misappropriation statute did not preempt software provider's claim that competitor tortiously induced customer to breach confidentiality agreement. W.S.A. 134.90(6)(a).

***582** Kenneth W. Starr (argued), Kirkland & Ellis, Washington, DC, William A. Streff, Kirkland & Ellis, Chicago, IL, for Plaintiff-Appellant IDX Systems Corp. in No. 01-3083.

William A. Streff, Kirkland & Ellis, Chicago, IL, for Plaintiff-Appellant IDX Systems Corp. in No. 01-3228.

Anthony A. Tomaselli, Nicholas J. Seay (argued), Quarles & Brady, Barbara A. Neider (argued), Stafford Rosenbaum, Steven M. Streck, Axley Brynelson, Jon G. Furlow (argued), Michael, Best & Friedrich, Madison, WI, for Defendants-Appellees Epic Systems Corp., Mitchell Quade, Michael Rosencrance and University of Wisconsin Medical Foundation.

Michael P. Crooks, Peterson, Johnson & Murray, Madison, WI, for Defendant-Appellee Westfield Ins. Co.

Before EASTERBROOK, RIPPLE, and DIANE P. WOOD, Circuit Judges.

EASTERBROOK, Circuit Judge.

Both IDX Systems and Epic Systems make software for use in managing the financial side of a medical practice: billing, insurance reimbursement and other collections, and the like. During the 1980s IDX sold this software package to two medical groups that later merged into the University of Wisconsin Medical Foundation, which now comprises more than 1,000 physicians. The Foundation continued to use ***583** IDX software until December 2000, when it switched to software developed by Epic. IDX believes that Mitchell Quade and Michael Rosencrance, former employees of Epic who came to manage data processing at the Foundation, not only instigated this change but also used their new positions to transfer valuable information to Epic. According to IDX's complaint, over the course of a year Quade and Rosencrance personally, and with the aid of other Foundation employees, furnished Epic with details about how IDX's software works, enabling Epic to enhance its own package and ultimately take the Foundation's business-and to match up better against IDX in the competition for other customers.

IDX's complaint under the diversity jurisdiction of 28 U.S.C. § 1332 charges the Foundation, Quade, and Rosencrance with stealing IDX's trade secrets and breaking contractual promises of confidentiality; it charges Epic with tortiously inducing the other defendants to do these things. The district court dismissed the tort claims against Epic on the pleadings, observing that Wis. Stat. § 134.90(6)(a) overrides any theory that conflicts with the state's law of trade secrets. Later it pared all contract-based claims out of the case, ruling that the confidentiality agreements are invalid under Wisconsin law (which the parties agree governs) because they do not contain temporal and geographic limitations. Finally, the court granted summary judgment to the defendants on the trade-secret claim, after concluding that IDX had failed to identify with specificity the trade secrets that it accuses the defendants of misappropriating. 165 F.Supp.2d 812 (W.D.Wis.2001). We shall start where the district court ended: with the trade-secret claim.

[1][2] Trade secrets are a subset of all commercially valuable information. Wisconsin has followed the Uniform Trade Secrets Act in defining "trade secret" this way:

> "Trade secret" means information, including a formula, pattern, compilation, program, device, method, technique or process to which all of the following apply:
>
> 1. The information derives independent economic value, actual or potential, from not being generally known to, and not being readily ascer-

tainable by proper means by, other persons who can obtain economic value from its disclosure or use.

2. The information is the subject of efforts to maintain its secrecy that are reasonable under the circumstances.

Wis. Stat. § 134.90(1)(c). Thus to show that particular information is a trade secret, a firm such as IDX must demonstrate that it is valuable, not known to others who might profit by its use, and has been handled by means reasonably designed to maintain secrecy. Like the district judge, we think that IDX failed to do this. It has been both too vague and too inclusive, effectively asserting that all information in or about its software is a trade secret. That's not plausible-and, more to the point, such a broad assertion does not match up to the statutory definition. Reluctance to be specific is understandable; the more precise the claim, the more a party does to tip off a business rival to where the real secrets lie and where the rival's own development efforts should be focused. Still, tools such as protective orders are available to make this process less risky, and unless the plaintiff engages in a serious effort to pin down the secrets a court cannot do its job.

According to IDX, "a 43-page description of the methods and processes underlying and the inter-relationships among various features making up IDX's software package" is specific enough. No, it isn't. ***584** These 43 pages describe the software; although the document was created for this litigation, it does not separate the trade secrets from the other information that goes into any software package. Which aspects are known to the trade, and which are not? That's vital under the statutory definition. Likewise, IDX's tender of the complete documentation for the software leaves mysterious exactly which pieces of information are the trade secrets. As we remarked in *Composite Marine Propellers, Inc. v. Van Der Woude,* 962 F.2d 1263, 1266 (7th Cir.1992), a plaintiff must do more than just identify a kind of technology and then invite the court to hunt through the details in search of items meeting the statutory definition. See also *AMP Inc. v. Fleischhacker,* 823 F.2d 1199, 1203 (7th Cir.1987). What is more, many of the items that appear in the 43-page description, such as the appearance of data-entry screens, are exceedingly hard to call trade secrets: things that any user or passer-by sees at a glance are "readily ascertainable by proper means". Perhaps screen displays could be copyrighted, but no copyright claim has been advanced, and a trade-secret claim based on readily observable material is a bust. *Minnesota Mining & Manufacturing Co. v. Pribyl,* 259 F.3d 587 (7th Cir.2001), on which IDX principally relies, did not involve such self-revealing information. Other details, such as the algorithms that the software uses to do real-time error checking (a vaunted feature of IDX's software), may be genuine trade secrets, but IDX has not tried to separate them from elements such as its input and output formats. Nor does it contend that the defendants decompiled the object code or otherwise obtained access to the algorithms that power the program; it alleges only that Foundation transferred to Epic those details that ordinary users of the software could observe without reverse engineering.

Because (as what we have already written illustrates) it is hard to prove that particular information qualifies as a trade secret, many producers of intellectual property negotiate with their customers for additional protection. This is a step that Wisconsin permits. See *ProCD, Inc. v. Zeidenberg,* 86 F.3d 1447 (7th Cir.1996) (Wisconsin law). Following § 7 of the Uniform Trade Secrets Act, Wis. Stat. § 134.90(6) provides:

(a) Except as provided in par. (b), this section displaces conflicting tort law, restitutionary law and any other law of this state providing a civil remedy for misappropriation of a trade secret.

(b) This section does not affect any of the following:

1. Any contractual remedy, whether or not based upon misappropriation of a trade secret.

2. Any civil remedy not based upon misappropriation of a trade secret.

3. Any criminal remedy, whether or not based upon misappropriation of a trade secret.

IDX and the Foundation (through its predecessors in interest) agreed to the sort of contractual remedy preserved in § 134.90(6)(b)1. The Foundation promised not to allow the software and related materials "furnished by" IDX to be "examined ... for the purpose of creating another system" and vowed in addition not to "use or disclose or divulge to others any data or information relating to" the system or "the technology, ideas, concepts, know-how, and techniques embodied therein." IDX has evidence (enough to survive summary judgment) that the Foundation, Quade, and Rosencrance broke these promises by describing IDX's system in detail to Epic and helping it duplicate those features that the Foundation liked. Nonetheless, the district judge held, the promises are unenforceable***585** because they are unlimited in temporal and geographic scope, and thus unduly restrain trade.

[3][4] In reaching this conclusion, the district court relied on decisions requiring restrictive covenants limiting competition between employers and their ex-employees to be reasonable, a limitation that in Wisconsin entails some restrictions on time and scope. See *Farm Credit Services v. Wysocki,* 243 Wis.2d 305, 627 N.W.2d 444 (2001); *Tatge v. Chambers & Owen, Inc.,* 219 Wis.2d 99, 579 N.W.2d 217 (1998); *Streiff v. American Family Mutual Insurance Co.,* 118 Wis.2d 602, 348 N.W.2d 505 (1984); Wis. Stat. § 103.465. Rules limiting the extent of no-compete clauses are based on the fact that they tie up human capital and, if widely adopted, may have the practical effect of preventing horizontal competition in economically significant markets. See Paul H. Rubin & Peter Shedd, *Human Capital and Covenants Not to Compete*, 10 J. Legal Studies 93 (1981). But neither rationale applies to contracts that restrict the use of particular information between businesses that have vertical (supplier-to-customer) rather than horizontal (competitor-to-competitor) relations. See Benjamin E. Hermalin & Michael L. Katz, *Judicial Modification of Contracts Between Sophisticated Parties: A More Complete View of Incomplete Contracts and Their Breach*, 9 J.L. Econ. & Org. 230 (1993); Robert Unikel, *Bridging the Trade Secret Gap*, 29 Loyola U. Chi. L.J. 841 (1998). IDX did not contract for limitations on Epic's ability to compete; contracts between IDX and the Foundation are vertical in nature and protect intellectual property without affecting competition. They may compel rivals such as Epic to do more work to develop software independently, but this promotes rather than restricts competition. *Kewanee Oil Co. v. Bicron Corp.,* 416 U.S. 470, 94 S.Ct. 1879, 40 L.Ed.2d 315 (1974), holds that trade-secret law is compatible with antitrust law; the same can be said for contracts protecting intellectual property that, though not demonstrably a trade secret, is commercially valuable. Rivals such as Epic, as non-parties to the vertical arrangements, remain entitled to discover and use the information independently and to compete vigorously. Nothing in the antitrust laws gives one producer a right to sponge off another's intellectual property, even when the producer of that knowledge has a market share much larger than IDX's. See *United States v. Microsoft Corp.,* 253 F.3d 34 (D.C.Cir.2001) (en banc).

The parties have not cited, and we have not found, any Wisconsin statute or decision subjecting non-disclosure agreements between suppliers and users of intellectual property to the rules that govern non-competition clauses between employers and employees. To the contrary, *Fullerton Lumber Co. v. Torborg,* 270 Wis. 133, 139, 70 N.W.2d 585, 588 (1955), tells us that Wisconsin allows "a much greater scope of restraint in contracts between vendor and vendee than between employer and employee." Section 134.90(6)(b)1 implies that contracts about intellectual property are valid, even when they exceed the domain of trade secrets. Restrictions on disclosure may make intellectual property more valuable to its producer, and thus promote both the creation of knowledge and competitions against other firms in the same industry. No one doubts this with physical property: General Motors is entitled to control 100% of its own output of mufflers, without handing any of them over to Ford or Toyota or Volkswagen. Permitting a producer the full return on its investment in mufflers (or any other product) is essential to promote investment in productive assets and rivalry with other producers. Just so with knowledge, an increasingly vital input into production. ***586** Why should IDX or any other maker of intellectual property be placed under legal rules that effectively entitle its rivals to a chunk of that asset's value?

No Wisconsin decision of which we are aware requires temporal or geographic limits as a condition to the enforcement of a non-disclosure agreement for intellectual property. It is impossible to understand how a non-disclosure agreement *could* place "geographical" limits on the dissemination of intellectual property comparable to those restricting the locale where a salesman may try to drum up customers for a new employer. If the Foundation were forbidden to disclose the details to Epic in Wisconsin, but allowed to do so in Indiana, that would be the same thing as permitting disclosure everywhere (and thus nixing all contractual limits)-for Epic could sell worldwide any software derived from what it learned in Indiana. Knowledge does not respect borders. *ProCD*, a case that the district court did not mention, enforced as a matter of Wisconsin law a contract placing worldwide restrictions on the use of intellectual property embedded in software.

Temporal limitations could make more sense. Perhaps Wisconsin's courts would deem contracts such as those between IDX and the Foundation to cover only information that is not generally known. What would be the point of forbidding the Foundation to talk in public about features of IDX's system that had been the subject of a review in a trade publication? But it is too early in this litigation to decide whether Wisconsin would curb the unqualified scope of this contractual language-and, if some limits would be interpolated into the text, whether these would shelter the actual disclosures that the Foundation made to Epic. (The Foundation contends, for example, that it had customized IDX's software extensively and disclosed to Epic details about its own additions rather than any information "furnished by" IDX and of which Epic was unaware before the disclosures. It also contends that IDX cannot establish damages. But these and other factual arguments must be developed through discovery rather than decided at the complaint stage.)

[5] Because further proceedings must be held on IDX's contractual claims against the Foundation and its employees, we must consider the contention that Epic tortiously induced the Foundation to break its promises (and that Quade and Rosencrance were in cahoots with Epic in this endeavor). Because this claim was dismissed on the pleadings, we assume that Epic did what IDX alleges. The district court held that Epic was free to induce the Foundation to dishonor its promises in light of § 134.90(6)(a), which "displaces conflicting tort law, restitutionary law and any other law of this state providing a civil remedy for misappropriation of a trade secret." That ruling suffers from two problems.

First, paragraph (a) begins with the words "[e]xcept as provided in par. (b)", and paragraph (b)2 carves out of paragraph (a) "[a]ny civil remedy not based upon misappropriation of a trade secret." The tort of inducing breach of a non-disclosure contract (the sort of contract independently protected by paragraph (b)1) is "not based upon misappropriation of a trade secret." It is based on interference with the contract.

Second, even when read apart from paragraph (b), paragraph (a) deals only with "*conflicting* tort law" (emphasis added). Enforcement of a non-disclosure agreement does not *conflict* with trade-secret law, and thus preventing third parties from inducing breach of such an agreement does not conflict with trade-secret law. The district court did not cite ***587** any Wisconsin case holding that the tort of interference with contract (or interference with economic advantage more generally) conflicts with trade-secret law for purposes of § 134.90(6)(a). In diversity litigation, our task is to implement state law as state courts would implement it, and we cannot think of any reason why the Supreme Court of Wisconsin would find such a conflict. The claims against Epic, Quade, and Rosencrance growing out of the Foundation's breach of its contracts with IDX therefore should not have been dismissed.

The judgment of the district court is affirmed to the extent it granted judgment to the defendants on IDX's trade-secret claims. The remainder of the judgment is reversed, and the case is remanded for further proceedings consistent with this opinion.

C.A.7 (Wis.),2002.
IDX Systems Corp. v. Epic Systems Corp.
285 F.3d 581, 62 U.S.P.Q.2d 1278

END OF DOCUMENT

TAB 7

C

Supreme Court, Monroe County, New York.
LAZER INCORPORATED, Plaintiff,
v.
Rosemarie KESSELRING, Defendant.
July 21, 2005.

Background: Employer brought action against former employee, alleging claims for breach of employment agreement. Employee moved for summary judgment.

Holding: The Supreme Court, Monroe County, Kenneth R. Fisher, J., held that provision in employment agreement prohibiting employee from soliciting employer's workers during one year post-employment period was unenforceable.

Motion granted.

West Headnotes

[1] Contracts 95 116(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases

Provision in employment agreement prohibiting employee from soliciting employer's workers during one year post-employment period was unenforceable, where enforcement of the nonrecruit provision would not serve any legitimate interest of employer.

[2] Contracts 95 116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases

An agreement restricting a former employee's freedom to solicit his former co-employees necessarily affects the general competitive mold of society, and is in derogation of the concept that the economy is premised on the competition engendered by the uninhibited flow of services, talent, and ideas.

[3] Contracts 95 116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases

A covenant not to solicit former co-employees is a species, albeit a limited one, of a covenant not to compete in the broad sense and is governed by the three part test of reasonableness applicable to restraints on competition. Restatement (Second) of Contracts § 188.

[4] Contracts 95 116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases

Generally, a restrictive covenant in an employment agreement is reasonable only if it: (1) is no greater than is required for the protection of the legitimate interest of the employer; (2) does not impose undue hardship on the employee; and (3) is not injurious to the public.

[5] Contracts 95 116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases
A violation of any prong of the three part test of reasonableness applicable to restraints on competition renders the covenant invalid.

[6] Contracts 95 116(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases
Enforcement of a covenant restricting employee competition will be upheld only to the extent it serves a legitimate interest of the employer to avoid unfair competition.
****835** Boylan Brown Code Vigdor & Wilson LLP, Rochester (Frank C. Pavia of counsel), for plaintiff.

Jaeckle Fleischmann & Mugal LLP, Rochester (Sharon P. Stiller of counsel), for defendant.

KENNETH R. FISHER, J.

***428** This matter is before the court following a motion for summary judgment filed by plaintiff and a cross-motion for summary judgment filed by defendant. Oral argument was held on July 6, 2005, and the court ruled at that time that plaintiff's motion for summary judgment was denied. Further, it was held that the portion of defendant's cross-motion which was for dismissal of plaintiff's cause of action grounded in unjust enrichment was granted. The court reserved decision on the remainder of defendant's cross-motion, and that will be addressed at this time.

Facts and Procedural Background

According to its own description as contained in the complaint, plaintiff is a corporation which, "has provided businesses with various digital services used in the production of marketing and packaging materials, including imaging, design and mechanical layout, electronic prepress, and catalog and packaging development." (Complaint, paragraph 3). Defendant was an employee of plaintiff who left its employ in July 2004, and began working for Jay Advertising ("Jay") immediately thereafter. According to the affidavit of Greg Smith, the President of Jay, Jay is a advertising and marketing company which conducts advertising, planning, research, promotions, media and public relations. These descriptions of the two companies have not been contested by either of the parties.

Defendant was required to execute an Employment Agreement on May 31, 2000. It contained, *inter alia,* restrictive covenants. One, found in paragraph 5.4, was a covenant not to compete. It consisted of general language in which defendant, for the period of one year following termination of employment with plaintiff, agreed, not to compete with plaintiff, nor solicit any customers of plaintiff, and not ****836** to work for a competitor. A second restrictive covenant was found in an entirely different paragraph. Paragraph 5.6 provided that, during the one year post-employment period, defendant "shall not hire any employee of the [Plaintiff] or solicit any employee of the [Plaintiff] to leave the employment of the [Plaintiff] for any reason." When defendant's initial term of employment was nearing an end, plaintiff sent defendant a letter in which plaintiff indicated that it wished to retain defendant as an employee, and made several amendments to the May 31, 2000, agreement. Among those revisions, ***429** plaintiff wrote that paragraph 5.8 was deleted in its entirety. Neither party contests that defendant was employed under the terms of the May 31, 2001 amendments to the May 31, 2000 Agreement.

Plaintiff filed suit against defendant alleging damages as the result of defendant's alleged solicitation of one of plaintiff's employees, Marianne Warfle. Plaintiff has asserted that defendant actively participated in the hiring of Warfle by Jay to such an extent that defendant violated her restrictive covenant not to solicit plaintiff's employees. Defendant, in response, has contended that she did nothing affirmative to seek out Warfle, that Warfle merely responded to a blind ad for an open position which turned out to be with Jay, and upon learning that Warfle had applied for the open position, informed both her and Jay that she could not actively assist in the potential hiring process of Warfle in deference to the restrictive covenant which she had executed with plaintiff. The parties' submissions on these motions focus primarily on this factual dispute. But defendant's cross motion may be resolved in her favor without a trial of that discrete factual issue.

Discussion and Analysis

The non-recruitment provision at issue appears in Article 5 of the agreement entitled "Covenants by Employee." The first three paragraphs of Article 5 concern confidential information. ¶ 5.4 is a covenant not to compete. Paragraph 5.5 is a non-solicitation of customers provision. Paragraph 5.6, the one at issue here, is a non-recruitment provision which reads, in its entirety, "During the non-competition period, the employee shall not hire any employee of the company or solicit any employee of the company to leave the employment of the company for any purpose." As I indicated at oral argument, two issues immediately present themselves by defendant's cross motion. First, can the non-recruitment provision be read as a stand-alone covenant, without regard to and not tied to the non-competition provisions? Second, if it can be read as a stand-alone provision, is it enforceable in this state? Both the structure of Article 5 of the agreement and the first clause of ¶ 5.6 compel a reading of the ¶ 5.6 covenant as erecting a non-recruitment duty only in conjunction with the non disclosure of propriety information provisions(¶ 5.1, ¶ 5.2, and ¶ 5.3) and the non-competition provisions (¶ 5.4, ¶ 5.5 and, as I find here, ¶ 5.6). The first clause of ¶ 5.6 ("During the non-competition ***430** period") makes the tie-in explicit, thus signaling the intention of the parties to make the non-recruitment duty applicable only in a case in which a competitor is involved or the protection of confidential or proprietary information is at stake.

[1] Even assuming, however, that the non-recruitment provision may be read as a standalone provision, having application to non-competitors in a case in which the former employer fails to establish that protection of confidential information is at stake, such a provision would be held unenforceable****837** in New York. The Court of Appeals has not considered whether a covenant not to recruit is enforceable in this state. The federal courts cite *Veraldi v. American Analytical Laboratories, Inc.*, 271 A.D.2d 599, 706 N.Y.S.2d 158 (2d Dept.2000), however, as authority for the proposition that "New York recognizes the enforceability of covenants not to solicit employees." *Global Telesystems, Inc. v. KPNQwest, N.V.*, 151 F.Supp.2d 478, 482 (S.D.N.Y.2001). *See also*, *Automated Concepts Incorporated v. Weaver*, unpublished, No. 99 C 7599 (N.D.Ill. August 9, 2000) (2000 WL 1134541).

Veraldi is indeed the only New York case I have been able to find treating a covenant not to solicit employees. The case involved a counter claim asserting that the former employee solicited the employer's customers and employees, both of which was covered by restrictive covenants. The court upheld the trial court's refusal to dismiss the counterclaims, observing that "the restrictive covenant does not violate public policy and, therefore, is enforceable." *Veraldi*, 271 A.D.2d at 600, 706 N.Y.S.2d 158. In support of this conclusion the court cited *Slomin's Inc. v. Gray*, 176 A.D.2d 934, 935, 575 N.Y.S.2d 545 (2d Dept.1991), which was a sale of business case not involving a covenant prohibiting solicitation of former co-employees. *See id.*, 176 A.D.2d at 935, 575 N.Y.S.2d 545. The court's cryptic statement that the covenant "does not violate public policy" did not reveal whether the covenant was tested under the concept of reasonableness applicable to restraints on competition (as a species of restraints on trade), A.L.I., *Restatement (Second) of Contracts* § 188 (1981); *BDO Seidman v. Hirshberg*, 93 N.Y.2d 382, 388-89, 690 N.Y.S.2d 854, 712 N.E.2d 1220 (1999) (three prong test), or the rule of reason test applicable to covenants in restraint of trade generally. A.L.I., *Restatement (Second) of Contracts* § 187, or some other test.

[2][3] I assume that, because the particular kind or type of restraint that is involved here is a post employment restraint on the conduct of an employee, the covenant should be analyzed according to the three pronged reasonableness formula of *BDO Seidman* and § 188 of the *Restatement (Second) of* ****431*** *Contracts. See generally,* Blake, *Employee Agreements Not To Compete,* 73 Harv. L. Rec. 625, 646 (1960)(tracing "the divorce of the law of employee

restraints from its rather unnatural marriage with the doctrines governing restraints of other types"). The New York cases, although invariably dealing with post employment covenants not to compete, speak of the "overriding requirement of reasonableness" as applying to "negative covenants" or "restrictive covenants" directed at employee conduct generally, with "the formula of reasonableness ... vary[ing] with the context and type of restriction imposed." *Reed, Roberts Associates, Inc. v. Strauman,* 40 N.Y.2d 303, 307-08, 386 N.Y.S.2d 677, 353 N.E.2d 590 (1976). But an agreement of the kind found here, restricting as it does a former employee's freedom to solicit his former co-employees, necessarily also affects "the general competitive mold of society," *American Broadcasting Companies, Inc. v. Wolf,* 52 N.Y.2d 394, 404, 438 N.Y.S.2d 482, 420 N.E.2d 363 (1981), and is in derogation of the concept, invoked in the cases on this subject, that "our economy is premised on the competition engendered by the uninhibited flow of services, talent and ideas." *Reed, Roberts Associates, Inc. v. Strauman,* 40 N.Y.2d at 307, 386 N.Y.S.2d 677, 353 N.E.2d 590. Accordingly, a covenant not to solicit former co-employees is a species, albeit a limited one, of a covenant not to compete in the broad sense and is governed by the three part test of reasonableness****838** articulated in *BDO Seidman* and § 188 of the *Restatement (Second) of Contracts.*

To be sure, such a covenant does not affect in the same way the "powerful considerations of public policy which militate against sanctioning the loss of a man's livelihood," *Purchasing Associates, Inc. v. Weitz,* 13 N.Y.2d at 272, 246 N.Y.S.2d 600, 196 N.E.2d 245. That factor, however, does not take such a covenant out of the class of anti-competitive employee covenants subject to reasonableness scrutiny generally applicable to non-compete agreements, because as stated above it is only "the formulation of reasonableness [that] may vary with the context and type of restriction imposed." *Reed, Roberts, Associates, Inc. v. Strauman,* 40 N.Y.2d at 307, 386 N.Y.S.2d 677, 353 N.E.2d 590. This is confirmed by the citation in *BDO Seidman,* 93 N.Y.2d at 389, 690 N.Y.S.2d 854, 712 N.E.2d 1220, of *Technical Aid Corp. v. Allen,* 134 N.H. 1, 591 A.2d 262 (1991), which upheld on its facts a covenant not to solicit the former employer's employees. *Id.,* 134 N.H. at 13-14, 591 A.2d at 269. The court agreed at "[s]uch a prohibition certainly may have some impact on ... [the former employee]'s employment," *id.,* 134 N.H. at 15, 591 A.2d at 270, and therefore it is appropriate to analyze ***432** ¶ 5.6 under the three-pronged test of reasonableness of *BDO Seidman,* or some variant thereof. [FN1]

FN1. There is authority to the contrary elsewhere. *Smith, Barney, Harris Upham & Co., Inc. v. Robinson,* 12 F.3d 515, 519 (5th Cir.1994) ("narrowly tailored covenant not to solicit employees of the employer is not among the kinds of agreement covered by the [Louisiana] statute"); *Beasley v. Hub City Texas, L.P.,* unpublished 2003 WL 22254692, at n. 3 (Ct.App.Tex. Sept. 29, 2003) ("nonrecruitment covenants ... do not necessarily restrict a former employee's ability to compete with his or her former employer and, like nondisclosure covenants, should not significantly restrain trade" (quoting *Totino v. Alexander & Assocs., Inc.,* unpublished 1998 WL 552818, text at 28-30)(Ct.App.Tex. Aug. 20, 1998)). Compare *YCA, LLC v. Berry,* unpublished 2004 WL 1093385 at *17-*18 (N.D.Ill. May 7, 2004), *with, Unisource Worldwide, Inc. v. Carrara,* 244 F.Supp.2d 977, 983 (C.D.Ill.2003), for varying approaches to Illinois Law. The problem with these cases, however, is that they completely remove the matter from any reasonableness analysis while the approach taken in the text above factors the more benign nature of the restrictive covenant into the common law reasonableness analysis. For the reasons stated above, I believe the Court of Appeals cases on restrictive employment covenants require this, as *Veraldi* seemed to recognize.

[4][5][6] Generally, a restrictive covenant in an employment agreement "is reasonable only if it: (1) is *no greater* than is required for the protection of the *legitimate interest* of the employer, (2) does not impose undue hardship on the employee, and (3) is not injurious to the public." *BDO Seidman,* 93 N.Y.2d at 388-89, 690 N.Y.S.2d 854, 712 N.E.2d 1220. "A violation of any prong renders the covenant invalid." *Id.,* 93 N.Y.2d at 389, 690 N.Y.S.2d 854, 712 N.E.2d 1220. As stated above, however, the reasonableness test "may vary" depending upon the type of restriction involved and the circumstances. The precise formulation of the reasonableness test for a covenant of this nature should be left to the Court of Appeals,

as the exclusive policy making arm of the state judiciary. But it has been held that the reasonableness inquiry may be avoided altogether when the court finds that application of a particular restrictive covenant will not serve any legitimate employer interest. *American Institute of Chemical Engineers v. Reber-Friel Co.*, 682 F.2d 382, 387 (2d Cir.1982) ("we need not reach the questions of reasonableness of the scope of the covenant because legitimate interests of the employer are not implicated"****839**). True, this is a federal case, but the clear message of *BDO Seidman* was the same: enforcement of a covenant restricting employee competition will be upheld only to the extent it serves a legitimate interest of the employer to avoid *unfair* competition. *BDO Seidman*, 93 N.Y.2d at 391-93, 690 N.Y.S.2d 854, 712 N.E.2d 1220 (drawing a sharp distinction between the concept of unfair competition***433** and the illegitimate purpose of avoiding competition in a general sense).FN2

FN2. This is just another way of saying that a failure to meet the first prong of the tripartite common law standard (restraint must be "*no* greater than is required for the protection of the *legitimate interest* of the employer," *BDO Seidman*, 93 N.Y.2d at 388-89, 690 N.Y.S.2d 854, 712 N.E.2d 1220 [emphasis in original]) obviates the need to consider the other two prongs of the test.

Here, defendant establishes as a matter of law that enforcement of the nonrecruit provision of the agreement will not serve any legitimate employer interest in the circumstances, and plaintiff fails to raise an issue of fact on the matter. It is not alleged that the employer allegedly recruited possesses any confidential or proprietary information of the plaintiff, nor is it alleged that she was in any position to acquire trade secrets. Plaintiff does not present any admissible evidence that she was a particularly valuable or unique employee, or provided services to plaintiff which cannot easily be replaced. *Ken J. Pezrow Corporation v. Seifert*, 197 A.D.2d 856, 602 N.Y.S.2d 468 (4th Dept.1993); *ABC Mobile Brakes, Division of D.A.Mote, Inc. v. Leyland*, 84 A.D.2d 914, 446 N.Y.S.2d 660 (4th Dept.1981). Most important, plaintiff fails to raise an issue of fact that Jay Advertising and it are competitors in any sense of the word other than that any two employers would like the services of a good employee. To the extent that interest is affected by the alleged recruitment here, it is not one of those interests which permit enforcement of a restrictive covenant in this state. *See Labriola v. Pollard Group, Inc.*, 152 Wash.2d 828, 847, 100 P.3d 791, 800 (2004) (holding unenforceable a restraint "designed to stabilize a company's current workforce"); *Schmersahl, Treloar & Co., P.C. v. McHugh*, 28 S.W.3d 345, 350 (Mo.Ct.App.E.D.2000) ("rationale for protecting trade secrets and customer contacts does not extend to protecting an employer's interest in keeping at-will employees from leaving their employment"). Cf., *National Employment Service Corporation v. Olsten Staffing Service, Inc.*, 145 N.H. 158, 161, 761 A.2d 401, 405 (2000) ("although there may be valid reasons to restrictive covenants, the mere cost associated with recruiting and hiring employees is not a legitimate interest protectable by a restrictive covenant in an employment contract"). Cf., *Lockheed Martin Corp. v. Aatlas Commerce, Inc.*, 283 A.D.2d 801, 803, 725 N.Y.S.2d 722 (3d Dept.2001); *Headquarters Buick-Nissan, Inc. v. Michael Oldsmobile*, 149 A.D.2d 302 303-04, 539 N.Y.S.2d 355 (1st Dept.1989) ("nor is the mere inducement of an at will employee to join a competitor actionable, unless dishonest means are employed, or the solicitation is part of a scheme ***434** designed to produce damage"). Accordingly, defendant establishes as a matter of law that, in these circumstances involving no competition, and no confidential or proprietary information at stake, no legitimate interest of the employer is served by the covenant, and plaintiff raises no issue of fact warranting a trial.

Conclusion

Defendant's cross-motion for summary judgment is granted. *Giuffrida v. Citibank Corporation*, 100 N.Y.2d 72, 760 N.Y.S.2d 397, 790 N.E.2d 772 (2003); ****840***Alvarez v. Prospect Hospital*, 68 N.Y.2d 320, 508 N.Y.S.2d 923, 501 N.E.2d 572 (1986).

SO ORDERED.

N.Y.Sup.,2005.
Lazer Inc. v. Kesselring
13 Misc.3d 427, 823 N.Y.S.2d 834, 2005 N.Y. Slip Op. 25587

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TAB 8

224 P.3d 355, 158 Lab.Cas. P 60,837, 29 IER Cases 460
(Cite as: 224 P.3d 355)

Colorado Court of Appeals,
Div. I.
LUCHT'S CONCRETE PUMPING, INC., a Colorado corporation, Plaintiff-Appellant,
v.
Tracy HORNER and Everist Materials, LLC, d/b/a Peak Concrete Pumping, an Iowa limited liability company, Defendants-Appellees.
No. 08CA0936.

June 11, 2009.

Background: Former employer brought action against former employee and employee's new employer, alleging violation of noncompete agreement, violation of duty of loyalty, and misappropriation of trade value. The District Court, Summit County, David R. Lass, J., entered summary judgment in favor of employee on noncompete agreement claim, and entered judgment following bench trial in favor of defendants on all remaining claims. Employer appealed.

Holdings: The Court of Appeals, Román, J., held that:
(1) as a matter of first impression, continued employment was not sufficient consideration for noncompete agreement;
(2) employee did not owe a "heightened" duty of loyalty to employer;
(3) employee, a manager with sufficient authority to create a principal-agent relationship, owed duty of loyalty to employer;
(4) employee did not violate duty of loyalty;
(5) trial court was required to issue ruling on claim; and
(6) evidence did not support claim for misappropriation of trade value.

Affirmed.

West Headnotes

[1] Contracts 95 65.5

95 Contracts
95I Requisites and Validity
95I(D) Consideration
95k65.5 k. Covenants not to compete. Most Cited Cases
Continued employment was not sufficient consideration for noncompete agreement signed by already-existing employee.

[2] Contracts 95 65.5

95 Contracts
95I Requisites and Validity
95I(D) Consideration
95k65.5 k. Covenants not to compete. Most Cited Cases
When an employee continues his or her job without receiving additional pay or benefits when a noncompete agreement is signed, the agreement lacks consideration; under these circumstances, additional consideration is required for the valid formation of the agreement.

[3] Contracts 95 65.5

95 Contracts
95I Requisites and Validity
95I(D) Consideration
95k65.5 k. Covenants not to compete. Most Cited Cases
A covenant not to compete must be supported by consideration.

[4] Contracts 95 50

95 Contracts
95I Requisites and Validity
95I(D) Consideration
95k49 Nature and Elements
95k50 k. In general. Most Cited Cases
"Consideration" is defined as something, such as an act, a forbearance, or a return promise, bargained for and received by a promisor from a promisee; that which motivates a person to do something, especially to engage in a legal act.

[5] Labor and Employment 231H 111

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk109 Employee's Duties
231Hk111 k. Fiduciary duty. Most Cited Cases
In Colorado there exists simply a duty of loyalty arising out of the employer-employee relationship; there is no "heightened" duty owed by employee to employer.

[6] Labor and Employment 231H ⚷111

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk109 Employee's Duties
231Hk111 k. Fiduciary duty. Most Cited Cases
If an employee is deemed an agent of the employer, the resulting relationship is fiduciary. Restatement (Third) of Agency § 1.01.

[7] Labor and Employment 231H ⚷111

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk109 Employee's Duties
231Hk111 k. Fiduciary duty. Most Cited Cases
Duty of loyalty owed by employee to employer applies in situations where an employer establishes that an employee has sufficient authority to create a principal-agent relationship. Restatement (Second) of Agency § 387; Restatement (Third) of Agency § 1.01.

[8] Labor and Employment 231H ⚷111

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk109 Employee's Duties
231Hk111 k. Fiduciary duty. Most Cited Cases
Employee, a manager at concrete pumping business with sufficient authority to create a principal-agent relationship, owed duty of loyalty to employer; employee maintained extensive customer relationships, was responsible for recruiting employees and for reporting on future work, held limited pricing authority, managed many aspects of certain customer accounts, supervised the work of other employees, and had ongoing personal contact with many important clients. Restatement (Second) of Agency § 387.

[9] Labor and Employment 231H ⚷114(2)

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk109 Employee's Duties
231Hk114 Conflict of Interest
231Hk114(2) k. Self-serving conduct. Most Cited Cases
An employee's duty of loyalty applies to both solicitation of customers and the solicitation of coworkers.

[10] Labor and Employment 231H ⚷155(2)

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk143 Actions by Employer Against Employee
231Hk155 Trial
231Hk155(2) k. Questions of law or fact. Most Cited Cases
Whether an employee owes an employer a duty of loyalty is typically a question of fact, but it can be analyzed as a matter of law in certain circumstances.

[11] Labor and Employment 231H ⚷114(2)

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk109 Employee's Duties
231Hk114 Conflict of Interest
231Hk114(2) k. Self-serving conduct. Most Cited Cases
Employee, a manager at concrete pumping business, did not violate duty of loyalty to employer by his conversing with competitor and assessing competitor's equipment needs; there was no evidence that employee solicited his employer's customers or employees or disclosed any trade secrets or proprietary information to competitor, and extent of conversations regarding the equipment prior to employee's

termination was minimal.

[12] Antitrust and Trade Regulation 29T ⚷520

29T Antitrust and Trade Regulation
29TVI Antitrust Regulation in General
29TVI(A) In General
29Tk520 k. In general. Most Cited Cases
Colorado favors a policy of free and vigorous economic competition.

[13] Labor and Employment 231H ⚷114(2)

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk109 Employee's Duties
231Hk114 Conflict of Interest
231Hk114(2) k. Self-serving conduct. Most Cited Cases
In light of state's policy of free and vigorous economic competition, an employee is entitled to take certain steps to prepare for competition with his or her employer after termination of employment.

[14] Labor and Employment 231H ⚷114(2)

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk109 Employee's Duties
231Hk114 Conflict of Interest
231Hk114(2) k. Self-serving conduct. Most Cited Cases
In evaluating whether an employee's actions constitute mere preparation for competition or active competition in violation of a duty of loyalty, courts focus on the nature of the preparations to determine whether a breach has occurred. Restatement (Third) of Agency § 8.04.

[15] Labor and Employment 231H ⚷155(2)

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk143 Actions by Employer Against Employee
231Hk155 Trial
231Hk155(2) k. Questions of law or fact. Most Cited Cases
Whether an employee's actions constitute a breach of his duty of loyalty involves a question of fact to be determined by the trial court in the first instance based on a consideration of all the circumstances of the case.

[16] Labor and Employment 231H ⚷114(2)

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk109 Employee's Duties
231Hk114 Conflict of Interest
231Hk114(2) k. Self-serving conduct. Most Cited Cases
An employee does not have a duty to disclose to employer his or her plans to compete. Restatement (Third) of Agency § 8.04.

[17] Appeal and Error 30 ⚷1177(8)

30 Appeal and Error
30XVII Determination and Disposition of Cause
30XVII(D) Reversal
30k1177 Necessity of New Trial
30k1177(8) k. Insufficiency of verdict or findings. Most Cited Cases
Trial court was required to issue a ruling on former employer's claim for misappropriation of business value based on former employee's retention of cellular telephone number while working for competitor, his new employer.

[18] Labor and Employment 231H ⚷307(1)

231H Labor and Employment
231HV Intellectual Property Rights and Duties
231Hk304 Trade Secrets or Confidential Information
231Hk307 Particular Trade Secrets or Information Protected
231Hk307(1) k. In general. Most Cited Cases

Labor and Employment 231H ⚷307(3)

231H Labor and Employment
231HV Intellectual Property Rights and Duties
231Hk304 Trade Secrets or Confidential In-

formation
231Hk307 Particular Trade Secrets or Information Protected
231Hk307(3) k. Customer information. Most Cited Cases
Evidence did not support former employer's claim against former employee and employee's current employer for misappropriation of trade value based on employee's alleged disclosure of former employer's business plan and established customer relationships; both employers, involved in concrete pumping business, had the same customers in the region and planned to grow their businesses through greater customer relationships, not novel business plans.
***357** Arckey & Reha, LLC, John F. Reha, Sara E. Yelton, Littleton, Colorado, for Plaintiff-Appellant.

Baker & McKenzie, LLP, Thomas Campbell, Chicago, Illinois; Letofsky & Dombrowski, Steven F. Letofsky, Frisco, Colorado, for Defendants-Appellees.

Opinion by Judge ROMÁN.

Plaintiff, Lucht's Concrete Pumping, Inc. (LCP), appeals the trial court's judgments in favor of defendants, Tracy Horner and Everist Materials, LLC (Everist), on claims regarding a noncompete agreement, duty of loyalty, and misappropriation of trade value. We affirm in part, reverse in part, and remand with directions.

I. Background

According to the trial court's findings of fact, LCP is in the concrete pumping business. Concrete pumpers use pumps that are mounted on trucks to deliver ready-mixed concrete to a construction site. Defendant Horner came to work for LCP as its mountain division manager in 2001. LCP understood that the key to the success or failure of its mountain division depended upon Horner and the relationships he would establish in that region. No other LCP employee possessed meaningful customer relationships in that region.

On April 15, 2003, two years after going to work for LCP, Horner, an at-will employee, was asked to sign, and did sign, an "employee non-disclosure and confidentiality agreement." The agreement stated, among other things, that in the event of Horner's termination, he agreed to return all company property and documents and further agreed not to compete with LCP for a period of twelve months following his termination.

Horner resigned from LCP on March 12, 2004.

Three days later, on March 15, 2004, Horner began working for Everist. Everist is a supplier of ready-mix concrete and had many of the same customers in the mountain region as LCP. Shortly after Horner began working for Everist, Everist entered the concrete pumping business and began directly competing against LCP. Everist and Horner had begun discussing the possibility of Everist entering the concrete pumping business-and bringing Horner over as its pumping manager-as early as February 2004.

LCP alleged at trial that Everist's entry into the concrete pumping market, with Horner as its pumping manager, directly led to LCP's demise in the mountain region and further alleged that its decision to discontinue its business in that territory was a direct result of Everist's competition and Horner's decision to work for Everist.

LCP sued Horner for breach of contract, breach of duty of loyalty, breach of fiduciary duty, and misappropriation of trade values. It also sued Everist for aiding and abetting breach of duty of loyalty, aiding and abetting breach of fiduciary duty, intentional interference with contract, and misappropriation of trade values.

The trial court granted summary judgment in favor of Horner on the noncompete agreement, concluding that the agreement was unenforceable due to lack of consideration. Following a bench trial, the court issued a judgment that included extensive findings of fact and found in favor of Horner and Everist on all remaining claims.

This appeal followed.

II. Noncompete Agreement

LCP contends the trial court erred in ruling as a matter of law that the noncompete agreement signed by Horner was unenforceable for lack of consideration. We conclude that continued employment was not sufficient ***358** consideration; instead, independent consideration was required to make the noncompete agreement at issue enforceable.

A. Standard of Review

Summary judgment is appropriate when the pleadings and supporting documentation demonstrate that no genuine issue of material fact exists and the moving party is entitled to judgment as a matter of law. C.R.C.P. 56(c); *Martini v. Smith,* 42 P.3d 629, 632 (Colo.2002). Appellate review of a summary judgment is de novo. *Martini,* 42 P.3d at 632.

B. Consideration

[1][2] We are asked to decide whether the continued employment of an already existing employee constitutes consideration for a noncompete agreement. This is a matter of first impression in Colorado. We hold that when an employee continues his or her job without receiving additional pay or benefits when a noncompete agreement is signed, the agreement lacks consideration. Under these circumstances, additional consideration is required for the valid formation of the agreement.

[3][4] A covenant not to compete must be supported by consideration. *Freudenthal v. Espey,* 45 Colo. 488, 499, 102 P. 280, 283-84 (1909). "Consideration is defined as '[s]omething (such as an act, a forbearance, or a return promise) bargained for and received by a promisor from a promisee; that which motivates a person to do something, [especially] to engage in a legal act.' " *Int'l Paper Co. v. Cohen,* 126 P.3d 222, 225 (Colo.App.2005) (quoting *Black's Law Dictionary* 324 (8th ed.2004)); *see* *Compass Bank v. Kone,* 134 P.3d 500, 502 (Colo.App.2006) (consideration may be "a benefit received or something given up as agreed upon between the parties" (quoting CJI-Civ. 4th 30:5 (1998))).

Here, after already working for LCP, Horner was asked to and did execute a noncompete agreement. However, he was not given a pay increase, promotion, or additional benefits in consideration of his new commitment. In short, Horner did not receive anything in return for his promise not to compete.

LCP contends that Horner's continued employment is sufficient consideration. We reject this contention. We have found no Colorado case where an already employed worker is required to give up something in exchange for merely continuing employment. Colorado law guides us to the conclusion that continued employment under the same terms is insufficient to constitute consideration, that is, a benefit received or thing given. *See* *Compass Bank,* 134 P.3d at 502.

In *Metropolitan State Faculty Federation v. State,* 32 Colo.App. 420, 425, 514 P.2d 784, 786 (1973), another division of this court found valid consideration where employees received employment to which they were not previously entitled under an earlier contract and therefore received a benefit in exchange for modifications to a second contract. Here, in contrast, Horner was already employed by LCP and received no additional benefit for his promise not to compete.

LCP asks us to hold, as some other jurisdictions have done, that an employer's forbearance of its right to discharge an at-will employee is sufficient consideration. *See* *Lake Land Emp. Group of Akron, LLC v. Columber,* 101 Ohio St.3d 242, 804 N.E.2d 27, 31-32 (2004). However, a covenant not to compete is unlike other "proposal[s] to renegotiate the terms of the parties' at-will employment." *Id.* at 32. Accordingly, we decline to so hold. Covenants not to compete not only are disfavored in Colorado, *see* *Nat'l Propane Corp. v. Miller,* 18 P.3d 782, 787 (Colo.App.2000), but also require an employee's promises that endure beyond the at-will relationship. While an employer may agree to continue an at-will employee's employment if the employee agrees to sign the covenant, nothing prevents the employer from discharging the employee at any future date. Thus, the employer's promise requires nothing more than was already promised in the original at-will agreement. *See* *Midwest Sports Mktg., Inc. v. Hillerich & Bradsby of Canada, Ltd.,* 552 N.W.2d 254, 265-66 (Minn.Ct.App.1996) (employee "received only a promise of employment and did not gain any real advantage by signing the noncompetition agreement"); ***359***Labriola v. Pollard Group, Inc.,* 152 Wash.2d 828, 100 P.3d 791, 796 (2004) (consideration lacking because "[e]mployer simply promised to perform what he promised [e]mployee in the original ... agreement in exchange for [e]mployee taking on the additional promise to not compete").

Conversely, the employee's promise to refrain from competition lasts months or years beyond the termination date. Thus, an independent consideration requirement "reflects the fact that employers and employees have unequal bargaining power." Sanborn Mfg. Co. v. Currie, 500 N.W.2d 161, 164 (Minn.Ct.App.1993); *see* Colo. Accounting Machs., Inc. v. Mergenthaler, 44 Colo.App. 155, 156, 609 P.2d 1125, 1126 (1980) (legislative intent of Colorado statute disfavors noncompetition agreements).

Although our supreme court has identified situations where continued employment may furnish the necessary consideration to make a policy or procedure binding upon an employer, *see* Kuta v. Joint Dist. No. 50(J), 799 P.2d 379, 382 (Colo.1990); Cont'l Air Lines, Inc. v. Keenan, 731 P.2d 708, 711-12 (Colo.1987), those cases are significantly different because they deal with benefits, rather than restrictions, construed in favor of employees, involve policies or procedures that are offered to a group of employees, and involve actions brought by employees to enforce an employer's promise. Kuta, 799 P.2d at 382; Cont'l Air Lines, 731 P.2d at 711-12. Additionally, the cases also require a finding that the "continued employment constituted acceptance of and consideration for" the new policies and procedures. Cont'l Air Lines, 731 P.2d at 711. As such, it is consistent to find consideration for continued employment in cases involving employee benefits but not for noncompete agreements involving already existing employees. *Compare* Pine River State Bank v. Mettille, 333 N.W.2d 622, 626-27 (Minn.1983) (Minnesota Supreme Court holds handbook policies binding upon employer where employee continued working with knowledge of the new or changed conditions), *with* Nat'l Recruiters, Inc. v. Cashman, 323 N.W.2d 736, 741 (Minn.1982) (Minnesota Supreme Court requires independent consideration for noncompete agreement).

Other jurisdictions have also held that continued employment, without any additional factor, is insufficient consideration for an employee's agreement not to compete. In Poole v. Incentives Unlimited, Inc., 345 S.C. 378, 548 S.E.2d 207, 209 (2001), the South Carolina Supreme Court concluded that when an employee's duties, position, and salary were left unchanged, a covenant not to compete entered after the employee began working was unenforceable for lack of consideration. Likewise, the Washington Supreme Court concluded that "[i]ndependent, additional[ ] consideration is required for the valid formation of a modification or subsequent agreement." Labriola, 100 P.3d at 794. The court explained that "[i]ndependent consideration involves new promises or obligations previously not required of the parties." Id.

We are persuaded by the rationale in these cases and in others that have similarly held that continued employment does not create consideration for a noncompete agreement once an employee has begun working for an employer. *See, e.g.,* Nat'l Recruiters, 323 N.W.2d at 741; Access Organics, Inc. v. Hernandez, 341 Mont. 73, 175 P.3d 899, 903 (2008); Stevenson v. Parsons, 96 N.C.App. 93, 384 S.E.2d 291, 293 (1989); George W. Kistler, Inc. v. O'Brien, 464 Pa. 475, 347 A.2d 311, 316 (1975); Martin v. Credit Prot. Ass'n, 793 S.W.2d 667, 670 (Tex.1990); PEMCO Corp. v. Rose, 163 W.Va. 420, 257 S.E.2d 885, 890 (W.Va.1979); Worley v. Wyo. Bottling Co., 1 P.3d 615, 621 (Wyo.2000).

Consequently, we conclude the trial court did not err in refusing to enforce the noncompete agreement.

III. Duty of Loyalty

LCP further contends the trial court misapplied the law established under Jet Courier Service, Inc. v. Mulei, 771 P.2d 486 (Colo.1989) (Mulei), when it determined that Horner did not breach a duty of loyalty to LCP. Although we agree that the trial court incorrectly applied the legal standards set forth in Mulei and later in Graphic Directions, Inc. v. Bush, 862 P.2d 1020 (Colo.App.1993), we perceive no error in the trial court's determination that Horner did not breach his duty of loyalty.

***360** In its judgment following the bench trial, the trial court determined that (1) Horner owed LCP a duty of loyalty, (2) Horner did not breach his duty of loyalty because his discussions with Everist and evaluation of pumping equipment were legally sanctioned pretermination activities, (3) Horner did not owe LCP a fiduciary duty, and (4) consequently, he did not breach any alleged fiduciary duty.

A. Duty of Loyalty Arising Out of Employer-Employee Relationship

[5] LCP first contends the trial court erred in determining that Horner did not owe it a "heightened" duty. We disagree that there exists a heightened duty and reaffirm that in Colorado there exists simply a duty of loyalty arising out of the employer-employee relationship.

In *Mulei,* the supreme court acknowledged that the parties in that case had characterized the duty of loyalty as a "fiduciary" duty of loyalty. *Mulei,* 771 P.2d at 492 n. 10. The *Mulei* court declined, however, to "delineate the precise scope of an employee's duty of loyalty as applied to all factual situations," and chose to label the duty at issue in that case "simply as a 'duty of loyalty' arising out of the employer-employee relationship." *Id.*

[6] We thus do not read *Mulei* to create a heightened duty of loyalty in the employment context. Indeed, the duty of loyalty that an employee owes his or her employer is largely derived from Restatement (Second) of Agency § 387 (1958). *Mulei,* 771 P.2d at 492. If an employee is deemed an agent of the employer, the resulting relationship is fiduciary. *See* Restatement (Third) of Agency § 1.01 (2006) ("Agency is the fiduciary relationship that arises when one person (a 'principal') manifests assent to another person (an 'agent') that the agent shall act on the principal's behalf...."); *Mulei,* 771 P.2d at 492 n. 10 (duty of loyalty applies when "the principal/agent analogy is apt beyond question"). Consequently, the employee in *Mulei* owed a fiduciary duty because he had sufficient authority, giving rise to the principal/agent analogy. *Id.*[FN1]

> FN1. The *Mulei* court acknowledged that there may be cases where an employee may not owe a duty of loyalty at all or for situations where an employee's duty of loyalty may not apply "in all its rigor ... regardless of the nature of the work performed." 771 P.2d at 492 n. 10. However, here, as in *Mulei,* we do not need to determine how broad the spectrum of the duty might be.

Likewise, in *Graphic Directions, Inc.,* an employer brought a claim for breach of fiduciary duty after three employees opened a competing business. There, another division of this court stated that under *Mulei,* "there may be circumstances under which the duty of loyalty does not apply to an employee." *Graphic Directions, Inc.,* 862 P.2d at 1023. However, that division likewise determined that the employee in that case held a position of sufficient authority to subject him to the duty established in *Mulei. Id.* The division's analysis in *Graphic Directions, Inc.* mirrored that of *Mulei.*

[7] To summarize, the duty of loyalty defined in *Mulei* and *Graphic Directions, Inc.* applies in situations where an employer establishes that an employee has sufficient authority to create a principal-agent relationship.

B. Whether Horner Owed a Duty of Loyalty

[8] We agree with the trial court that Horner owed LCP a duty of loyalty because he was a manager with sufficient authority that the principal/agent analogy is apt.

[9] The Restatement (Second) of Agency § 387 (1958) states that "an agent is subject to a duty to his principal to act solely for the benefit of the principal in all matters connected with his agency." It follows that an agent has a corresponding duty "not to compete with the principal concerning the subject matter of his agency." Restatement (Second) of Agency § 393 (1958). An employee's duty of loyalty applies to both solicitation of customers and the solicitation of coworkers. *Mulei,* 771 P.2d at 492.

[10] Whether an employee owes an employer a duty of loyalty is typically a question of fact, but it can be analyzed as a matter of law in certain circumstances. ***361***Graphic Directions, Inc.,* 862 P.2d at 1022 (citing *Paine, Webber, Jackson & Curtis, Inc. v. Adams,* 718 P.2d 508, 518 (Colo.1986)). Where, as here, the trial court's factual findings have ample record support, the legal effect of those facts is a question of law. *Golden Lodge No. 13, Indep. Order of Odd Fellows v. Grand Lodge of Indep. Order of Odd Fellows,* 80 P.3d 857, 859 (Colo.App.2003). We review de novo the court's application of the governing legal standards. *Lawry v. Palm,* 192 P.3d 550, 558 (Colo.App.2008).

Horner and Everist argue that, unlike the employees in *Mulei* and *Graphic Directions, Inc.,* Horner did not hold a position of sufficient authority and, therefore, is not subject to the same duty of loyalty. We disagree because the trial court found that Horner maintained extensive customer relationships, was responsible for recruiting employees and for reporting on future work, and held limited pricing authority. Much like the employees in Graphic Directions, Inc., Horner managed many aspects of certain customer accounts, supervised the work of other employees, and more important, had ongoing personal contact with many important clients. *See* Graphic Directions, Inc., 862 P.2d at 1023.

The trial court's findings of fact are supported by the record and we therefore accept them. We thus conclude that Horner's position was one of sufficient authority so that the principal/agent analogy is apt beyond question. *See* id. Horner owed LCP a duty of loyalty.

C. Whether Horner Breached His Duty of Loyalty

[11] To establish a claim for relief, it is insufficient to show only that an employee owed a duty of loyalty; instead, it must also be shown that the employee breached that duty of loyalty. We turn next to whether the trial court erred in finding that Horner did not breach his duty of loyalty, and we perceive no error.

[12][13][14] Colorado favors a policy of "free and vigorous economic competition." *Mulei,* 771 P.2d at 493. In light of that policy, an employee is entitled to take certain steps to prepare for competition with his or her employer after termination of employment. In evaluating whether an employee's actions constitute mere preparation or active competition, courts focus on the nature of the preparations to determine whether a breach has occurred. *Id.* at 492-93; *Graphic Directions, Inc.,* 862 P.2d at 1023; *see* Restatement (Third) of Agency § 8.04 (2006) (during period of agency relationship, "agent may take action, not otherwise wrongful, to prepare for competition following termination of the agency relationship").

[15] "[W]hether an employee's actions constitute a breach of his [or her] duty of loyalty involves a question of fact to be determined by the trial court in the first instance based on a consideration of all the circumstances of the case." *Mulei,* 771 P.2d at 494.

LCP maintains Horner breached his duty of loyalty by withholding key information as to Everist's impending large-scale entry into the pumping market and by actively helping Everist enter into that market in direct competition with LCP while Horner was still in LCP's employ. Specifically, LCP asserts that Horner failed to disclose that he was going to work for Everist, that he was leaving LCP just before the start of the construction season, and that Everist was buying pumps that would allow it to dominate the market.

[16] The trial court found that Horner conversed with Everist while still in LCP's employ and that Horner was aware of Everist's preparations to enter the concrete pumping business. However, an employee does not have a duty to disclose his or her plans to compete. Restatement (Third) of Agency § 8.04 cmt. c (2006) ("In this respect, the social benefits of furthering competition outweigh the principal's interest in full disclosure by its agents."); *Allied Supply Co. v. Brown,* 585 So.2d 33, 35 (Ala.1991) (employee has no duty to disclose plans to resign even when resignation is followed by competition with former employer).

Moreover, the trial court found no evidence that Horner solicited LCP customers or employees or disclosed any trade secrets or proprietary information. *Cf.* ***362***Graphic Directions, Inc.,* 862 P.2d at 1024 (breach of duty where employees solicited other employees and customers while still employed by employer); *Koontz v. Rosener,* 787 P.2d 192, 196 (Colo.App.1989) (breach of duty where employees agreed to terminate their employment en masse and set up a competing business); *Maryland Metals, Inc. v. Metzner,* 282 Md. 31, 382 A.2d 564, 569-70 (1978) (breach of duty where employee solicited customers prior to termination).

Although the trial court found some evidence to support LCP's claim that Horner was involved in assessing Everist's equipment needs and attended an equipment demonstration on behalf of Everist, the trial court determined that the product demonstration occurred after Horner's termination and that the extent of prior conversations regarding the equipment was minimal. Notably, permissible pretermination activities include "arranging for space and equipment." Restatement (Third) of Agency § 8.04 cmt. c (2006); *Veco Corp. v. Babcock,* 243 Ill.App.3d 153, 183 Ill.Dec. 406, 611 N.E.2d 1054, 1059 (1993) ("employees may plan, form, and outfit a competing corporation while still working for the employer but may not commence competition").

Accordingly, we perceive no error in the trial court's conclusion that Horner did not breach his duty of loyalty.

Based on this outcome, we need not address LCP's contentions that Everist aided and abetted Horner's alleged breach of duty.

IV. Misappropriation of Business Value

[17] We agree with LCP, however, that the trial court erred when it did not issue a ruling on its claim for misappropriation of business value based on defendants' retention of Horner's cellular telephone number. We thus remand to the trial court to issue a conclusion of law consistent with its extensive findings of fact on this claim. *See* *Bob Blake Builders, Inc. v. Gramling,* 18 P.3d 859, 866 (Colo.App.2001) (remand is appropriate remedy when trial court order lacks sufficient findings of fact or conclusions of law for appellate review); *see also* *People v. Ingram,* 984 P.2d 597, 604 (Colo.1999).

[18] LCP also argues that its business plan and Horner's established customer relationships constitute business values. We agree with the trial court that neither claim alleges sufficient novelty as required for misappropriation of an idea as business value. *See* *Smith v. TCI Communications, Inc.,* 981 P.2d 690, 694 (Colo.App.1999) (to support a claim for misappropriation based upon an idea, that idea must be novel). The evidence at trial was that both companies had the same customers in the mountain region and planned to grow their businesses through greater customer relationships, not novel business plans.

Finally, we deny LCP's request for costs on appeal. *See* C.A.R. 39(a) ("if a judgment is affirmed or reversed in part, or is vacated, costs shall be allowed only as ordered by the court").

The judgment is reversed as to LCP's claim for misappropriation of business value based on defendants' retention of Horner's cellular telephone number, and the case is remanded to the trial court for conclusions of law consistent with its findings of fact regarding that claim. In all other respects, the judgment is affirmed.

Judge TAUBMAN and Judge LICHTENSTEIN concur.
Colo.App.,2009.
Lucht's Concrete Pumping, Inc. v. Horner
224 P.3d 355, 158 Lab.Cas. P 60,837, 29 IER Cases 460

END OF DOCUMENT

TAB 9

C

NOTE: THIS OPINION WILL NOT APPEAR IN A PRINTED VOLUME. THE DISPOSITION WILL APPEAR IN A REPORTER TABLE.

Court of Appeals of North Carolina.
MSC INDUSTRIAL DIRECT CO., INC., Plaintiff,
v.
James Gregory STEELE, Defendant.
No. COA08-418.

Aug. 18, 2009.

West KeySummary

Contracts 95 ⚷65.5

95 Contracts
95I Requisites and Validity
95I(D) Consideration
95k65.5 k. Covenants Not to Compete. Most Cited Cases

Labor and Employment 231H ⚷305

231H Labor and Employment
231HV Intellectual Property Rights and Duties
231Hk304 Trade Secrets or Confidential Information
231Hk305 k. In General. Most Cited Cases

A grant of restricted shares to employee was not proper consideration for a confidentiality, non-solicitation, and non-competition agreement. The grant of the shares was made more than thirty days before the agreement was entered. Employee had no rights to the shares when they were granted but merely an expectation of rights in the future. Also, the employer reserved all rights to terminate employee at any time without cause. Any value in the grant of shares was illusory.

*1 Appeal by plaintiff from an order entered 30 January 2008 by Judge W. David Lee in Union County Superior Court. Heard in the Court of Appeals 22 October 2008.

Jackson Lewis, LLP, by Paul H. Derrick, for plaintiff-appellant.

Black Ruth Grossman & Cain, P.A., by Aimee E. Cain and Lucas T. Baker, for defendant-appellee.

JACKSON, Judge.

MSC Industrial Direct Co., Inc. ("plaintiff") appeals the 30 January 2008 denial of a preliminary injunction and dissolution of a temporary restraining order. For the reasons stated below, we affirm.

Plaintiff, a direct marketer of industrial products, hired James Gregory Steele ("defendant") on 17 October 1994 as an Outside Sales Associate. He was promoted to the position of Senior Account Executive in 1999. On 19 August 2005, defendant signed an Associate Confidentiality, Non-Solicitation and Non-Competition Agreement in connection with his having been given the use of a company car.

On 19 February 2006, defendant signed a second Associate Confidentiality, Non-Solicitation and Non-Competition Agreement ("the Agreement") which, pursuant to its terms, superceded "any and all prior agreements or understandings" between the parties. The Agreement stated that defendant signed it in exchange for (1) restricted shares of plaintiff's stock, (2) his continued employment, (3) his compensation, and (4) plaintiff's entrustment to him of confidential information related to its business. Plaintiff terminated defendant's employment on 11 May 2007 for alleged violations of the Agreement. In August 2007, defendant began working for Hagemeyer North America, one of plaintiff's competitors.

On 10 October 2007, plaintiff filed a complaint in Union County Superior Court seeking a temporary restraining order ("TRO") and preliminary injunction, enjoining and restraining defendant from engaging in allegedly restricted activity. Also on that date, plaintiff filed a motion seeking the same relief. An order granting a TRO in favor of plaintiff was filed 11 October 2007. Defendant's deposition was taken on the morning of 21 December 2007, and a Consent Temporary Restraining Order was filed later that afternoon. Plaintiff's motion for a preliminary injunction was heard 14 January 2008. The trial court denied the motion and dissolved the TRO. Plaintiff appeals.

As a preliminary matter, we must determine if this appeal has been brought prematurely. "A preliminary injunction is interlocutory in nature and therefore not immediately appealable unless it deprives the appellant of a substantial right that he would lose absent immediate review." *Redlee/SCS Inc. v. Pieper,* 153 N.C.App. 421, 423, 571 S.E.2d 8, 11 (2002) (citing *Wade S. Dunbar Ins. Agency, Inc. v. Barber,* 147 N.C.App. 463, 466, 556 S.E.2d 331, 334 (2001)).

In *QSP, Inc. v. Hair,* 152 N.C.App. 174, 566 S.E.2d 851 (2002), this Court noted that "[i]n cases involving an alleged breach of a non-competition agreement and an agreement prohibiting disclosure of confidential information, North Carolina appellate courts have routinely reviewed interlocutory court orders both granting and denying preliminary injunctions holding that substantial rights have been affected." *Id.* at 175, 566 S.E.2d at 852. *QSP* went on to hold that the denial of a preliminary injunction "(1) prohibiting defendant from using or disclosing QSP's confidential information and trade secrets and (2) prohibiting defendant from soliciting for one year the same customers defendant solicited while working for QSP" would deprive the plaintiff of a substantial right absent a review prior to a final determination. *Id.* at 176, 566 S.E.2d at 852. As plaintiff in the case *sub judice* sought a similar preliminary injunction, which was denied, the appeal is appropriate for our review at this time.

*2 We first address defendant's contention that the issue is moot because the period covered by the Agreement has passed. We disagree.

"Whenever, during the course of litigation it develops that ... the questions originally in controversy between the parties are no longer at issue, the case should be dismissed, for courts will not entertain or proceed with a cause merely to determine abstract propositions of law." *In re Peoples,* 296 N.C. 109, 147, 250 S.E.2d 890, 912 (1978) (citations omitted), *cert. denied,* 442 U.S. 929, 99 S.Ct. 2859, 61 L.Ed.2d 297 (1979).

Pursuant to the terms of the Agreement, if valid, defendant is prohibited from (1) using or disclosing confidential information for so long as the information generally is not known to the public, (2) competing with plaintiff while employed there and for one year after the termination of his employment, and (3) soliciting its customers while employed there and for one year after the termination of his employment. However, in the event it is determined that defendant violated the Agreement, the duration of the second and third restrictions would be extended for an amount of time equal to the period during which such violations occurred.

Clearly, with respect to the first restriction, the restrictive period could extend indefinitely. With respect to the second and third restrictions, because defendant was terminated on 11 May 2007, with no other facts appearing, the applicable period would expire 10 May 2008, which has passed. However, it is alleged that defendant violated the Agreement. Therefore, pursuant to the Agreement the restricted period would extend for an amount of time equal to the period during which the violations occurred, if such violations are found to have occurred.

A TRO was ordered on 11 October 2007 and was to "remain in full force and effect until such time as this [c]ourt specifically orders otherwise[.]" The 11 October order also set a hearing on plaintiff's motion for 17 October 2007. It appears from defendant's deposition testimony that a hearing was held on that date and that the TRO remained in effect from that point in time. However, there is no direct evidence in the record with respect to a hearing on 17 October 2007 or at any other time prior to the deposition. The 21 December 2007 consent order does not purport to extend an existing TRO. It orders that a TRO "issue immediately" and that plaintiff post bond. This implies that an existing TRO was not in effect at that time. In any event, a TRO finally was dissolved on 14 January 2008, by order filed 30 January 2008.

With the exception of the three-month period during which a TRO was in place, defendant is alleged to have been in violation of the terms of the Agreement. As of the date of this opinion, if a court were to determine that defendant was, in fact, in violation of the Agreement, his business activities would be restricted by the Agreement's terms for a period of time equal to at least an additional twenty-four months beyond the one-year post-separation period, or at least 10 May 2010 which has not passed yet. Because the question originally in controversy between the parties-whether defendant's activities are restricted, and if so, for how long-has not been resolved, the issue is not moot.

***3** Therefore, we consider the merits of the appeal. Plaintiff argues that the trial court erred in failing to grant a preliminary injunction because it demonstrated a substantial likelihood of success on the merits. We disagree.

The scope of appellate review of a trial court's grant or denial of a preliminary injunction is essentially *de novo* because the appellate court "is not bound by the [trial court's] findings [of fact], but may review and weigh the evidence and find facts for itself." *A.E.P. Industries v. McClure,* 308 N.C. 393, 402, 302 S.E.2d 754, 760 (1983) (citations omitted).

> In considering the propriety of a preliminary injunction, this Court does not determine whether a confidentiality, no-solicitation, and non-competition agreement is in fact enforceable, but reviews the evidence and determines (1) whether plaintiff has met its burden of showing a likelihood of success on the merits and (2) whether plaintiff is likely to sustain irreparable loss unless the injunction is issued.

QSP, 152 N.C.App. at 176, 566 S.E.2d at 853 (citing *A.E.P. Industries,* 308 N.C. at 401, 302 S.E.2d at 759). However, "[w]here a preliminary injunction is sought to enforce a non[-]competition clause in an employment contract, [the Supreme] Court has held that the employment agreement itself must be valid and enforceable in order for the employer to be able to show the requisite likelihood of success on the merits." *Triangle Leasing Co. v. McMahon,* 327 N.C. 224, 227-28, 393 S.E.2d 854, 857 (1990) (citing *A.E.P. Industries,* 308 N.C. 393, 302 S.E.2d 754).

Although both parties discussed in their briefs the issue of choice of law-the Agreement called for New York law to apply-plaintiff did not assign error to the trial court's determination that North Carolina law governs the enforceability of the Agreement. "[T]he scope of review on appeal is confined to a consideration of those assignments of error set out in the record on appeal[.]" N.C. R.App. P. 10(a) (2007). Because no assignment of error addresses choice of law, the issue is not within the scope of our review. Therefore, we apply the same law the trial court did-North Carolina law.

"Under North Carolina law, covenants not to compete are valid and enforceable if: '(1) in writing; (2) made part of a contract of employment; (3) based on valuable consideration; (4) reasonable both as to time and territory; and (5) not against public policy.' " *Calhoun v. WHA Med. Clinic, PLLC,* 178 N.C.App. 585, 597, 632 S.E.2d 563, 571 (2006) (quoting *QSP,* 152 N.C.App. at 176, 566 S.E.2d at 852), *disc. rev. denied,* 361 N.C. 350, 644 S.E.2d 5 (2007). Defendant contends that plaintiff was not likely to succeed on the merits because the Agreement was unenforceable due to a lack of valuable consideration.

As stated above, there were four bases for defendant's agreeing to be bound by the Agreement's restrictive covenants. First, defendant received eighty-five "MSC Restricted Shares effective January 10, 2006, with a price of $42.86" ("the Grant") as stated consideration for entering into the Agreement. Pursuant to *Kinesis Adver., Inc. v. Hill,* 187 N.C.App. 1, 652 S.E.2d 284 (2007), *disc. rev. denied, appeal dismissed,* 362 N.C. 177, 658 S .E.2d 485 (2008), uncertificated shares of stock are valuable consideration to support a non-compete agreement entered during the course of an existing employment relationship. *Id.* at 11-12, 652 S.E.2d at 292-93. In *Kinesis,* upon our review of summary judgment, this Court determined that there was a genuine issue of material fact as to whether the shares actually had been issued. *Id.* at 13, 652 S.E.2d at 293. That is not the issue before us in the instant case. Although uncertificated shares of stock can be valuable consideration, here, the evidence of record makes clear that the stock at issue was not.

*4 On 19 February 2006, defendant signed the Agreement as well as a Restricted Stock Award ("the Award") pursuant to plaintiff's 2005 Omnibus Equity Plan ("the Plan"). Pursuant to the Award, the terms and conditions of the Grant were controlled in all respects by the Award, the Agreement, and the Plan. The Award, signed 19 February 2006, states that the "Award Date" is 10 January 2006. The Grant was transferred into an account in defendant's name on 10 January 2006-more than thirty days *before* either the Award or the Agreement was signed.

Pursuant to the Award, fifty percent of the shares would vest on 10 January 2009, seventy-five percent would vest on 10 January 2010, and the remaining shares would vest on 10 January 2011. If defendant's employment ended due to death, disability, or retirement, any unvested shares would become vested. If his employment terminated by any other means-involuntary discharge for cause, involuntary discharge without cause, or resignation-any unvested shares were to be redelivered to plaintiff. Until they vested, defendant had no right to vote the shares, no right to receive dividends, and no right of alienation.

The Award stated that it was not an employment contract. It conferred no right to continued employment and did not interfere with plaintiff's right to discharge defendant. It further stated that the Plan was discretionary on plaintiff's part and participation was voluntary on defendant's part. The Award was not to be considered as a part of defendant's salary.

Keeping in mind the terms of the Award, we see no valuable consideration for the Agreement. The Grant was made more than thirty days *before* defendant entered into the Agreement. At the time the Grant was given, defendant had no rights to the shares, merely an expectation of rights in the future. Pursuant to the terms of the Award, plaintiff retained the right to discharge defendant at any time without cause, including the right to discharge him only moments after signing the Award and the Agreement. Any value in the Grant was illusory. This Court has held that a non-compete agreement may be set aside for lack of consideration when the stated consideration is illusory. *Milner Airco, Inc. v. Morris,* 111 N.C.App. 866, 870, 433 S.E.2d 811, 814 (1993). In *Milner,* as in the case *sub judice,* the agreement recited consideration but did not actually bind the employer to any promise. *Id.*

Having determined that the stock does not constitute valid consideration, we consider the promise of continued employment and defendant's compensation as stated consideration for entering into the Agreement. Defendant had been employed by plaintiff for over ten years when he signed the Agreement. When the employer-employee relationship exists already without a restrictive covenant, any new agreement not to compete must be in the nature of a new contract based upon new consideration. *Engineering Associates v. Pankow,* 268 N.C. 137, 139, 150 S.E.2d 56, 58 (1966); *Kadis v. Britt,* 224 N.C. 154, 163, 29 S.E.2d 543, 548 (1944).

*5 "[C]ontinued employment is insufficient consideration to support a covenant not to compete where the employee receives 'no change in compensation, commission, duties, nature of employment or other consideration in exchange for signing the agreement[.]' " *Howard v. Oakwood Homes Corp.*, 134 N.C.App. 116, 121, 516 S.E.2d 879, 882 (quoting *Cox v. Dine-A-Mate, Inc.*; 129 N.C.App. 773, 776, 501 S.E.2d 353, 356, *disc. rev. denied,* 349 N.C. 355, 525 S.E.2d 449 (1998)), *disc. rev. denied,* 350 N.C. 832, 539 S.E.2d 288 (1999), *cert. denied,* 528 U.S. 1155, 120 S.Ct. 1161, 145 L.Ed.2d 1072 (2000). However, continued employment for a specified period of time constitutes consideration to support a non-compete agreement when an employment relationship already exists. *See Amdar, Inc. v. Satterwhite,* 37 N.C.App. 410, 414, 246 S.E.2d 165, 167 (new contract of employment bound the employer for an additional year), *disc. rev. denied,* 295 N.C. 645, 248 S.E.2d 249 (1978).

Here, there was no change in defendant's "compensation, commission, duties, or nature of employment" which could be consideration for the restrictive covenants. Further, as determined above, the Grant is not "other consideration" for the restrictive covenants. Plaintiff was not bound to employ defendant for any specified period of time, remaining free to terminate the relationship with or without cause at any time. Accordingly, defendant's continued employment and associated salary does not constitute valid consideration to support the Agreement.

Finally, the Agreement stated that plaintiff entrusted defendant with confidential information relating to its business as consideration. However, it appears clear that such information had been entrusted to defendant for a number of years prior to the signing of the Agreement. There was no new information entrusted to defendant, therefore, this does not constitute valid consideration.

Because pursuant to North Carolina law no valuable consideration was given in exchange for defendant's entering into the Agreement, the Agreement was not enforceable. Therefore, plaintiff was not likely to succeed on the merits and the trial court did not err in denying a preliminary injunction and dissolving the TRO.

Affirmed.

Judges STEELMAN and STROUD concur.
Report per Rule 30(e).

N.C.App.,2009.
MSC Indus. Direct Co., Inc. v. Steele
682 S.E.2d 248, 2009 WL 2501762 (N.C.App.)

END OF DOCUMENT

TAB 10

H

United States District Court,
E.D. Pennsylvania.
MEXTEL, INC., et al. Plaintiffs,
v.
AIR-SHIELDS, INC., et al. Defendants.
HILL-ROM MANUFACTURING, INC., et al. Counterclaim Plaintiffs,
v.
MEXTEL, INC., et al. Counterclaim Defendants.
No. Civ.A.01-CV-7308.

Jan. 31, 2005.

Background: Manufacturer of electronic medical assemblies brought action against health care industry service provider, alleging breach of development and supply agreement. Manufacturer moved for partial summary judgment.

Holdings: The District Court, Davis, J., held that:
(1) sensor module was not covered by agreement;
(2) fact issues existed whether manufacturer provided engineering services to service provider; and
(3) service provider failed to compensate manufacturer for controllers shipped to it.

Motions granted in part and denied in part.

[1] Sales 343 0

343 Sales
Production and supply of sensor modules was not covered by development and supply agreement, for purposes of claim brought by manufacturer of electronic medical assemblies against health care industry service provider, alleging breach of contract under Pennsylvania law; neither express terms of agreement at issue nor alternative oral or written contracts encompassed such obligations, and accounting documentation only identified date of shipping rather than type of products supplied. 13 Pa. Cons.Stat. Ann. § 2-107(a).

[2] Federal Civil Procedure 170A 0

170A Federal Civil Procedure
Genuine issues of material fact, regarding whether manufacturer of electronic medical assemblies provided engineering services to health care industry service provider and whether development and supply agreement between parties covered such services, precluded summary judgment on manufacturer's claim against provider, alleging breach of contract under Pennsylvania law.

[3] Sales 343 0

343 Sales
Manufacturer of electronic medical assemblies that sued health care industry service provider, alleging breach of development and supply agreement, established that provider failed to provide compensation for controllers that it had received, as required to maintain claim for breach of contract under Pennsylvania law; there was insufficient evidence that products at issue were non-conforming at time of their receipt. 13 Pa. Cons.Stat. Ann. § 2-606.
William C. Cagney, Lane & Mittendorf LLP, Tara Jones Hughes, Rodman E. Honecker, Windels, Marx, Lane & Mittendorf, LLP, New Brunswick, NJ, for Plaintiffs.

Philip H. Lebowitz, Erik N. Videlock, Kathleen A. Johnson, Pepper, Hamilton & Scheetz, Phila, PA, Tammy J. Meyer, A. Richard M. Blaiklock, Lewis and Wagner, Indianapolis, IN, for Defendants.

MEMORANDUM AND ORDER

DAVIS, J.

*1 Presently before the Court are Plaintiffs' Motion for Partial Summary Judgment In Favor of Plaintiffs' Contract Claims and Dismissal of Defendants' Contract Counterclaims (Doc. No. 64), filed on April 14, 2004, and all responses and supplemental briefs thereto; Plaintiffs' Second Motion for Partial Summary Judgment With Respect to the Dismissal of Patent Defenses and Counterclaims (Doc. No. 66), filed on April 14, 2004, and all responses and supplemental briefs thereto; Defendant's Motion for Summary Judgment on Plaintiffs' Amended Complaint and Count IX of Defendants' Counterclaim (Doc. No. 74), filed on April 14, 2004, and all responses and supplemental briefs thereto; Defendants' Motion to Strike Portions of Plaintiffs' Opening Brief in Support of Their First Motion for Partial Summary Judgment, First Declaration of Vedran Skulic, First Declaration of Novela Skulic, and Plaintiffs' Statement of Undisputed Material Facts in Support of Their First Motion for Partial Summary Judgment (Doc. No. 82), filed on May 6, 2004, and all responses and supplemental briefs thereto; and Defendants' Motion to Strike Portions of the Affidavit of Oleh V. Bilynsky, Third Declaration of Vedran Skulic, and Declaration of Harry Gugnani (Doc. No. 87), filed on May 19, 2004, and all responses and supplemental briefs thereto.

I. Factual and Procedural History

The genesis of this litigation stems from an arrangement between the parties for the development and supply of component medical devices. Defendant Air Shields, Inc., the successor in interest to defendant Hill-Rom Manufacturing Inc. ("Hill-Rom"),[FN1] a holding company that provides products and services for the health care industry, and plaintiff Mextel, Inc. ("Mextel"), an Illinois-based designer and manufacturer of electronic assemblies, entered into a "Development and Supply Agreement" on December 7, 1996. The Development and Supply Agreement was made retroactive to October 1995. It was supplemented with an "Addendum to the OEM Supply Agreement of October 1, 1995," which the parties executed on February 20, 1997, and by an "Amendment to the Development and Supply Agreement," which the parties executed on December 16, 1997. (*See* Addendum and Amendment, attached as Ex. 2 and 3 to Pl.App.). Collectively, these three documents shall be referred to as the "Agreement."

> FN1. Throughout the opinion, this Court refers to Hill-Rom, and its successors, including Air-Shields, collectively as "Hill-Rom."

A. The Agreement

The Agreement required Mextel to design, manufacture, and supply an electronic controller for use in the Hill-Rom's Isoletee, model C2HS infant incubator (the "C2000 incubator"). The C2000 incubator is a neonatal incubator, which, as defined by federal regulation, is a "device consisting of a rigid boxlike enclosure in which in an infant may be kept in a controlled environment for medical care...." *See* 21 C.F.R. § 880.5400. The C2000 is used for critically ill newborn premature babies. (*See* March 28, 1998 Summary of Findings, at FDA00246). The standard model of the C2000 consists of a hood/shell assembly, a heater, a controller, a sensor module, two skin temperature probes, an air temperature probe, and an air flow probe. (*Id.*). The electronic controller in the C2000 incubator is the "brain" of the device, controlling the incubator's operations and ensuring that the heating, humidity, and oxygen systems operate effectively and according to programmed specifications. (*Id.; see* Pl. Mot. For SJ., at 2).

*2 Pursuant to the Agreement, Mextel was required to comply with specific design, manufacturing, supply, and regulatory obligations. First, with respect to design obligations, Mextel was required, *inter alia,* to design the product in accordance with performance specifications prescribed by the Agreement; to provide validation of the product design to enable Hill-Rom to obtain FDA marketing clearance for the infant incubators; and to use its "best efforts" to design and provide validation of the product. (*See* Agreement, at ¶ 2.1(a); ¶ 2.1(b); ¶ 2.4(a)). Second, with respect to manufacturing obligations, Mextel was required to manufacture the controller in accordance both with manufacturing and quality assurance specifications prescribed by the Agreement and with good manufacturing practices ("GMPs") under the United States Food, Drug, and Cosmetic Act of 1938 (the "Act") and its attending regulations. (*Id.* at ¶ 6.1(a)-(b)). Third, with respect to supply obligations, Mextel was required, prior to shipment, to examine all controllers in accordance with the quality assurance procedures prescribed by the Agreement and to provide a written confirmation that the products conformed to product design specifications; to submit to quality assurance audits, as prescribed by the Agreement; to maintain all manufacturing records, including lot histories and device master records; and to provide copies of these records to Hill-Rom quarterly for all products manufactured in that quarter. (*Id.,* at ¶¶ 9.3, 9.4, 8.2). Finally, with respect to regulatory obligations, Mextel agreed to provide Hill-Rom "with any assistance reasonably required" in connection with the generation and development of data necessary to obtain FDA approval to market the incubator. (*Id.,* at ¶ 11.2).

In exchange for Mextel's development and supply of the controllers, Hill-Rom agreed to use Mextel as its exclusive supplier. (*See* Agreement, at ¶ 6.2). As such, Hill-Rom contracted to purchase a minimum of 8000 controllers throughout the life of the Agreement. (*See* Addendum to Agreement, at ¶ 2). The Agreement established an arrangement by which Hill-Rom would submit purchase orders to Mextel for the supply of the controllers. (*Id.*, at ¶ 9.7). Purchase orders were required to be placed at least fourteen weeks prior to the requested date of the shipment. (*Id.*, at ¶ 9.9). Hill-Rom was required to pay Mextel within forty days from the date of shipment of the controllers. (*Id.*, at ¶ 9.6). Hill-Rom also agreed to compensate Mextel for services associated with the development of the controller, including a non-recurring engineering charge and reasonable out-of-pocket travel expenses in connection with services performed under the Agreement. (*Id.*, at ¶ 2.2).

To ensure the exclusivity of the arrangement, Hill-Rom extended several representations and warranties to Mextel. (*Id.*, at ¶ 15.1). In ¶ 15.1(c), Hill-Rom represented and warrantied that it:

> ***3** is not currently a party to any agreement or undertaking, oral or written, that would, in any manner be inconsistent with the rights herein granted to MEXTEL to design, develop and SUPPLY a PRODUCT and shall not enter into any such agreement or understanding, oral or written, during the term of the Agreement, nor, during the term of this Agreement, directly or indirectly, engage in any activity that would, in any manner, be inconsistent with the right herein granted to MEXTEL to design, develop and SUPPLY a PRODUCT, except as specifically authorized herein.

(*Id.*, at ¶ 15.1(c)).

1. Recalls

The Agreement contained a provision expressly allocating liability for costs in the event of a "recall" of Hill-Rom's products using the controller. This provision stated that:

> In the event of a recall of any Air-Shields products that use PRODUCT [the controller] supplied by MEXTEL hereunder, when it is determined that such an event is caused by PRODUCT malfunction and not by specification or requirement change, MEXTEL shell [sic] repair or replace all such PRODUCTS. Whether it is claimed that PRODUCT is causing such an event or not, AIR-SHIELDS will indemnify, defend, and hold MEXTEL, its current directors, officers, employees, and agents harmless from and against any and all claims, liability, product and warranty liability, loss, damages, costs, or expenses.

(*See* Agreement, at ¶ 10.2). The Agreement did not define the term "recall."

2. Duration and Termination

The duration of the Agreement was for four years, with automatic renewal "for successive one (1) year term [sic] unless sooner terminated...." (*See id.*, at ¶ 16). Although not expressly referenced in the duration clause, the Agreement provided, in a separate section marked "Termination," several ways for both Hill-Rom and Mextel to end its existence. (*Id.*, at ¶¶ 18, 19).

Pursuant to ¶ 18.1 and ¶ 19.1, both parties enjoyed the right to terminate the Agreement upon the occurrence of certain enumerated events after providing sixty days written notice. (*Id.*, at ¶ 18.1, 19.1). One of these enumerated events included the noticed party's failure to meet "any of its material obligations under the Agreement." (*Id.*, at ¶ 18.1(c), 19.1(c)). Nonetheless, the noticed party retained a right to cure its default within sixty days after receipt of notice; and, if able to do so, the Agreement was to remain in effect. (*Id.*).

The Agreement also provided an additional mechanism by which Hill-Rom could terminate it:

> AIR-SHIELDS shall have the right to terminate the agreement at any time after giving sixty (60) days' written notice to MEXTEL if AIR-SHIELDS shall, in its sole discretion, determine either that the PRODUCTS are obsolete or that the infant incubators or infant radiant warmers into which such PRODUCTS are incorporated are obsolete.

(*Id.*, at ¶ 18.2). This mechanism was exclusively reserved for Hill-Rom, and, in contrast to ¶ 18.1, did not trigger a right by Mextel to cure.

3. Applicable Law

*4 The parties agreed that Pennsylvania law would apply to all disputes arising from the Agreement. (*Id.*, at ¶ 27). The parties further consented to the exercise of personal jurisdiction by the federal and state courts of Pennsylvania. (*Id.*).

B. Design and Supply of the Sensor Module

In addition to designing, manufacturing, and supplying the controller, Mextel also designed and supplied to Hill-Rom a sensor module for use in the C2000 incubator. The sensor module was the subject of United States Patent 5,957,830 ('830 patent), which was issued to plaintiff Vedran Skulic ("Skulic"), the founder and president of Mextel (collectively "plaintiffs"), on September 8, 1999. (*See* '830 Patent, attached as Ex. B to Second Skulic Declaration).FN2 The function of the sensor module was to measure the temperature, humidity, and oxygen inside the incubator, and then to feed the relevant data to the controller. (*See* Pl. Mot. For SJ., at 2).

FN2. The '830 patent is one of two patents at issue in this litigation. The other patent, U.S. Patent 5,707,006 (the " '006 patent"), was issued to Skulic on January 13, 1998. (*See* '006 Patent, attached as Ex. A to Second Skulic Declaration). The '006 patent covers a removable heater assembly for an infant incubator. (*Id.*).

The design and supply of the sensor module was not covered by the Agreement, which, according to its terms, applied only to the "electronic controller." (*See* Agreement, at ¶ 1.17). Instead, the sensor module was shipped pursuant to an informal arrangement between the parties, whereby Hill-Rom would issue purchase orders for controllers and/or sensor modules and Mextel would fill the purchase orders. (*See* Pl. Br. In Opp'n. to Def. Mot. For SJ., at 12; *see also* December 1, 1999 letter placing production hold on controllers and sensor modules, attached as Ex. 16 to Pl. Mot. For SJ.). Mextel supplied the sensor modules during the time when the Agreement was in existence. (*See* Purchase Orders, attached as Ex. 15 to Pl. Mot. For SJ.).

C. The Relationship

Between 1996 and December 1999, Mextel designed and shipped controllers and sensor modules to Hill-Rom for use in the C2000 incubator. In order to understand the collapse of this arrangement, and to frame the issues concerning liability and damages in the pending motions, it is necessary to provide: (i) a genealogical discussion of the regulatory requirements applicable to manufacturers of finished medical devices throughout the course of the parties' relationship; and (ii) a chronological recitation of the major events, correspondence, and regulatory problems associated with the C2000 incubator during the course of the parties' arrangement.

1. Regulatory Requirements

The FDA initially issued market clearance for the C2000 incubator in July 1996. (*See* July 1996 Marketing Clearance letter, attached as Ex. 8 to Pl. Mot. For SJ.). The letter reiterated that, to maintain the right to market the C2000 incubator, Hill-Rom needed to comply with GMPs pursuant to the Federal Food, Drug, and Cosmetic Act ("FDCA"), 21 U.S.C. § 301 *et seq.*, and that failure to comply with these practices could result in FDA action. (*Id.*).

The FDCA authorizes the FDA to promulgate regulations "requiring that the methods used in, and the facilities and controls used for the manufacture, preproduction design validation (including a process to access the performance of a device but not including an evaluation of the safety or effectiveness of a device), packing, storage, and installation of a device conform to current good manufacturing practice ... to assure that the device will be safe and effective and otherwise in compliance with this chapter." 21 U.S.C. § 360j(f)(1)(A) (West 2005). In 1976, the FDA promulgated a series of good manufacturing practice regulations, known as GMPs, that preemptively require manufacturers to build quality into their devices, rather than [to] permit a defective device to be distributed and used to treat patients." *U.S. v. 789 Cases, More or Less, of Latex Surgeon's Gloves,* 799 F.Supp. 1275, 1285 (D.P.R.1992). These regulations apply to manufactures of finished medical devices. *See* 21 C.F.R. § 820.1(a). Manufacturers of medical device components, on the other hand, are exempt. *Id.* ("This regulation is not intended to apply to manufacturers of components or parts of finished devices, but such manufacturers are encouraged to use appropriate provisions of this regulation as guidelines.").

***5** By 1996, the year in which the Agreement was signed, GMPs had been promulgated in the following areas connected with the manufacture of medical devices: organization and personnel; buildings; equipment; control of components; production and process controls; packaging and labeling control; holding, distribution, and installation; device evaluation; and records. *See* 21 C.F.R. Part 820. With respect to records, GMPs required (and continue to require) manufacturers to maintain product records during the design and expected life of the device. 21 C.F.R. §§ 820.180-198 (1996). Manufacturers were (and continue to be) required to keep the following: (i) a device master record ("DMR"), which includes device specifications, production process specifications, quality assurance procedures, and packing and labeling; (ii) a device history record ("DHR"), which ensures that the device was manufactured in accordance with the device master record by including the dates of manufacture, the quantity manufactured, the quantity released for distribution, and any control number used; and (iii) complaint files. *Id.*

On October 7, 1996, the FDA published the Quality System ("QS") regulation in the Federal Register. *See* Medical Devices; Current CGMP (CGMP) Final Rule; Quality System Regulation, 61 Fed.Reg. 52,602, 52,654 (Oct. 7, 1996) (to be codified at 21 C.F.R. pt 820). The QS regulation redefined GMPs, creating stricter standards for manufacturers of finished medical devices. *Id.* Although published in October 1996, the QS regulation did not take effect until June 1, 1997. *Id.* The QS regulation remains in effect today.

As part of the QS regulation, the FDA made verification and validation requirements part of GMPs. The QS regulation defines validation as "establishing by objective evidence that device specifications conform with user needs and intended use(s)." 21 CFR § 820.4(z). Verification is defined as "confirmation by examination and provision of objective evidence that specified requirements have been fulfilled." *Id.* § 820.4(aa).

The QS regulation implements verification and validation requirements through specific forms of controls, including design, production and process, and document controls. First, with respect to design controls, the QS regulation requires manufacturers of medical devices to maintain procedures for verifying the device design, which must conform to designated output meets design input requirements, and for validating the device design, which must be performed on initial production units and which must ensure that devices confirm to designed user needs and intended uses. *Id.* § 820.30(a)-(j). The results of the design verification and validation must be documented. *Id.* § 820.30(f)-(g). Furthermore, a design history file ("DHF") must be established and maintained to demonstrate "that the design was developed in accordance with the approved design plan." *Id.* § 820.30(j).

***6** Second, with respect to production and process controls, the QS regulation requires manufacturers to validate the production process with a high degree of assurance to ensure that a device confirms to its specifications, when such a process cannot be fully verified by subsequent inspections and tests. *Id.* § 820.75. The validation activities and results must also be documented. *Id.*

Third, the QS regulation imposes additional document controls and quality system controls, including the maintenance of a quality system record to document executive responsibility for, and commitment to, quality. *Id.* §§ 820.20, 820.40, 820.186.

2. Chronology of Events

Hill-Rom started placing orders for controllers from Mextel in 1996. (*See* First Declaration of Vedran Skulic, at ¶ 2). For each controller, Mextel kept "Certificates of Conformance" to certify that the product was manufactured in accordance with the specifications in the purchase order and tested according to the design specifications prescribed by the Agreement. (*Id.,* at ¶ 23; *see also* Sample Certificates of Conformance, attached as Ex. 22 to Pl. Mot. For SJ.). Nonetheless, regulatory concerns with the controller started to arise almost immediately.

In the summer of 1996, Hill-Rom started to request from Mextel documentation concerning the controller that was necessary for the C2000 incubator to comply with GMPs. On July 10, 1996, September 3, 1996, September 5, 1996, September 24, 1996, and October 11, 1996, Hill-Rom sent facsimile transmissions to Mextel demanding the immediate production of DMR documentation, DHR documentation, and verification and validation information for the controller and sensor module, and identifying the information necessary to satisfy the DMR and DHR requirements. (*See* Letters requested documentation, attached as Ex. 4B at Def. Mot. For SJ.). On November 5, 1996, plaintiff Skulic and a representative from Hill-Rom signed a certification statement indicating that complete DMR documentation had been developed for several models of the controllers, and that, although currently in an untidy and informal form, Mextel would deliver "complete" and "formalized" documentation by December 31, 1996. (*See* November 5, 1996 Certification, attached as Ex. 3A to Def. Mot. For SJ.).

In February 21, 1997, Hill-Rom again wrote to Mextel concerning the "lack of product device master record documentation" and an "unacceptable level of change controls existing between our respective firms." (*See* February 21, 1997 letter, attached as Ex. 4B to Def. Mot. For SJ.). The February 21, 1997 correspondence further asserted that "device master record documentation is past due and urgently requested." (*Id.*). On September 3, 1997, Hill-Rom sent a letter to Mextel concerning outstanding quality problems with the controller, including the lack of complete DMR documentation, and suggested that Hill-Rom was not "in a good position to withstand regulatory audit scrutiny by FDA" due to these problems. (*See* September 3, 1997 letter, attached as Ex. 4C to Def Mot. For SJ.). Indeed, the letter demanded that a complete DMR was to be provided to Hill-Rom and continuously maintained at both Mextel's and Hill-Rom's facilities. (*Id.*). Perhaps in response to these requests, on November 10, 1997, Skulic signed a letter on behalf of Mextel stating that Mextel "will fully cooperate with Air-Shields in an effort to implement QSR [QS] requirements." (*See* November 10, 1997 Letter, attached as Ex. 12A to Def. Mot. In Opp'n.).

*7 In March 1998, an independent research organization, CriTech Research Inc. ("CriTech"), performed an on-site evaluation of Mextel's software verification and validation methodology, equipment, and records. (*See* CriTech Research Software Verification and Validation Assessment Report, attached as Ex. 28 to Pl. Mot. For SJ.). The final report indicated that Mextel was able to produce "a software source code." (*Id.*). However, the report concluded that components of the "Design History File" were missing and that "no documented evidence of Software Verification and Validation, nor of the expected work products of software development, was found during CriTech's on site assessment." (*Id.*). Indeed, as a result of the lack of documentation, CriTech issued a proposal on April 6, 1998, which was then later reissued on November 10, 1999, to Hill-Rom to "develop a Design History File for the Mextel controller integrated into the ... Air Shields Isolette." (*See* CriTech Proposal, attached as Ex. 30 to Pl. Br. In Opp'n.).

In January and February 1998, the FDA started to actively monitor the regulatory compliance of the C2000 incubator, making unannounced inspections of Hill-Rom's facility in Hatboro, Pennsylvania (the "Hatboro facility"), where the C2000 incubator was manufactured. (*See* Certified FDA documents, attached as Ex. 14 to Def. Br. In Opp'n.). On March 26, 1998, the FDA issued a "Form FDA 483" to Hill-Rom, listing observations of problems with the C2000 incubator, including a lack of software validation data, an incomplete DMR from the vendor of the controller and sensor module, and incomplete device history records for the C2000 incubator. (*See* March 26, 1998 Letter, attached as Ex. 14 to Def. Br. In Opp'n., at FDA 00286-291). Hill-Rom met with the FDA to discuss these findings. (*See* Utterback Aff., attached as Ex. 3 to Def. Mot. For SJ., at ¶ 3).

In response to this letter and meetings with the FDA, Hill-Rom issued an "Urgent Medical Device Notice/Recall" for the incubator on May 18, 1998, citing temperature fluctuations, humidity departures from set points, and air flow probe failures as the causes of the notice. (*See* May 18, 1999 Urgent Medical Device Notice/Recall, attached as Ex. 12 to Pl. Mot. For SJ.). This notice was issued in conjunction with and at the recommendation of the FDA. (*See* October 3, 2001 Memorandum Summarizing Recall, attached as Ex. 14 to Def. Br. In Oppn., at FDA 00293-00294). An FDA memorandum indicated that the reason for the May 18, 1998 notice was the C2000 incubator's "potential for causing serious injuries or deaths," specifying that the "unresolved problems were with regard to the controller and the humidity module." (*Id.*, at 00294). The memorandum further identified overheating problems with the controller and humidity module, which increased the possibility that an infant in the C2000 could "dry out and experience respiratory distress." (*Id.,* at 00295).

***8** On June 18, 1998, Skulic sent Hill-Rom a letter contesting an accusation that Mextel was failing to help Hill-Rom fulfill FDA requirements. (*See* June 18, 1998 Letter, attached as Ex. 29 to Pl. Br. In Opp'n.). The letter stated that Mextel was available and willing to offer assistance in responding to FDA issues. (*Id.*).

On June 25, 1998, the FDA issued a "Warning Letter" to Hill-Rom. (*See* June 25, 1998 Warning Letter, attached as Ex. 21 to Pl. Mot. For SJ.). The warning letter found that "the C2000 devices are adulterated within the meaning of Section 501(h) of the FD & C Act in that methods used in, or facilities or controls used for, their manufacturing, packing, storage, or installation are not in conformance with the good manufacturing (CGMP) regulations" of the FDCA. (*Id.,* at E22258). The warning letter provided a non-exhaustive list of twenty-four violations, including, *inter alia,* a failure to include information regarding component specifications in the DMR for the controller, the failure to include the primary history label and labeling for each product unit in the DHR, and the failure to assure that production processes for the controller conform to its specifications. (*Id.*). The warning letter noted that the controllers were associated with a 15% failure rate at incoming inspection and that the FDA's inspection "revealed significant deviations" from the GMPs. (*Id.,* at E22259).

Immediately after the June 25, 1998 warning letter, Hill-Rom sent a letter to Mextel demanding rectification of several FDA observations related to the controller. (*See* June 30, 1998 letter, attached as Ex. 4D to Def. Mot. For SJ.). The June 30, 1998 letter stated that the "recall was largely driven by the lack of verification and validation of the controller software and the unacceptably high fallout rate during incoming inspection and test." (*Id.*). It also noted that Hill-Rom still had not received DMR materials, and that, if these materials were not provided, Hill-Rom would ask the FDA to directly inspect the DMR materials for the controller at Mextel's facility. (*Id.*).

In September 1998, Hill-Rom exercised its right under ¶ 9.4 of the Agreement and conducted a quality audit of Mextel's facility to ensure compliance with quality assurance protocols. The Hill-Rom used the regulations promulgated by the FDA as the gauge to determine compliance. (*See* 1998 Quality Audit Report, attached as Ex. 4E to Def. Mot. For SJ.). The quality audit in September 1998 resulted in an overall survey score of 58.7%, and a conditional certification level grade for Mextel. (*Id.*).

On October 7 and 8, 1998, representatives from both Hill-Rom and Mextel with the agenda of "problem solving," which included discussions of the incoming inspection failures of the controllers and sensor modules. (*See* Itinerary of October 7 and 8, 1998 Meeting, attached as Ex. 13 to Pl. Mot. For SJ.).

The FDA conducted another unannounced inspection of Hill-Rom's Hatboro facility in February 1999. Following this inspection, the FDA issued a second 483 letter to Hill-Rom on February 19, 1999. (*See* February 19, 1999 letter, attached as Ex. 14 to Def. Br. In Opp'n., at FDA00230-00285). The February 19, 1999 letter listed fourteen observations of problems with the C2000 incubator, including, *inter alia,* that "design verification did not confirm that the design output meets the design input requirements through software verification," that "actions needed to correct and prevent recurrence of nonconforming product and quality problems in regards to the control module are incomplete," and that "the DHR does not include or refer to the location of acceptance records which demonstrate the device is manufactured in accordance with the DMR." (*See id.*).

***9** In April 1999, Hill-Rom conducted a second quality audit of Mextel's manufacturing facility to determine compliance with GMPs. (*See* April 1999 Supplier Survey Results, attached as Ex. 4F To Def. Mot. For SJ.). Again, Hill-Rom used the QS regulations as the template to determine quality audit compliance. The audit produced an overall survey score of 34%, with a designated certification level of "unacceptable." (*Id.*). As a result of the low score, Hill-Rom demanded the submission of improvement plans to Hill-Rom's development team within thirty days of receipt of the survey. (*Id.*).

After the quality audit, Hill-Rom sent Mextel an April 27, 1999 letter, in which Hill-Rom referenced the poor certification level, listed many alleged deficiencies in Mextel's methodology and performance as a supplier of medical components, and threatened to terminate the Agreement if Mextel did not take "appropriate action." (*See* April 27, 1999 letter, attached as Ex. 4G to Def. Mot. For SJ.).

In October and November 1999, the FDA again conducted a series of inspections at Hill-Rom's Hatboro facility. On November 30, 1999, the FDA sent Hill-Rom a third 483 letter. (*See* November 30, 1999 Letter, attached as Ex. 14 to Def. Br. In Opp'n., at FDA00179-00181). The letter emphasized failures with respect to Hill-Rom's procedures for handling complaints associated with the C2000 incubator. (*Id.*). Complaints concerning the sensor module and controller were documented and reviewed by the FDA. (*See* Summary of Findings for November 30, 1999 Report, EIR Addendum, attached as Ex. 14 to Def. Br. In Opp'n., at 00178).

D. Termination

In February 1998, Hill-Rom contemplated the possibility of exiting the contractual arrangement with Mextel through a buy-out of Hill-Rom's remaining obligations. (*See* Estimate of Buyout, attached as Ex. 25 to Pl. Br. In Opp'n.). In July 13, 1998, Hill-Rom accepted a detailed quotation from Comtec Systems, Inc. ("Comtec") "for the development of a replacement controller" for the C2000 incubator. (*See* July 13, 1998 Letter, attached as Ex. 27 to Pl. Br. In Opp'n). Hill-Rom also accepted a proposal from Battelle to conduct a design and development program for the re-design of the controller. (*See* Battelle Proposal, attached as Ex. 26 to Pl. Br. In Opp'n.).

Despite accepting quotations and proposals from new suppliers for the development of a replacement controller, Hill-Rom continued to place purchase orders for sensor modules and controllers through November 1999. (*See* Purchase Orders, attached as Ex. 14 to Pl. Mot. For SJ.). On December 16, 1999, however, Hill-Rom notified Mextel that it was placing a production hold on all sensors and controllers, with the exception of spares. (*See* December 16, 1999 Letter (dated December 1, 1999), attached as Ex. 16 to Pl. Mot. For SJ.; *see* Skulic's First Declaration, at ¶ 10). Shortly thereafter, Skulic asserts that he notified Hill-Rom that it would not ship any more products until outstanding invoices were paid. (*See* Skluic's First Declaration, at ¶ 10). Then, on December 28, 1999, Hill-Rom sent Mextel another letter purporting to terminate the Agreement, citing ¶¶ 18.1 and 18.2 as the justification for this right to terminate. (*See* December 28, 1999 Letter, attached as Ex. 17 to Pl. Mot. For SJ.). The December 28, 1999 letter declared that this termination was effective immediately. (*Id.*).

***10** After purporting to terminate the Agreement, Hill-Rom met with the FDA in January 2000. (*See* Johnson Aff., attached as Ex. 3 to Def. Mot. In Opp'n., at ¶ 5-6). Hill-Rom issued a revised recall letter for the C2000 incubator on January 5, 2000, based in part on an overheating issue with the controller. (*See* October 3, 2001 FDA Memorandum, attached as Ex. 14A to Def. Br. In Opp'n., at FDA00292-FDA00295). Hill-Rom then replaced Mextel's controller with a replacement controller for every C2000 incubator. (*See* Johnson Aff., at ¶ 8). Hill-Rom also replaced Mextel's sensor module with a new sensor module. After the completion of this process, Hill-Rom started to sell a new version of the C2000 incubator ("new C2000 incubator"), without the Mextel products, on the market.

E. Litigation

On December 28, 2001, plaintiffs filed a complaint, which was later amended on April 26, 2002. The amended complaint alleged eleven counts against Hill-Rom: breach of contract (Count I); quantum meruit (Count II); unjust enrichment (Count III); breach of implied covenant of good faith and fear dealing (Count IV); fraud and deceit (Count V); patent infringement (Count VI); misappropriation of trade secrets (Count VII); trade dress infringement (Count VIII); common law unfair competition (Count IX); one count against fictitious individuals incorporating the substance of each prior claim (Count X); and one count against fictitious corporations incorporating the substance of each prior claim (Count XI). On November 8, 2002, the Court dismissed Counts V, X, and XI for failure to state a claim, and dismissed Counts I-IV on behalf of Skulic. (Doc. No. 20).

The Court issued a scheduling order on October 17, 2002 requiring fact discovery to conclude by March 31, 2003. (Doc. No. 19). On March 10, 2003, the Court amended this order, extending the end date for factual discovery until June 30, 2003 and for expert discovery until September 31, 2003. (Doc. No. 22). On May 9, 2003, the Court amended the scheduling order for a second time, extending the deadline for fact discovery until August 29, 2003 and for expert discovery until November 30, 2003. (Doc. No. 24). On August 4, 2003, after plaintiffs' representation that neither party deposed any witnesses, the Court issued a third amended scheduling order, requiring all fact discovery to end by December 27, 2003 and all expert discovery to conclude by April 14, 2004. (Doc. No. 28), including the submission of expert witness reports.

Subsequent to the issuance of the third amended scheduling order, Hill-Rom filed three motions to compel discovery responses and plaintiffs filed one motion. (Doc. No. 29, 30,. 37). On December 19, 2004, the Court advised the parties to resolve their discovery disputes privately. (Doc. 38). The Court further extended the deadline to file specific motions to compel on particular discovery issues to January 15, 2004 and February 2, 2004, in the event the parties failed to privately resolve their discovery disputes. (*Id.*). Neither party filed a motion to extend the discovery deadlines or a motion to amend the August 4, 2003 scheduling order during this period.

***11** The parties were unable to work out their discovery disputes, and Hill-Rom filed a motion to compel on January 15, 2004 (Doc. No. 39). Pursuant to its January 29, 2004 Order, the Court granted Hill-Rom's motion to compel and required plaintiffs to produce a copy of the electronic source code for the controller. On February 2, 2004, the Court again extended its deadline, from February 2, 2004 until February 27, 2004, for plaintiffs to file a motion to compel (Doc. No. 49) the production of allegedly privileged documents. On March 30, 2004, the Court resolved the plaintiffs' motion to compel in favor of Hill-Rom. (Doc. No. 59). Because none of the parties requested additional time for fact or expert discovery, the March 30, 2004 order enforced the existing August 4, 2003 scheduling order, officially closed the discovery period for fact and expert discovery, and demanded the filing of dispositive motions by April 14, 2004. (*Id.*).

On April 14, 2004, both sides filed summary judgment motions. (Doc. No. 63-74). This was followed by an array of briefs in opposition, reply briefs, statements of disputed and undisputed material facts, and motions to strike.

II. Discussion

A. Motions to Strike

It is well-established that "only evidence which is admissible at trial may be considered in ruling on a motion for summary judgment." *Countryside Oil Co., Inc. v. Travelers Ins. Co.,* 928 F.Supp. 474, 482 (D.N.J.1995); *see also* *Pamintuan v. Nanticoke Mem. Hosp.,* 192 F.3d 378, 388 (3d Cir.1999); Fed.R.Civ.P. 56(e) (requiring affidavits in support of summary judgment motion to be made on personal knowledge, to set forth facts that would be admissible in evidence, and to show affirmatively that the affiant is competent to testify to such matters). Both parties challenge the admissibility of affidavits and documents attached to their opponents' motions.

1. Plaintiffs' Objections

Plaintiffs argue that the affidavits of Susan Reilly ("Reilly Affidavit"), James Utterback ("Utterback Affidavit"), and Otho Boone ("Boone Affidavit"), and the documents attached to the Utterback and Boone Affidavits, constitute inadmissible evidence that may not be relied upon to resolve Hill Rom's motion for summary judgment. (*See* Pl. Br. In Opp'n., at 5-8).

a. The documents attached to the Boone Affidavit and Utterback Affidavit are admissible.

Plaintiffs seek to strike the documents attached to the Boone and Utterback Affidavits because the documents are unauthenticated and because the letters do not constitute business records within the hearsay exception. (*Id.,* at 7). FN3 The Court rejects plaintiffs' motion.

FN3. The documents attached to the Utterback Affidavit are attached as Exhibits A-C to the Boone Affidavit.

The documents attached to the Boone Affidavit are admissible. Mr. Boone is the custodian of domestic records of regularly conducted activity for Hill-Rom and its predecessors, including Air-Shields. (*See* Boone Aff., attached as Ex. 4 to Def. Mot. For SJ., at ¶ 2). Boone provides testimony to authenticate the documents-that they were made by a person with knowledge at or near the time of the occurrences of the matters set forth in the letters; that they were kept in the course of regularly conducted business activity as part of a regular business practice; and that they were made in the course of a regularly conducted business practice. *See* Fed. R. Ev. 902(11). Furthermore, to the extent that Hill-Rom seeks to introduce these documents for their truth-value, these authenticated documents meet the business records exception to the hearsay rule. *See* Fed. R. Ev. 803(6) (custodian may establish admissibility of records of regularly conducted business activities). Finally, plaintiffs cite no caselaw to support their position that letters kept in the course of regularly conducted activity fail to constitute a "memorandum, report, record, or data compilation" within the meaning of Federal Rule of Evidence 803(6).

b. The Utterback Affidavit is admissible.

***12** Plaintiffs seek to strike the Utterback Affidavit on the basis that Mr. Utterback lacks personal knowledge of the testimony in his affidavit and on the basis that his testimony puts in issue communications relating to the FDA that were previously withheld by Hill-Rom on the basis of the attorney-client and work-product privilege. (*See* Pl. Br. In Opp'n., at 6-7). The Court rejects plaintiffs' motion.

The Utterback Affidavit is admissible. First, the Utterback Affidavit does not put in issue privileged communications between Mr. Utterback and his client to which plaintiffs were previously denied access during discovery, such as communications embodying Mr. Utterback's direction of Hill-Rom's response to FDA investigations. Instead, the Utterback Affidavit refers to, and provides documents concerning, communications between Hill-Rom and the FDA, communications to which the attorney-client privilege does not attach. (*See* Utterback Aff., attached as Ex. 3 to Pl. Mot. For SJ., at ¶ 2-4); *see* 42 Pa. Cons.Stat. Ann. § 5928 (attorney-client privilege protects confidential communications between attorney and client). These documents were turned over in the course of discovery, rather than withheld through Hill-Rom's discovery logs. (*See* Def. Response to Mot to Compel, at 23-24) ("Hill-Rom has not withheld documents provided to the FDA").

Furthermore, the Court finds that Mr. Utterback, as in-house counsel for Hill-Rom, has knowledge of the factual averments in his affidavit. Fed.R.Civ.P. 56(e) (requiring affiant to set forth facts made on personal knowledge). Plaintiffs cite one lone example-Mr. Utterback's reference to the December 31, 1996 certificate statement in which Mextel promised to deliver formal DMR documentation-to support its contention that "Utterback's affidavit is largely not based on personal knowledge." (*See* Pl. Mot. In Opp'n., at 6). In contrast to plaintiffs' argument, Mr. Utterback does not testify to the circumstances behind the signing of the certificate statement, which occurred prior to his employment at Hill-Rom; but, instead, merely references the existence of the certificate statement in his discussion of Mextel's alleged failure to deliver pertinent DMR information to Hill-Rom both before and after the commencement of FDA investigations. (*See* Utterback Affidavit, at ¶ 3c). More importantly, assuming *arguendo* that Mr. Utterback's reference to the December 31, 1996 letter should be stricken, plaintiffs' general contention of lack of personal knowledge, without specific examples, fails as a matter of law to render inadmissible the remaining testimony in the Utterback Affidavit. *See* Wright, Miller & Kane, 10B Federal Practice & Procedure § 2738, at 377 (3d ed. 1998) ("It follows that a motion to strike should specify the objectionable portions of the affidavit and the grounds for each objections. A motion asserting only a general challenge to an affidavit will be ineffective.").

c. The Reilly Affidavit is inadmissible.

***13** Plaintiffs seek to exclude the affidavit of Susan C. Reilly, an expert in the field of regulatory compliance for the medical device and diagnostic industry, on the basis of Hill Rom's violation of discovery deadlines. (*See* Pl. Br. In Opp'n., at 5). The Court agrees.

Ms. Reilly was not designated as an expert witness prior to the close of expert discovery. Nor did Ms. Reilly file an expert report prior to the close of expert discovery. Hill-Rom's untimely introduction of Ms. Reilly's testimony in affidavit form at the summary judgment stage therefore violates the Court's August 4, 2003 scheduling order. (Doc. No. 28). Accordingly, after weighing the relevant factors, particularly the prejudice to plaintiffs, this Court finds that an appropriate sanction pursuant to Federal Rule of Civil Procedure 37(b)(2)(B) is to bar Ms. Reilly's testimony at trial, thereby making her affidavit inadmissible for purposes of Hill Rom's summary judgment motion. *See, e.g., Oliver v. Ingber,* 1998 WL 107299, at *2 (E.D.Pa. March 9, 1998) (excluding expert testimony at trial for failure to meet pre-trial deadline for exchange of expert witness information because defendant would have been prejudiced by allowance of expert testimony); *Perkasie Ind. Corp. v. Advance Transformer, Inc.,* 143 F.R.D. 73, 77 (E.D.Pa.1992) (excluding expert testimony for failure to comply with pre-trial scheduling order).

d. Conclusion

This Court finds the Utterback Affidavit, the Boone Affidavit, and the documents attached to these affidavits admissible as a matter of law. However, the Court grants plaintiffs' motion to strike the Reilly Affidavit.

B. Summary Judgment Motions

Plaintiffs and Hill-Rom have filed motions for summary judgment.

1. Standard

In considering a motion for summary judgment, the court must determine whether "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue of material fact and that the moving party is entitled to judgment as a matter of law." Fed.R.Civ.P. 56(c); *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 247, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986); *Arnold Pontiac-GMC, Inc. v. General Motors Corp.,* 786 F.2d 564, 568 (3d Cir.1986). Only facts that may affect the outcome of a case are "material." *Anderson,* 477 U.S. 248. All reasonable inferences from the record are drawn in favor of the nonmovant. *See id.* at 256.

The movant has the initial burden of demonstrating the absence of genuine issues of material fact. This "burden ... may be discharged by 'showing' that there is an absence of evidence to support the non-moving party's case." *Celotex Corp. v. Catreet,* 477 U.S. 317, 323, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986). Once this burden is discharged, the non-movant must then establish the existence of each element on which it bears the burden of proof. *See J.F. Feeser, Inc. v. Serv-A-Portion, Inc.,* 909 F.2d 1524, 1531 (3d Cir.1990). A plaintiff cannot avert summary judgment with speculation or by resting on the allegations in his pleadings, but rather must present competent evidence from which a jury could reasonably find in her favor. *Anderson,* 477 U .S. at 248; *Ridgewood Bd. of Educ. v. N.E. for M.E.,* 172 F.3d 238, 252 (3d Cir.1999); *Williams v. Borough of West Chester,* 891 F.2d 458, 460 (3d Cir.1989); *Woods v. Bentsen,* 889 F.Supp. 179, 184 (E.D.Pa.1995).

2. Plaintiffs' Motion for Summary Judgment

***14** Plaintiffs seek summary judgment with respect to certain breach of contract claims in Count I of the amended complaint, Hill-Rom's contract counterclaims, and Hill-Rom's patent defenses and counterclaims. (*See* Pl. Mots. For SJ.).[FN4]

FN4. This Court addresses plaintiffs' summary judgment argument with respect to dismissing Hill Rom's patent defenses and counterclaims in the context of Hill Rom's summary judgment motion.

A. Breach of Contract

Mextel's summary judgment motion alleges that Hill-Rom breached the Agreement in numerous ways.[FN5] First, Mextel claims that Hill-Rom refused to pay invoices from March 12, 1998 to January 12, 2000 covering controllers and sensor modules shipped to and accepted by Hill-Rom. (*See* Pl. Mot. For SJ., at 10-12). Second, Mextel claims that Hill-Rom refused to pay for unshipped products after placing purchase orders pursuant to the Agreement. (*Id.,* at 12-13). Third, Mextel contends that Hill-Rom did not purchase the minimum of 8,000 controllers, as required by the Agreement, but, instead, purchased only 5,621 controllers. (*Id.,* at 13-14).[FN6]

FN5. Mextel notes that it has not moved for summary judgment on all its breach of contract allegations, including damages stemming from Hill-Rom's breach of its obligations to use plaintiff as the exclusive supplier for replacement controllers, from plaintiff's exclusive controller design and development rights, and from plaintiff's rights to other damages and attorney's fees. (*See* Pl. Mot. For SJ., at 10 n. 2).

FN6. As a threshold question, this Court must first determine what law to apply to the dispute. The Agreement calls for the application of Pennsylvania law. (*See* Agreement, at ¶ 27). Neither party has expressly determined whether the Pennsylvania Uniform Commercial Code ("UCC") applies to the Agreement. Article II of the Pennsylvania UCC applies to transactions involving the sale of goods. *See* 13 Pa. Cons.Stat. Ann. § 2-102 (Article II of UCC applicable to "transactions in goods"). Although the Agreement covers the design, development, and manufacture of controllers, as well as the provision of other types of engineering services, its primary purpose is the supply/sale of these controllers to the Hill-Rom. (*See* Agreement, at ¶ 9). This Court concludes that Article II of UCC applies to the parties' breach of contract dispute. *See* Advent Systems Ltd. v. Unisys Corp., 925 F.2d 670 (3d Cir.1991). This conclusion is further confirmed by the parties, who, in their respective briefs, both rely upon the Pennsylvania UCC as controlling law.

i. The sensor module was not covered by the Agreement.

[1] Mextel seeks summary judgment on its breach of contract claim with respect to the contract price both of delivered and of ordered, but undelivered sensor modules. (*See* Pl. Mot. For SJ., at 10-12). However, Mextel admits in its brief in opposition to Hill-Rom's summary judgment motion that the production and supply of sensor modules are not covered by the Agreement. (*See* Pl. Br. In Opp'n. to Def. Mot. For SJ., at 12).[FN7] Nor does Mextel supply alternative oral or written contracts between Mextel and Hill-Rom for the supply of sensor modules. *See, e.g.,* Rototherm Corp. v. Penn Linen & Uniform Serv., 1998 WL 134222, at *3 (E.D.Pa. March 19, 1998) (granting summary judgment to defendant for plaintiff's failure to demonstrate the existence of contract between two parties, "an essential element of its claim for breach of contract"). Moreover, the accounting documentation Mextel submits as proof of its production and supply of sensor modules to Hill-Rom only identifies the date of shipping, rather than the type of products supplied to Hill-Rom. (*See* Ageing Accounts, attached as Ex. 5 and 7 to Pl. Mot. For SJ.). Without an express written or oral contract for the supply and purchase of sensor modules, Mextel is not entitled to summary judgment on a breach of contract theory as to the cost of the shipped or unshipped sensor modules. *See* 13 Pa. Cons.Stat. Ann. § 2107(a) (contract for the sale of goods for the price of $500 or more is not enforceable by way of action or defense unless some writing indicating existence of contract for sale between parties and unless signed by party against whom enforcement is sought).

FN7. Specifically, Mextel concedes that the production and supply of sensor modules to Hill-Rom was not covered by the Agreement, asserting instead that the sensor modules would be supplied to Hill-Rom pursuant to an informal arrangement by which Hill-Rom would place purchase orders both for controllers and sensor modules. (*See* Pl. Br. In Opp'n., at 12-13; *see also* December 1, 1999 Letter placing "all sensors and controllers" on hold, attached as Ex. 6 to Pl. Mot. For SJ.).

ii. Mextel is entitled to summary judgment on liability for Hill Rom's refusal to pay for controllers that it received and accepted; however, Mextel is not entitled to summary judgment for services received by Hill-Rom.

Mextel also asserts that it is entitled to summary judgment on Hill-Rom's failure to compensate Mextel for controllers shipped to Hill-Rom between March 12, 1998 and January 12, 2000, and for engineering services rendered to Hill-Rom in connection with the design and production of these products. (*See* Pl. Mot. For SJ., at 10-12). Mextel asserts that the contract price for the delivered products and services was $278,385. (*Id.*). Hill-Rom admits that outstanding invoices exist for certain shipments. However, Hill-Rom challenges the amount of products received and justifies non-payment on the basis that the products were non-conforming at the time of their receipt. (*See* Def. Br. In Opp'n., at 2-4).

a. Engineering Services

***15** [2] To support its claim for the value of engineering services rendered, Mextel relies upon the affidavit of Novela Skulic, an employee of Mextel who managed product orders, shipping, and invoicing between Mextel and Hill-Rom. (*See* First Skulic Declaration, at ¶ 2). However, Skulic's affidavit does not identify the type of "services" rendered. (*Id.* at ¶ 4). Moreover, Mextel has failed to identify under what provision of the Agreement it is entitled to the reasonable value of engineering services. *See, e.g.,* *Omicron Systems, Inc. v. Weiner,* 860 A.2d 554, 564 (Pa.Super.Ct.2004) (breach of contract requires plaintiff to establish existence of contract, breach of duty imposed by contract, and resultant damages). Nor has Mextel provided an invoice detailing when engineering services were rendered, why these services were rendered, and the amount of these services. Thus, genuine issues of material fact exist as to whether Mextel provided engineering services to Hill-Rom, whether the Agreement covered these services, and the amount of those services.

b. Controllers

[3] The shipment of controllers is governed by the Agreement, and, thus, by the Pennsylvania UCC. Under the Pennsylvania UCC, upon delivery of a commercial unit, a buyer may reject the whole, accept the whole, or accept any commercial units and reject the rest. *See* 13 Pa. Cons.Stat. Ann. § 2-601. An acceptance of goods occurs when the buyer either: (1) after a reasonable opportunity to inspect the goods signifies to the seller that the goods are conforming or that she will take or retain them in spite of their nonconformity; or (2) fails to make an effective rejection after a reasonable time for inspection. *Id.* § 2-606. The buyer must pay at the contract rate for any goods accepted. *Id.* § 2-607(a).

To make an "effective rejection," a buyer must notify the seller of the non-conforming nature of the goods "within a reasonable time after the delivery or tender of the goods." *Id.* § 2-602(a)-(b). The seller must then hold the goods "with reasonable care at the disposition of the seller for a time sufficient to permit the seller to remove them." *Id.* § 2-602((b).

(i) Liability

The Agreement required Hill-Rom to pay Mextel forty days from the date of shipment of the controllers, thereby setting the date for rejection of delivered controllers at a maximum of forty days. (*See* Agreement, at ¶ 9.6). It is indisputable that Hill-Rom immediately rejected a number of incoming controllers for poor quality and then returned these products to Mextel to cure their defects. (*See* Wenstrup Aff., attached as Ex. 1 to Def. Br., at ¶ 8); (Ferrante Aff., attached as Ex. 6 to Def. Mot. For SJ., at ¶ 5); (Drinkwater Aff., attached as Ex. 4 to Def. Br., at ¶ 4) ("When Mextel products would arrive, they would be tested to determine if they worked correctly. If they did not, they would be returned to Mextel. As a general rule, when that occurred, Mextel was very uncooperative with Hill-Rom's efforts to get the problems corrected and the controller timely returned"). It is also indisputable that Hill-Rom "accepted" a number of Mextel's controllers by taking steps inconsistent with Mextel's ownership-Hill-Rom incorporated these controllers in the C2000 incubator, sold the C2000 incubator, and then failed to pay Mextel within forty days from the date of shipment (*See* Novela Skulic Declaration, at ¶¶ 3-5). *See* *Comfort Springs Corp. v. Allancraft Furniture Shop,* 165 Pa.Super. 303, 67 A.2d 818, 820 (Pa.Super.Ct.1949) (holding that "buyer's rights to reject goods must be exercised promptly and unequivocally and that complaint as to qualify [sic] while exercising dominion over the goods is not rejection"); *Foell Packing Co. v. Harris,* 127 Pa.Super. 494, 193 A. 152 (Pa.Super.Ct.1937) (resale of product constitutes act inconsistent with seller's ownership). Nor has Hill-Rom provided documentation to indicate that it effectively rejected those controllers that passed Hill-Rom's initial inspection test; [FN8] indeed, although Hill-Rom constantly notified Mextel of its general inability to demonstrate and document that the controller was manufactured in accordance with GMPs, Hill-Rom never notified Mextel in writing of particular defects with particular installments, nor offered to return allegedly defective controllers to Mextel.[FN9] *See* 13 Pa. Cons.Stat. Ann. § 2-602; *see* *Julian C. Cohen Salvage Corp. v. Eastern Elec. Sales Co.,* 205 Pa.Super. 26, 206 A.2d 331, 334 (Pa.Super.Ct.1965) (buyer of 36,440 pounds of defective cable accepted cable when it failed to give written notice of rejection and never offered or attempted to return cable from warehouse). Accordingly, regardless of whether those controllers that passed the initial inspection test were non-conforming at the time of delivery, Hill-Rom "accepted" those controllers within the meaning of section 2-606 of the Pennsylvania UCC. Mextel is therefore entitled to summary judgment on its breach of contract claim for those controllers that Hill-Rom received and accepted, but for which Hill-Rom never paid.

FN8. In fact, as plaintiff points out, Hill-Rom's December 28, 1999 termination letter never suggested that the controllers received by Hill-Rom were non-conforming. (*See* December 28, 1999 Termination Letter).

FN9. Hill-Rom's arguments to the contrary are not persuasive. Hill-Rom argues that Mextel's controllers were not manufactured in accordance with GMPs, that Hill-Rom returned controllers because they did not pass initial inspections, and that the FDA "suggested" that Hill-Rom terminate its contract with Mextel in 1999. Hill-Rom claims that these acts, some initiated by Hill-Rom and some initiated by third parties, constitute a sufficient "rejection" of non-conforming controllers. (Def. Mot. For SJ., at 2-4). With respect to controllers received by Hill-Rom, this Court disagrees. Hill-Rom continued to place orders for controllers until December 1999, continued to use those controllers that passed the initial screening test in the C2000 incubator, and never indicated nor expressed in writing an intent to reject allegedly defective controllers that it received from Mextel. *See* 13 Pa. Cons.Stat. Ann. § 2-602.

(ii) Damages

***16** Under the Pennsylvania UCC, "the buyer must pay at the contract rate for any goods accepted." *See* 13 Pa. Cons.Stat. Ann. § 2-607(a). However, several genuine issues of material fact exist as to the amount of damages.

Mextel has not provided the original purchase orders or supplemental documentation indicating how many controllers Hill-Rom ordered and accepted. Instead, Mextel provides accounting information in the form of "ageing detail reports" of accounts receivable, which identify the date of the invoice and the amount owed for the invoice. (*See* Ageing Detail Reports, attached as Ex. 5 and 7 To Pl. Mot. For SJ.). This accounting information does not specify what types of goods were delivered, let alone whether the invoices were for the shipment of controllers. (*Id.*). Nor does the accounting information identify what goods Hill-Rom accepted, what goods Hill-Rom rejected through the initial screening test, and what products were immediately rejected and then cured, if at all, by Mextel. (*Id.; see* February 17, 1998 letter from Hill-Rom to Mextel discussing the return of a defective controller, attached as Ex. 40 to Pl. Mot. In Opp'n.). Accordingly, a genuine issue of material fact exists as to the number of controllers that were delivered to Hill-Rom and that were accepted within the meaning of section 2-615 of the Pennsylvania UCC.

By implication, a genuine issue of material fact also exists as to the actual amount owed for those controllers shipped to and accepted by Hill-Rom. Mextel provides invoices, along with the affidavit of Mextel's shipping and invoicing personnel, concluding that the total value of the unpaid invoices from March 12, 1998 until January 12, 2000 is $278,384.95. (*See* Novella Skulic Aff., at ¶ 4). Hill-Rom, however, has provided an affidavit from Mextel's manager of finance, Doreen Tierney, who states that the Hill-Rom's accounting department only retains a record of $106,664 in outstanding invoices. (*See* Tierney Aff., attached as Ex. 9 to Def. Br. In Opp'n. to Pl Mot. For SJ.). Accordingly, there is a genuine issue of material fact as to the total value of the unpaid controllers received by Hill-Rom.

iii. Hill-Rom properly terminated the Agreement pursuant to ¶ 18.2, and, therefore, Hill-Rom is entitled to summary judgment on Mextel's breach of contract claim for obligations that were executory at the time of Hill-Rom's termination of the Agreement.

Mextel also claims that it is entitled to summary judgment with respect to two obligations that were outstanding when Hill-Rom first placed a "production hold" on ordered controllers on December 16, 1999 and then purported to terminate the Agreement on December 28, 1999. (*See* Pl. Mot. For SJ., at 12-13). First, Mextel asserts that Hill-Rom was required to pay for manufactured, but undelivered, controllers. (*Id.*). Second, Mextel asserts that Hill-Rom was required to purchase the minimum aggregate number of 8000 controllers over the course of the Agreement.[FN10] (*See* Addendum to Agreement, at ¶ 1). According to this logic, because Hill-Rom wrongfully repudiated its Agreement obligations by placing a production hold on all purchase orders and by impermissibly terminating the Agreement, Mextel is entitled to summary judgment on its contract claim for ordered but unshipped controllers and for unordered controllers. (*Id.*).[FN11]

FN10. The February 20, 1997 Addendum to the Agreement states that Hill-Rom shall purchase a minimum of two thousand controllers per year during the term of the Agreement. (*See* Addendum, attached as Ex. 2 to Pl. Mot. For SJ., at ¶ 2). Mextel contends that Hill-Rom only purchased 5,621 controllers, and that, even if justified in terminating the contract, Hill-Rom was bound to purchase the remaining 2,379 controllers. (*See* Novela Skulic Declaration, at ¶ 6).

FN11. Under the Pennsylvania UCC, an anticipatory repudiation of a performance not yet due permits the aggrieved party to resort to any remedy for the breach and to either suspend her own performance or to identify goods to the contract. 13 Pa. Cons.Stat. Ann. § 2-610. The measure of damages for the buyer's repudiation is the difference between the market price at the time of tender and the unpaid contract price and incidental damages, minus expenses saved in consequence of the breach. *Id.* § 2-708(a).

*17 Hill-Rom admits that it continued to place orders for controllers throughout the fall of 1999. (*See* Drinkwater Aff., attached as Ex. 4 to Def. Mot. For SJ., at ¶ 6). Hill-Rom also admits that it did not purchase the minimum number of controllers contemplated by the Agreement. (*See* Def. Br. In Opp'n. To Pl. Mot. For SJ., at 10; Tierney Aff., attached as Ex. 9 to Def. Br. In Opp'n., at ¶ 3). However, Hill-Rom rejects Mextel's characterization of the December 16, 1999 letter FN12 placing a "production hold" on ordered controllers and the December 28, 1999 letter terminating the Agreement as an anticipatory repudiation of the Agreement. Instead, Hill-Rom asserts that Mextel's breach of contract claim with respect both to the unshipped controllers under the suspended purchase orders and to the unordered controllers must fail for any of three reasons: (i) Hill-Rom properly terminated the Agreement prior to the receipt of these products; (ii) Hill-Rom properly cancelled the Agreement pursuant to section 2-612 of the Pennsylvania UCC; and/or (iii) continued performance of the Agreement in December 1999 was impracticable.

FN12. The letter placing a "production hold" on ordered controllers is dated December 1, 1999, but, according to Skulic's First Declaration, was not issued by Hill-Rom until December 16, 1999. (*See* Skulic First Declaration, at ¶ 10).

The resolution of Mextel's summary judgment motion hinges on the characterization of Hill-Rom's December 1999 correspondence with Mextel either as an anticipatory repudiation of the Agreement or as a proper termination. FN13 If no genuine issue of material fact exists that Hill-Rom Rom improperly repudiated its performance, then Mextel is entitled to the difference between the market price at the time of tender, on one hand, and the unpaid contract price and incidental damages, on the other hand, minus expenses saved in consequence of the breach. *See* 13 Pa. Cons.Stat. Ann. §§ 2-608(a), 2-610. However, if Hill-Rom was correct in terminating the Agreement, or if continued performance under the Agreement was impracticable, then Hill-Rom's executory obligations under the Agreement were discharged, and Mextel is not entitled to summary judgment on its contract claims for the unshipped and unordered controllers. *See id.* §§ 2105(a)-(b) (effect of both "termination" and "cancellation" of sale of goods means that all executory obligations on both sides are discharged, but any right based on prior breach or performance survives). Furthermore, Hill-Rom may be entitled to summary judgment if Hill-Rom acted properly in terminating the Agreement due to Mextel's material breaches.

FN13. To the extent that Mextel's briefs raise this issue, the Court finds that the December 16, 1999 letter, standing alone, was not an "anticipatory repudiation" of Hill-Rom's obligations pursuant to § 2-610. Although the statutory text of the Pennsylvania UCC does not define the phrase "anticipatory repudiation," the commentary indicates that an "anticipatory repudiation" depends on the circumstances of the situation. *Id.*, at comment 2. According to this commentary, an anticipatory repudiation may be evidenced by words or actions, and occurs when a party "reasonably indicates a rejection of the continuing obligation." *Id.* The rejection itself, however, must be "definite and unequivocal." *Anderson on the Commercial Code* § 2-610:16 (2004).

The December 16, 1999 letter does not meet this standard. This letter tersely states that, pursuant to an earlier telephone conversation between the parties, "all sensors and controllers are on 'Production Hold' with the exception of spares, which will be handled on an as-needed basis." (*See* December 16, 1999 Letter, attached as Ex. 6 to Pl. Mot. For SJ.). This letter does not indicate that Hill-Rom was no longer willing to perform under the Agreement, that Hill-Rom was refusing to pay for controllers that had been manufactured, that Hill-Rom was refusing shipment of controllers that had already been produced and manufactured, or that Hill-Rom was not going to continue to purchase controllers from Mextel in the future. In fact, through the reference to an earlier conversation, the December 16, 1999 letter does not clearly indicate that the production hold was a unilateral action taken by Hill-Rom. As such, the December 16, 1999 letter did not manifest a definite and unequivocal refusal to perform an obligation not yet due. *See* 13 Pa. Cons.Stat. Ann. § 2-610.

Nonetheless, the December 26, 1999 termination letter, when read in conjunction with the December 16, 1999 letter, connotes a clear refusal by Hill-Rom to perform under the Agreement. Consequently, to the extent that the December 26, 1999 letter improperly terminated the Agreement, Hill-Rom repudiated the contract within the meaning of 2-610 of the Pennsylvania UCC.

a. Hill-Rom terminated the Agreement pursuant to ¶ 18.2 in a procedurally and substantively proper manner, but failed to properly terminate the Agreement pursuant to ¶ 18.1(c).[FN14]

FN14. The Court uses the term "termination" as employed in the Agreement: as covering all instances when a party properly puts an end to a contractual relationship. Nonetheless, the Court recognizes the distinction between "termination," which refers to when "either party puts an end to the contract otherwise than for its breach," and "cancellation," which refers to when "either party puts an end to the contract for breach by the other." *See* 13 Pa. Cons.Stat. Ann. § 2106(c)-(d). This distinction is important with respect to the remedies that are available the terminating or cancelling party. *Id.*

(i) Moment of Contractual Demise

Before this Court determines whether Hill-Rom properly ended the contractual arrangement between the parties in December 1999, this Court must first address Mextel's contention that Hill-Rom impermissibly "decided to terminate the Agreement when it began to develop knock-offs of the Mextel controller and sensor module in 1998." (*See* Pl. Disputed Facts, at ¶ 14). In other words, Mextel argues that Hill-Rom "repudiated" the Agreement prior to December 1999 by surreptitiously violating its representation and warranty of exclusivity in ¶ 15.1(c), indeed, by "negotiating and contracting with third parties to copy plaintiffs' intellectual property and supply the component parts developed and manufactured by Mextel" (Pl. Undisputed Facts, at ¶ 7). As such, Mextel argues that this earlier breach, albeit unknown to Mextel at the time, discharged Mextel's obligations to perform under the Agreement. *See* 13 Pa. Cons.Stat. Ann. § 2-610(a) (anticipatory repudiation constitutes breach of contract and entitles seller to suspend performance); *see also* Ott v. Buehler Lumber Co., 373 Pa.Super. 515, 541 A.2d 1143, 1145 (Pa.Super.Ct.1988) ("the general rule is that a party who has materially breached a contract may not complain if the other party refuses to perform his obligations under the contract"); *Oak Ridge Construction Co. v. Tolley,* 504 A.2d 1343, 148 (Pa.Super.Ct.1986) ("If a breach constitutes a material failure of performance, then the non-breaching party is discharged from all liability under the contract.").

***18** Hill-Rom admits that it hired a third-party to design and develop a new controller. (Def. Mot. For SJ., at 21-22). However, Hill-Rom asserts that this relationship with a third-party did not violate the Agreement because the third-party never supplied controllers during the life of the contract. (*Id.*).

In ¶ 15.1(c) of the Agreement, Hill-Rom represented and warrantied that it:

> [i]s not currently a party to any agreement or undertaking, oral or written, that would, in any manner be inconsistent with the rights herein granted to MEXTEL to design, develop, and SUPPLY a PRODUCT and shall not enter into any such agreement or understanding, oral or written, during the term of the Agreement, nor, during the terms of this Agreement, directly or indirectly, engage in any activity that would, in any manner, be inconsistent with the right herein granted to MEXTEL to design, develop, and SUPPLY a PRODUCT, except as specifically authorized herein....

(*Id.*). The clear language of ¶ 15.1(c) of the Agreement prohibits Hill-Rom from "design[ing], develop[ing], and supply[ing] a product" during the life of the contract. *Id.* The conjunction "and" precludes a breach of this provision if Hill-Rom only hired a third party to design and develop a replacement controller, without using this third party to supply the product. *Id.*

Mextel has provided evidence, to which Hill-Rom admits, that by June 1998, Hill-Rom was accepting detailed quotations and proposals from third parties to develop a replacement controller for the C2000 incubator. (*See* Comtec and Battelle Proposals, attached as Ex. 26-27 to Pl. Br. In Opp'n.). It is also true that Mextel could not have waived its right to discharge its obligations under the Agreement based upon Hill-Rom's alleged repudiation by continuing to perform, as Mextel was not aware of Hill-Rom's solicitation of these quotations and proposals. (*See* Vedran Skulic's Third Declaration, at ¶ 8); *see also* Keenan v. Scott Township Auth., 151 Pa.Cmwlth. 225, 616 A.2d 751, 755 (Pa.Commw.Ct.1992) (waiver requires "intentionally relinquishing or abandoning some known right, claim or privilege"); 13 Williston on Contracts § 39:22 (4 th ed.2004) (party charged with waiver of contractual breach must possess knowledge or notice of opponent's breach). However, Mextel provides no evidence to indicate that Hill-Rom contracted with a third party to *supply* a replacement controller in June 1998 or, then again, prior to Hill-Rom's attempt to terminate the Agreement in December 1999. As such, no evidence suggests that Hill-Rom breached ¶ 15(c) of the Agreement prior to December 1999. Therefore, Mextel was not discharged of its obligations under the Agreement by virtue of Hill-Rom's solicitation of proposals for the design and manufacture of a replacement controller in 1998.

(ii) Contractual Termination of the Agreement

Hill-Rom relies upon two different contractual provisions to justify its termination of the Agreement. First, ¶ 18.1(b) gives Hill-Rom the right to terminate the Agreement "at any time after giving sixty (60) days' written notice to Mextel upon the occurrence of" Hill-Rom's failure to meet any of its material obligations under this Agreement. (*See* Agreement, at ¶ 18.1(b)). Paragraph 18.1(b) also gives Mextel the right to cure any material breach within sixty days after receipt of Hill-Rom's written notice. (*Id.*).

***19** Second, ¶ 18.2 grants Hill-Rom the right to terminate the Agreement after providing sixty days written notice, if Hill-Rom "in its sole discretion, determine [sic] that the PRODUCTS are obsolete or that the infant incubators or infant radiant warmers into which such PRODUCTS are incorporated are obsolete." (*See* Agreement, at ¶ 18.2). Unlike ¶ 18.1, the decision to terminate under ¶ 18.2 resides solely within Hill-Rom's discretion, and does not require Hill-Rom to provide Mextel a right to cure the controller's obsolescence.

Mextel challenges the procedural and substantive propriety of Hill Rom's invocation of ¶ 18.1(b) and ¶ 18.2 to terminate the contract.

(a) Procedural Propriety

Under Pennsylvania law, "conditions precedent to a contract termination must be strictly fulfilled." *Accu-Weather, Inc. v. Prospect Communications, Inc.,* 435 Pa.Super. 93, 644 A.2d 1251, 1254 (Pa.Super.Ct.1994); *see also* 13-68 Corbin on Contracts § 68.9 ("Notice within the designed time period is the condition precedent to the effective exercise of the power reserved. If a party who has a power of termination by notice fails to give the notice in the form and at the time required by the Agreement, it is ineffective as a termination."). This rule leads to two important corollary rules, both of which are applicable to the resolution of this dispute. First, according to the Pennsylvania Supreme Court, notice to terminate a contract must be "clear and unambiguous," and "where the conduct of one having the right to terminate is ambiguous, he will be deemed not to have terminated the contract." *Maloney v. Madrid Motor*

Corp., 385 Pa. 224, 122 A.2d 694, 696 (Pa.1956); *see also* 17B C.J.S. Contracts § 446 ("A clear and unambiguous notice, timely given, and in the form prescribed by the contract, is essential to the exercise of an option to terminate the contract."). Second, notice provided after the contractual deadline for providing termination is ineffective to avoid renewal of a contract among sophisticated commercial entities pursuant to an automatic renewal provision. *See, e.g.,* Otis Elevator Co. v. George Washington Hotel Corp., 27 F.3d 903, 909 (3d Cir.1994) (holding under Pennsylvania law that failure to comply with ninety-day deadline for providing notice of termination prior to automatic renewal of contract renders termination ineffective, even without a showing of prejudice by noticed party).

Nonetheless, in contrast to ambiguous and/or untimely notice, Pennsylvania law relaxes in at least one instance the rule of strict compliance with condition precedents to contractual termination. Consistent with the "universally accepted rule," timely notice that purports to terminate the contract in a shorter amount of time than that stipulated in the termination clause effectively terminates the contract, but only after the expiration of the prescribed time within the termination clause. *See, e.g.,* Shain v. Washington Nat'l Ins. Co., 308 F.2d 611, 614 (8th Cir.1962) (J. Blackmun) ("it is the general rule that were a contract, whether it be for one for employment or for insurance or of a different kind, requires written notice of cancellation upon a stated time, a notice failing to meet the time requirement, but otherwise appropriate, is nonetheless effective upon the lapse of the time required by the contract"); Wetherell v. Sentry Reinsurance, 743 F.Supp. 1157, 1176 (E.D.Pa.1990) (applying Pennsylvania law and finding that notice of termination providing less time than required under reinsurance contract was effective at the conclusion of proper date as between sophisticated insurance companies and brokers); 14 Summ. Pa. Jur.2d Ins. § 3:58 ("the fact that the notice contains a time limitation which is void because it is less than that required by the policy does not void the notice or make it inoperative; rather, the notice is effective, but is to be read as though it stated the proper date which would be allowed by the policy"). Of course, notice declaring termination in a shorter amount of time than that stipulated in the contract is effective only to the extent that it does not seek to circumvent or nullify other contractual precedents to termination. Accordingly, such notice is ineffective when the contract affords the noticed party the right, during the stipulated notice period, to cure the conditions that would negate the opposing party's right to terminate the contract. *See, e.g.,* *Luden's Inc. v. Local Union No. 6 of the Bakery, Confectionary, and Tobacco Workers,* 805 F.Supp. 313, 317 (E.D.Pa.1992), *vacated and remanded on other grounds,* 28 F.3d 347 (3d Cir.1994) (general rule that termination notice is not rendered ineffective merely because it states shorter period than that required by Agreement carries exception where "the contract affords the noticed party the right during the stipulated period to bring about a condition which will negate the other party's right to terminate"); *see also* W.C. Crais III, Annotation, *Effect of Attempt to Terminate Employment or Agency Contract Upon Shorter Notice Than That Stipulated in Contract,* 96 ALR2d 272 (1964) (exception to general rule in context of terminating agency or employment contract is recognized in the "situation where the contract affords the noticed party the right, during the stipulated notice period, to perform certain acts or bring into existence certain conditions which will nullify or negate his adversary's right to give effective notice").

(i) ¶ 18.1(b)

***20** Hill-Rom asserts that it properly terminated the Agreement pursuant to ¶ 18.1(b). First, Hill-Rom argues that it satisfied its 60-day advance notice of termination when it sent Mextel the April 27, 1999 letter detailing all of the pending problems with the relationship, and advising Mextel that if they were not remedied, the Agreement could be terminated. (Def. Br. In Opp'n., at 5). Second, even if this did not constitute adequate notice, Hill-Rom contends that the December 26, 1999 termination letter was sufficient under the Agreement. (*Id.,* at 5-8; Statement of Disputed Facts, at ¶ 10). Hill-Rom's arguments fail as a matter of law.

The April 27, 1999 letter failed to establish unequivocal notice of termination. *See, e.g.,* *Pomerantz v. Mutual Fire Ins. Co.,* 279 Pa. 497, 124 A. 139, 140 (Pa.1924) ("If the notice be equivocal or not indicative of a present cancellation, but a mere intention or desire to cancel in the future, a cancellation will not be effected."); 16 Summa. Pa. Jur.2d Commercial Law § 5:25 ("Notice to terminate a contract must be clear and unambiguous. Where a notice by Hill-Rom to terminate a contract is unclear and ambiguous it is not effective."). The letter listed various problems with Mextel's design and development of the controllers, including a failure to maintain good design controls and quality work standards, and then threatened that if Mextel "continues to conduct business in this manner, we will have to take appropriate action, which could include termination of Mextel as a developer/supplier as provided under the contract." (*See* April 27, 1999 letter, attached as Ex. 4G To Def. Mot. For SJ.). A threat of possible termination in the future does not constitute clear and unambiguous notice. *See* Accu-Weather, 644 A.2d at 1255 (notice stating that termination of contract applies in "ninety-days," but that services may be "continued" on some later date, is unclear and ambiguous). Furthermore, Hill-Rom's continued performance under the Agreement, as evidenced by its placing of orders for Mextel's controllers in fall 1999, is inconsistent with a clear intent to terminate the contract. *Id.* (no legal notice of termination when party allegedly giving notice continues to perform under Agreement because continued performance gives "mixed and ambiguous" message).

It is equally evident that the December 28, 1999 letter, which purported to terminate the Agreement immediately, failed to comply with the contractually imposed conditions precedent to termination. (*See* December 28, 1999 Termination Letter, attached as Ex. 17 to Pl. Mot. For SJ.). First, the letter failed to provide sixty days notice of termination, as required by ¶ 18.1(b). (*Id.*). Second, and most importantly, the letter failed to give Mextel sixty days to cure the alleged breaches of the Agreement and to thereby maintain the parties' contractual relationship, as required by ¶ 18.1. (*Id.*). Instead, the letter sought to preempt this right to cure by immediately terminating the Agreement, a maneuver that was not permitted by the termination procedures of the Agreement. Accordingly, because Hill-Rom did not follow the conditions precedent to termination, thereby depriving Mextel of its right to nullify Hill-Rom's justifications for termination, the notice based upon ¶ 18.1(b) was ineffective. *See, e.g.,* Luden's Inc., 805 F.Supp. at 323 n. 15. Therefore, Hill-Rom was not excused from complying with the terms of the Agreement based upon its ¶ 18 .1(b) notice of termination.

(ii) ¶ 18.2

***21** Hill-Rom also claims that the December 28, 1999 letter properly terminated the Agreement under ¶ 18.2 of the Agreement because the controller was "obsolete." (*See* Def. Br. In Opp'n., at 8). Although ¶ 18.2 required sixty days notice prior to termination, it did not provide Mextel the right to cure the controller's "obsolescence" within a designated time. (*Id.*).

Hill-Rom's purported termination under ¶ 18.2 was procedurally effective, but only after the expiration of sixty days from the mailing of the termination letter. *See, e.g.,* Wetherell, 743 F.Supp. at 1176. Because Mextel did not have the contractual right to cure the reasons for Hill-Rom's determination of the controller's obsolescence, the only condition precedent with which Hill-Rom failed to comply was the provision of the contractually prescribed amount of sixty days notice. Unlike ¶ 18.1, therefore, the procedural appropriateness of Hill-Rom's purported termination under ¶ 18.2 of the Agreement is covered by the general rule that timely notice of termination allowing a period of time shorter than that stipulated in the contract is effective after the lapse of the stipulated time period. *See, e.g.,* In re Best Film & Video Corp., 46 B.R. 861, 873 (E.D.N.Y.1985). Accordingly, so long as Hill-Rom was justified in concluding that the controller was obsolete, the Agreement expired sixty days after mailing the December 28, 1999 notice of termination to Mextel.

(b) Substantive Propriety

The Court has concluded that the notice of termination pursuant to ¶ 18.1 was procedurally ineffective. However, because the notice of termination pursuant to ¶ 18.2 was procedurally appropriate, the Court now considers whether Hill-Rom was substantively justified as a matter of law in terminating the contract pursuant to ¶ 18.2. Importantly, however, the Agreement does not define the term obsolete, and, in fact, leaves the determination of the controller's obsolescence to the "sole discretion" of Hill-Rom. (*See* Agreement, at ¶ 18.2).

Hill-Rom construes "obsolete" in its colloquial sense, as an outmoded or outdated product. In support of its claim, Hill-Rom provides the testimony of Jan Wenstrup, the engineer responsible for the development of the C2000 incubator. (*See* Wenstrup Aff., attached as Ex. 1 to Def. Br., at ¶ 19). Wenstrup contends that by December 1999, the product was obsolete for several reasons. First, the controller contained an outdated computer processor that was introduced into the marketplace in the mid-1970's and that had limited expansion capabilities. (*Id.*). Second, the controller failed to comply with the initial product specifications by accommodating an interface function, which would have allowed the controller to interface with other devices in addition to the C2000 incubator. (*Id.*). Third, the controller was unable to accommodate a monitoring feature that would have allowed constant monitoring of a baby's vital signs while in the C2000 incubator. (*Id.*).

***22** Mextel provides no direct testimony or other evidence to dispute Wenstrup's conclusion regarding the obsolescence of the controller. Instead, Mextel challenges the definition of "obsolete," contending that the parties' course of dealing establishes that the term "obsolete" means a product that is not marketable. (*See* Pl. Statement of Undisputed Facts, at ¶ 37). Using this definition, Mextel argues that the product could not have been obsolete because "between November of 1996 and December of 1999, Mextel manufactured and shipped to Air-Shields over 5000 controllers covered by the Agreement." (*Id.*). Mextel further argues that during this period, Hill-Rom repeatedly manifested a belief that the controllers were not obsolete. (*Id.*).

This Court must ascertain the mutual intent of the parties by examining the language of the Agreement. *See, e.g., Duquesne Light Co. v. Westinghouse Elec. Corp.,* 66 F.3d 604, 613 (3d Cir.1995) (applying Pennsylvania law). In ascertaining the mutual intent of the parties, the Court must construe terms according to their ordinary usage and meaning. *Id.; Raymark Industries Inc., v. Butera, Beausang, Cohen & Brennan,* 1997 WL 746125, at *7 (E.D.Pa. Dec.1, 1997) (applying Pennsylvania law). The term "obsolete," as defined in Webster's Collegiate Dictionary, means "no longer in use or no longer useful." (*See* Webster's Collegiate Dictionary, at 816 (1990)). This definition is echoed by Black's Law Dictionary, which defines "obsolete" as "no longer in general use; out-of-date." (*See* Black's Law Dictionary, at 1105 (7th ed.1999). Furthermore, Webster's Third International Dictionary notes that the term "obsolete" may apply to any product that is out-of-date, regardless of whether that product is in use or not. (*See* Webster's New Third International Dictionary, at 1558 (1993)). Accordingly, in this context, the Court adopts both the legal and colloquial definition of "obsolete" as a product that is "out-of-date," even if that product is currently in use in some capacity. To be "obsolete" therefore, the controller need not have been unmarketable, although the controller's lack of marketability, its inability to be commercially distributed, would certainly establish its obsolescence.

Mextel provides no evidence to rebut Hill-Rom's testimony that the product was, in an objective sense, out-of-date by December 1999. Nor has Mextel provided any evidence to establish that Hill-Rom's decision to terminate the contract pursuant to ¶ 18.2 was made in bad faith, as a mere pretext for financial or other motivations unrelated to the product's technological outdatedness. Based upon the testimony of Wenstrup, and upon the Mextel's failure to provide evidence to the contrary, no jury could conclude that Hill-Rom's categorization of the product as obsolete in December 1999 was unreasonable. Indeed, although Hill-Rom continued to place orders for the controllers up to December 1999, the controllers lacked significant technological features required both by the original product specifications, such as the RS-232 interface and the SPO2 monitoring system, and by technological advancements in the marketplace, such as a more advanced computer processor, thereby rendering the controller "out-of-date." (*See* Wenstrup Aff., at ¶ 19).

***23** Furthermore, assuming *arguendo* that this Court accepts the strict definition of "obsolete" proffered by Mextel, as the state of being unmarketable, Hill-Rom was still justified in terminating the contract pursuant to ¶ 18.2 because no jury could conclude that Hill-Rom's belief in the unmarketability of the controller in December 1999 was unreasonable. Hill-Rom presents evidence that the controller presented numerous quality issues that hindered its marketability. For instance, Mextel's controller suffered from a failure rate of 21.8% for 1997 and 1998, as compared to a 6% failure rate for the replacement controllers for the time period April 30, 2001 through April 23, 2002. (*See* Ferrante Aff., attached as Ex. 6 to Def. Rsp. To Pl. Mot. For SJ., at ¶ 5). Based upon an analysis of warranty data, Mextel's controller also suffered from a field replacement rate of 15% between the period November 1996 and October 1999, as compared to a field replacement rate of 3% or lower for the replacement controller. (*Id.,* at ¶¶ 6-7). Moreover, according to Wenstrup's testimony, "the rejection rate for incoming controllers from Mextel was ... at an unacceptably high level, as were warranty claims related to the Mextel controller." (*See* Wenstrup Aff., attached as Ex. 1 to Def. Br., at ¶ 8). Richard Drinkwater, the buyer responsible for purchasing products and services from Mextel, also provides affidavit testimony that Mextel's "products were returned at an abnormally high, and ultimately, unacceptable level." (*See* Drinkwater Aff., attached as Ex. 4 to Def. Br. In Opp'n., at ¶ 4).

Hill-Rom also provides evidence to justify a reasonable belief that, in addition to lacking the requisite level of quality, the product was *per se* unmarketable in December 1999 because the continued distribution of C2000 incubators with Mextel's controllers would have subject Hill-Rom to FDA enforcement action. James Utterback, an in-house counsel for Hill-Rom who worked directly with the FDA between January 1998 and December 1999, offers affidavit testimony that Mextel's failure to provide verification, validation, and DMR documentation for the controller precluded Hill-Rom from complying with GMPs. *See* Utterback Aff., at Ex. 3 to Def. Mot. For SJ., at ¶ 3b-e). This, in turn, resulted in a warning letter from the FDA, a finding that the C2000 incubator was "adulterated," and two recalls of the C2000 incubator. (*Id.*). Utterback further testifies that the termination of the contract in December 1999 was the direct result of Hill-Rom's inability to comply with submissions required by the FDA in response to the FDA's complaints and warning letters received in 1998 and 1999. (*Id.*)

James Utterback's testimony is echoed by that of James Wenstrup and Timothy Johnson, Hill-Rom's vice-president of operations until February 2002. According to Wenstrup's testimony, interactions between the FDA and Hill-Rom involved problems with the controller; and specifically, Hill-Rom's inability to provide necessary DMR and verification and validation documentation to satisfy regulatory requirements for medical devices. (Wenstrup Aff., attached as Ex. 1 to Def. Br. In Opp'n., at ¶¶ 4-17). Moreover, according to Johnson's affidavit, Mextel's inability to provide information necessary for Hill-Rom to comply with FDA regulations, coupled with the investigations performed by the FDA in 1998 and 1999, led Hill-Rom "to conclude that there was a very real possibility that the FDA was going to take drastic action against Hill-Rom," such as a seizure of the C2000 inventory or an action to shut down Hill-Rom's Hatboro facility. (*See* Johnson Aff., at Ex. 3 to Def. Br. In Opp'n., at ¶ 4). Indeed, according to Johnson, "my interactions with the FDA in October and November [1999] led me to conclude that a predominant concern the FDA had was with the C2000 controller." (*Id.* at ¶ 5).

*24 Mextel cites the affidavit testimony of Vedran Skulic to rebut Hill-Rom's evidence that the product was unmarketable. Skulic's testimony references the fact that Hill-Rom purchased controllers between November 1996 and December 1999, even after the FDA warning letters and the two recalls. (*See* First Declaration of Vedran Skulic, at ¶ 35). Mextel also cites a December 10, 1996 letter from Hill-Rom to its employees stating that the C2000 "exceeds all other incubators on the market," and a February 1999 comparative review of three nursing incubators by the Medical Devices Agency favorably reviewing the C2000 incubator. (*See* Reports, attached as Ex. 23 to Pl. Mot. For SJ.). However, neither Skulic's testimony, nor the documents cited by Mextel, disputes the failure and replacement rate of the controller. Nor does this evidence render unreasonable Hill-Rom's belief that by December 1999, the FDA was preparing to take "drastic action" against Hill-Rom for problems related to the controller. Finally, Mextel fails to dispute the reasonableness of Hill Rom's belief that by December 1999, due to the lack of verification and validation and of DMR documentation, it was no longer safe to sell the controller on the market to consumers.

Based upon the available record, this Court holds as a matter of law that Hill-Rom was justified in providing notice to terminate the contract in December 2000 based upon ¶ 18.2 of the Agreement. No genuine issue of material fact exists to challenge the reasonableness of Hill-Rom's belief that the controller was "obsolete," both in the sense of being unmarketable and in the sense of being technologically outdated. Furthermore, regardless of whether Mextel was required to follow GMPs in the design and manufacture of the controller, and regardless of whether Mextel breached these practices, Hill-Rom's inability to provide the FDA with necessary validation, verification, and DMR information rendered the controller unusable and unmarketable.

This Court further concludes that because Hill-Rom did not provide sixty days notice of the obsolescence of the controller, the termination of the contract did not become effective until Saturday, February 26, 2000, sixty days after the mailing of the December 28, 1999 letter. (*See* Agreement, at ¶ 24). Hill-Rom was required to perform its obligations under the contract until that date. However, the effective termination of the Agreement on February 26, 2000 discharged Hill-Rom's executory obligations, which included the purchase both of manufactured, but unshipped controllers and of the remaining controllers necessary to reach the minimum amount of 8000 controllers under the Agreement.

b. Cancellation of the Agreement FN15

FN15. Mextel does not assert that ¶ 18.1(b) of the Agreement modified this statutory remedy by prescribing specific procedures for ending the Agreement upon the occurrence of material breaches, which is the definition of "cancellation" under the Pennsylvania UCC. *See* 13 Pa. Cons.Stat. Ann. § 2-106(d) (definition of "cancellation"). Because Mextel failed to raise this argument, and because the Court finds that Mextel was not entitled to cancel the Agreement in December 1999 pursuant to § 2-711(a) of the Pennsylvania UCC, the Court does not address this argument.

Hill-Rom also contends that it properly cancelled the Agreement in December 1999 pursuant to the statutory authority of the Pennsylvania UCC. In support of its position, Hill-Rom characterizes the Agreement as an "installment contract," which the UCC defines as "one which requires or authorizes the delivery of goods in separate lots to be separately accepted ..." 13 Pa. Cons.Stat. Ann. § 2-612(a). In turn, because the Agreement was an installment contract, the failure of past installments of controllers to substantially conform to commercial expectations and contractual specifications constituted a breach of the contract as a whole. *Id*. § 1-612(c) ("Whenever nonconformity or default with respect to one or more installments substantially impairs the value of the whole contract there is a breach of the whole."). As the buyer, Hill-Rom was therefore entitled to cancel the contract and all unexecuted performances. *Id.* § 2-711(a) ("Where the seller fails to make delivery or repudiates or the buyer rightfully rejects or justifiably revokes acceptance then with respect to any goods involved, and with respect to the whole if the breach goes to the whole, the buyer may cancel....").FN16

FN16. This argument, if successful, insulates Hill-Rom from liability for damages for any breaches between December 1999 and the date of the termination of the Agreement, on February 26, 2000.

***25** Hill-Rom's argument fails as a matter of law. Regardless of whether the earlier deliveries of controllers were non-conforming and regardless of whether they impaired the value of the Agreement as a whole, thereby giving Hill-Rom the right to treat the earlier nonconforming deliveries as complete breach, Hill-Rom's post-delivery conduct consistently reinstated the terms of the Agreement up to December 1999. *See* 13 Pa. Cons.Stat. Ann. § 2-612(c) (aggrieved party reinstates contract by accepting nonconforming installation without seasonably notifying of cancellation or demands performance as to future installments). For instance, there is no dispute that Hill-Rom accepted controllers in previous installments without notifying Mextel of its intent to cancel the Agreement. Furthermore, even after receipt of the allegedly non-conforming deliveries, Hill-Rom continued to demand shipments of additional controllers up until the point of cancellation in December 1999. *See, e.g., Traynor v. Walters,* 342 F.Supp. 455, 461 (M.D.Pa.1972) (holding that buyer reinstated contract under Pennsylvania UCC by demanding delivery in future installments of yet undelivered trees, despite allegedly non-conforming aspects of first two deliveries of trees). By placing new purchase orders, Hill-Rom reaffirmed the contract and could only have rejected the yet underlivered installments after delivery, rather than through a premature cancellation. *See* 13 Pa. Cons.Stat. Ann. § 2-612 comment 6 (although defects in prior installments are cumulative in effect, "if only the seller's security in regard to future installments is impaired, he has the right to demand adequate assurances of proper future performance but had not an immediate right to cancel the entire contract"). Accordingly, this Court holds that Hill-Rom was not entitled to cancel the Agreement pursuant to § 2-711 of the UCC.

c. Impracticability/Frustration of Purpose FN17

FN17. Again, this argument, if successful, would insulate Hill-Rom for damages for any breaches between December 1999 and February 26, 2000.

Hill-Rom also argues that it was not required to purchase unshipped controllers or to purchase the minimum number of controllers because the performance of these obligations was impracticable by December 1999. (*See* Def. Br. In Opp'n., at 9; Def. Mot. For SJ., at 16-17).

The Pennsylvania UCC provides a defense when performance "becomes commercially impracticable because of unforeseen supervening circumstances not within the contemplation of the parties at the time of contracting." *See* Comment 1 to 13 Pa. Cons.Stat. Ann. § 2-615. Section 2-615 excuses a seller from delay in delivery or non-delivery if "performance as agreed has been made impracticable by the occurrence of a contingency the non-occurrence of which was a basic assumption on which the contract was made or by compliance in good faith with any applicable foreign or domestic governmental regulation or order whether or not it later proves to be invalid." *See* 13 Pa. Cons.Stat. Ann. § 2-615. To invoke this defense, the seller "must notify the buyer seasonably that there will be delay or nondelivery." *Id.* § 2-615(c).

***26** Although the defense of impracticability within the Pennsylvania UCC does not apply by its literal terms to buyers, Comment 9 to the provision indicates that the rationale for the exemption may apply to the buyer in certain instances. *See* Comment 9. One particular instance is "where the buyer's contract is in reasonable commercial understanding conditioned on a definite and specific venture or assumption, as, for instance, a war procurement subcontract known to be based on a prime contract which is subject to termination, or a supply contract for a particular construction venue." *Id.* Accordingly, this Court concludes that the defense of impracticability is available to buyers under the Pennsylvania UCC in the limited instances articulated in Comment 9.

The defense of impracticability is unavailable to Hill-Rom in this instance. Hill-Rom argues that Mextel's failure to design and manufacture the controller in accordance with FDA regulations made the continued purchase of controllers impracticable, as Hill-Rom would not have been able to resell the controllers in accordance with FDA regulations. (Def. Mot. For SJ., at 15-16). However, the alleged failure to design and manufacture the controller in accordance with FDA regulations was not an "unforeseeable supervening circumstance." *See* Pa. Cons.Stat. Ann. § 2-615, Comment 1; *see also* Restatement (Second) of Contracts § 264 (impracticability applies when supervening government action prohibits performance). Instead, Mextel's alleged failure to meet design specifications was foreseeable, a breach of the provisions the parties negotiated. Indeed, as evidenced by the termination procedures in ¶ 18 and ¶ 19 of the Agreement, the parties contemplated this type of material breach at the time of the formation of the contract, and expressly allocated the risk for such an occurrence by creating procedures to exit the Agreement in the event of such a breach. *See* Anderson on the Uniform Commercial Code § 2-615:42 ("In order to excuse performance, the contingency must be unforeseen and unusual, and mist be distinct from the risks and hazards of a foreseeable character).

Nor does Hill-Rom provide evidence of a supervening FDA action that prohibited the sale of the C2000 incubators with the Mextel controller. The record indicates that the FDA might have been contemplating action against Hill-Rom, but that no enforcement action was taken with respect to the C2000 incubators, and, more specifically, with respect to the controller manufactured by Mextel. Furthermore, although Hill-Rom alleges that it was unable to comply with government regulations, both parties were aware of the existence of FDA regulations at the time of contract formation and incorporated these regulations into the Agreement. Accordingly, Hill-Rom may not invoke section 2-615 of the Pennsylvania UCC to excuse Hill-Rom's obligations under the Agreement. *See, e.g., Rohm & Hass Co. v. Crompton Corp.,* 2002 WL 1023435, at *7 (Pa. C.P. April 29, 2002) (seller's compliance with pre-existing consent decree that substantially increased costs in requirements contract does not make performance impracticable because compliance was foreseeable and not supervening).

3. Hill-Rom's Motion for Summary Judgment

***27** Hill-Rom moves for summary judgment on the remaining counts in plaintiffs' amended complaint, and on Hill-Rom's counterclaims for breach of contract.

A. Breach of Contract Counterclaim

This Court has found that Hill-Rom breached the Agreement by failing to pay Mextel for delivered and accepted controllers and that Mextel reaffirmed the Agreement by continuing to deliver installments of controllers to Hill-Rom, despite lack of payment. This Court has also found that Hill-Rom's failure to follow the appropriate procedures rendered Hill-Rom's attempt to terminate the Agreement based upon ¶ 18.1(b) is ineffective, without deciding whether Hill-Rom was substantively justified in invoking ¶ 18.1(b). Nonetheless, as the Agreement did not terminate until February 26, 2000, Hill-Rom may still recover damages for preceding breaches of the Agreement by Mextel. *See* 13 Pa. Cons.Stat. Ann. § 2-608(a) (when buyer accepts goods and gives notification pursuant to § 2-607(c), buyer may recover damages for any non-conformity of tender the loss resulting in the ordinary course of events from the seller's breach); *see also* Times Mirror Magazine, 103 F.Supp.2d 711, 736 (S.D.N.Y.2000) ("A non-breaching party who elects to continue to perform a contract may still sue later and recover damages solely for the *breach* of the Agreement, provided that it gives notice of the breach to the breaching party."); Restatement (Second) of Contracts § 246 comment b (party who tenders defective, but excused performance still liable "for damages for partial breach because of his defective performance").

Although Hill-Rom's counterclaim includes a laundry list of 24 alleged breaches, the Court will only address those breaches discussed in Hill-Rom's various briefs. (*See* Counterclaim, at ¶ 39(a)-(x)). First, Hill-Rom claims that Mextel breached ¶ 6.1 and ¶ 8.2 of the Agreement by failing to comply with GMPs, such as by failing to provide Hill-Rom with DMR documentation, to perform verification and validation and to provide Hill-Rom with verification and validation documentation, and to maintain for the life of the controller all manufacturing records. (*See* Def. Undisputed Facts, at ¶¶ 2-19). Second, Hill-Rom contends that Mextel breached ¶ 9.4 by failing to correct negative audit findings. (*Id.*, at ¶¶ 20-24). Third, Hill-Rom argues that Mextel breached ¶ 2.1(b) by failing to provide Hill-Rom with information needed to obtain FDA marking clearance for the C2000. (*Id.*, at ¶ 3).

1. Good Manufacturing Practices

Hill-Rom contends that Mextel breached ¶ 6.1 of the Agreement by failing to manufacture the controller in accordance with GMPs. (*See* Def. Mot. For SJ., at 2-7, 15-17).

Mextel, however, contends that it was not subject to GMPs as a matter of contract interpretation. Mextel contends that ¶ 6.1(b) did not require Mextel to comply with GMPs because these regulations expressly exempt "manufacturers of components or parts of finished devices." (Pl. Mot. For SJ., at 18). Instead, ¶ 6.1(b) merely indicates that "Mextel would comply with whatever obligations would be imposed on Mextel by the FDA Act." (*Id.*). Mextel contends that this interpretation is confirmed by Exhibit E to the Agreement, which states that Mextel "is not a medical device manufacturer and is not subject to FDA regulations." (*Id.; see also* Ex. E to Agreement, attached as Ex. 1 to Gugnani Declaration). Mextel further argues that ¶ 6.1(b) is prophylactic, "having been apparently copied from some other agreement." (*Id.*, at 18).

***28** This Court finds as a matter of law that Mextel contractually agreed to manufacture the controller in accordance with GMPs. (*See* Agreement, at ¶ 6.1(b)). The unambiguous language of ¶ 6.1(b) of the Agreement clearly imposes such a contractual obligation:

> The PRODUCTS manufactured by MEXTEL and sold to AIR-SHIELDS under this AGREEMENT shall be ... (b) manufactured in accordance with good manufacturing practices under the ACT.

The obligation is presented in clear, mandatory terms, requiring Mextel to comply with all GMPs during the manufacture of controllers for the term of the contract. *See, e.g.,* *PBS Coals, Inc. v. Barnham Coal Co.,* 384 Pa.Super. 323, 558 A.2d 562, 564 (Pa.Super.Ct.1989) ("In determining the intent of parties to a written agreement, the court looks to what they have clearly expressed, for the law does not assume that the language of the contract was chosen carelessly."). It does not contain conditional or suppositional language, nor does it limit Mextel's private obligation to comply with GMPs to a hypothetical future date. Moreover, although Mextel is correct in pointing out that, as a "manufacturer of components or parts of finished devices," it was exempt from compliance with GMPs pursuant to 21 C.F.R. §

820.1(a), this regulatory provision also states that "such manufacturers are encouraged to use appropriate provisions of this regulation as guidance." *Id.* The Agreement merely transforms this recommendation into a mandatory obligation in the private setting.

Mextel's reliance on Exhibit E and the statement that Mextel is "not a medical device manufacturer and is not subject to FDA regulations" as nullifying ¶ 6.1(b) is misplaced. Exhibit E only confirms that the contractual arrangement between the parties, and Mextel's agreement to comply with GMPs, would not subject Mextel to FDA action for failure to comply with FDA regulations. Exhibit E's declaration does not absolve Mextel of private liability for the contractual assumption of compliance with particular FDA regulations. Moreover, Exhibit E is only relevant with respect to the obligations imposed by ¶ 6.1(a) of the Agreement and other paragraphs in the contract that expressly reference or rely upon Exhibit E, such as the contractual prescription for confirming product conformance in ¶ 9.3. Indeed, to exempt Mextel from compliance with GMPs based upon the existence of Exhibit E would render the language of ¶ 6.1(b) mere surplusage, and the obligations imposed meaningless. *See, e.g., Tenos v. State Farm Ins. Co.,* 716 A.2d 626, 631 (Pa.Super.Ct.1998) (Pennsylvania contract law "does not permit words in a contract to be treated as surplusage."). Such an outcome would violate traditional principles of contract interpretation. *See, e.g., Meeting House Lane, Ltd. v. Melso,* 427 Pa.Super. 118, 628 A.2d 854, 857-58 (Pa.Super.Ct.1993) ("One part of a contract cannot be interpreted so as to annul another part, and a contract must be construed, if possible, to give effect to all of its terms.").

*29 Because the language of the Agreement is clear and unambiguous, the Court need not resort to extrinsic evidence to interpret ¶ 6.1(b).[FN18] *See, e.g., Sabad v. Fessenden,* 825 A.2d 682, 688 (Pa.Super.Ct.2003) (unambiguous contract interpreted according to language selected by parties, while extrinsic evidence only appropriate to interpret ambiguous contractual terms). Consequently, the Court finds that Exhibit E only modifies ¶ 6.1(a), and not ¶ 6.1(b), and that, pursuant to the Agreement, Mextel was required to comply with GMPs during the manufacture of controllers.

FN18. Nonetheless, the Court notes that the use of extrinsic evidence to interpret ¶ 6.1(b) of the Agreement confirms the Court's interpretation. According to David Ascher, Hill Rom's attorney who negotiated the Agreement with Mextel, the intent of ¶ 6.1 was to ensure that Mextel would manufacture the controller so that Hill-Rom could satisfy its regulatory obligations. (*See* Ascher Affidavit, attached as Ex. 13 To Def. Mot. For SJ., at ¶ 6). Although this conflicts with Skulic's understanding of the Agreement, any other interpretation would violate principles of common sense. After all, unless Mextel contractually assumed responsibility for complying with the QS regulation, Hill-Rom, as a regulated party, would have been unable to meet its obligations under the FDCA, thereby subjecting itself to perpetual enforcement action by the FDA and dooming the success of the C2000 incubator from the outset.

a. DMR Documentation

Hill-Rom contends that Mextel breached ¶ 6.1(b) and ¶ 8.2 by refusing to generate and maintain DMR documentation, including device specifications, production process specifications, quality assurance procedures, and packing and labeling, and by refusing to provide Hill-Rom with DMR documentation on a quarterly basis. (Def. Br. In Opp'n., at 11-17; Def. Mot. For SJ., at 15-17). This Court agrees.

From 1996 until April 1999, Hill-Rom sent numerous letters to Mextel demanding DMR documentation, including an April 27, 1999 letter revealing Mextel's continued failure to generate and to provide DMR documentation for the controller. James Utterback, Hill-Rom's in-house counsel from September 1997 until September 2002, Jan Wenstrup, the engineer responsible for development of the C2000 incubator, Doug Spencer, the Vice-President and General Manager of Hill-Rom's Maternal and Infant Care Business Unit until June 22, 1999, and Timothy Johnson, the General Manager at the Hatboro manufacturing facility after 1999, all testify that Mextel never produced, made available, or supplied the information necessary to compile an appropriate DMR for the controller. (*See* Affidavits, attached as Ex. 1-4 to Def. Br. In Opp'n. and Ex. 3 to Def. Mot. For SJ.). Furthermore, FDA documentation, including the June 1998 Warning Letter, the March 1998 483 Letter, the February

1999 483 Letter, and the various inspection reports, confirmed that DMR documentation was lacking with respect to the controller. Finally, an independent audit conducted in April 1999 documented Mextel's lack of compliance with the QS regulations, including a finding of little or no documentation for design control, inspection and testing, and quality records. (*See* April 1999 Supplier Survey Results, attached as Exhibit 3C at Def. Mot. For SJ.).

Despite admitting that Skulic had no prior experience in designing or manufacturing components for medical devices regulated by the FDA, Mextel nonetheless contends that it maintained DMR documentation and provided copies of all manufacturing records for the life of the controllers. (*See* Gugnani Declaration, at ¶ 14; *see* Pl. Statement of Disputed Facts, at ¶ 9). To support this contention, Mextel relies upon: (i) Skulic's affidavit testimony; (ii) a November 5, 1996 certification statement, signed by representatives from Mextel and Hill-Rom, indicating that "complete device mast record documentation per 21 CFR § 820.181 has been developed of the models C2C-1 and C2C-1E Air-Shields Infant Incubator Controllers" and that DMR documentation "in its current form is adequate to provide functional and configuration traceability and to control production processes"; and (iii) a selection of certificates of conformance accompanying the shipment of various orders of controllers. (*See* Pl. Statement of Disputed Facts, at ¶ 9; First Vedran Skulic Declaration, at ¶ 23).

***30** Mextel's proffered evidence fails to raise a genuine issue of material fact. First, Mextel is correct in noting that the November 5, 1996 certification statement averred that DMR documentation in its current form, however "untidy and informal," is "adequate" to "provide functional and configuration traceability and to control production processes." (*See* November 5, 1996 Certification Statement, attached as Ex. 3A to Def. Mot. For SJ.). However, the November 5, 1996 certification statement does not make clear that Mextel possessed formal DMR documentation in compliance with GMPs. Nor does the certification statement indicate that Hill-Rom had access to, evaluated, or approved this form of DMR documentation. In fact, the certification statement suggests the opposite, codifying Mextel's obligation to provide formal DMR documentation to Hill-Rom by December 31, 1996. (*Id.*). Based upon subsequent correspondence, including the February 21, 1997, September 3, 1997, June 30, 1998, and April 27, 1999 letters from Hill-Rom to Mextel demanding DMR documentation, as well as the internal FDA documents and the testimony of Hill-Rom's quality assurance personnel, it is clear that Mextel never provided formal DMR documentation to Hill-Rom on December 31, 1996 or throughout the relationship.

Second, rather than supporting Mextel's position, Skulic's affidavit suggests ambiguity with respect to Mextel's compliance with GMPs. Skulic indicates that Mextel "comported its facilities and Product records as if it were subject to the FDA *to the extent possible* ...." (*See* First Declaration of Vedran Skulic, at ¶ 23) (emphasis added). Skulic also testifies that although Mextel was not subject to FDA regulations, Mextel "did internally comply with all such *substantive* good manufacturing processes." (*Id.*, at ¶ 20) (emphasis added). Furthermore, Skulic suggests lacking the resources and expertise to write the DMR, conceding that "my obligation was to assist in that endeavor, not to write the document." (*Id.*, at ¶ 6). Finally, although Skulic suggests that Mextel "maintained all manufacturing records for the life of the controllers by serial number," Hill-Rom only provides two certificates of conformance as evidence of the existence of DMR documentation. (*Id.*, at ¶ 23).

The certificates of conformance are signed by Mextel's representative, and certify that the controllers were produced "in accordance with the specifications" in Hill-Rom's purchase order and with the "Approved Design Specifications." (*See* Certificates of Conformance, attached as Ex. 22 to Pl. Mot. For SJ.; *see also* First Declaration of Skulic, at ¶ 23). The Certificates of Conformance also provide lot serial numbers, purchase order numbers, and customer part number and description. (*Id.*). The Certificates of Conformance were mandated by ¶ 9.3 of the Agreement, and confirm that the products confirm to quality assurance procedures and specifications identified in Exhibits E and F to the Agreement.

***31** The certificates of conformance do not constitute DMR documentation within the meaning of the FDA regulations. Indeed, they do not contain: (i) device specifications, including appropriate drawings, composition, formulation, and component specifications; (ii) production process specifications, including the appropriate equipment specifications, production methods, production procedures, and production environment specifications; (iii) quality assurance procedures and specifications, including quality assurance checks used and the quality assurance apparatus used; and (iv) packaging and labeling specifications, including methods and processes. *See* 21 CFR § 820.181 (1995). In fact, the certificates of conformance do not even indicate that the products were produced in accordance with GMPs.

Based upon Hill-Rom's overwhelming evidence concerning Mextel's failure to provide DMR documentation, and based upon Mextel's inability to challenge this evidence, this Court concludes that Mextel breached ¶ 6.1(b) and ¶ 8.2 of the Agreement by failing to create, maintain, and provide Hill-Rom with DMR documentation. Hill-Rom is therefore entitled to summary judgment on counterclaims 39(h) and 39(j) with respect to DMR documentation.

b. Verification and Validation

Hill-Rom next argues that Mextel breached ¶ 6.1(b) and ¶ 8.2 by failing to generate and to provide verification and validation information for the controller. (*See* Def. Mot. For SJ., at 16-17). Mextel's alleged breach with respect to verification and validation takes two forms: (a) failure to provide access to the controller source code, which was necessary to enable Hill-Rom to conduct verification and validation and to establish the root causes for allegedly high warranty and failure rates for the Mextel controller; and (b) failure to conduct verification and validation for device design, to validate the production process, and to provide verification and validation records to Hill-Rom. (*See* Def. Statement of Disputed Facts, at ¶ 7; Def. Statement of Undisputed Facts, at ¶¶ 2-4).

i. Source Code

A genuine issue of material fact exists as to whether Mextel provided the controller source code to Hill-Rom. On one hand, Mextel contends that it did provide the source code to a third-party, Cri-Tech, which Hill-Rom hired to develop the verification and validation dossier for the C2000 controller in March 1998. A March 9, 1998 document identified by Mextel states that, despite numerous other failings, Mextel "presented" two components of the controller: the "software source and engineering notes/memos" (*See* March 9, 1998 CriTech Report, attached as Ex. 28 to Pl. Br.). Furthermore, Skulic's affidavit states that he personally provided to Cri-Tech "the source code for the electronic controller software." (*See* Vedran Skulic's Third Declaration, at ¶ 8).

On the other hand, the March 9, 1998 document states that "Mextel still controls the critically needed software source." (*See* March 9, 1998 CriTech Report, attached as Ex. 28, at E09378). Furthermore, an affidavit from the president of Cri-Tech states that noone associated with CriTech has "received or taken any source code from Mextel, Inc., nor has CriTech given Hill-Rom a computer source code drafted by Mextel, Inc." (*See* Rajewski Aff ., attached as Ex. 23, at ¶¶ 4-5). Accordingly, there is a general issue of material fact as to whether Mextel provided the source code to Hill-Rom, and, therefore, whether Mextel breached ¶ 6.1(b) of the Agreement.

ii. Verification and Validation Records

***32** Verification and validation obligations for medical devices were promulgated pursuant to the QS Regulation on October 7, 1996. *See* 21 CFR Part 820 (1997). These regulations were made effective on June 1, 1997. *Id.* These obligations required manufacturers of medical devices to implement "design controls," such as establishing and maintaining procedures for verifying and validating the device design, establishing and maintaining a device history file, and documenting the results of the design verification and validation process. *See* 21 CFR § 820.30(f)-(j) (1997). These obligations also required manufacturers to implement "production and process controls," including validating the production process to establish by "objective evidence that a process consistently produces a result or product meeting its predetermined specifications." *Id.* § 820.70. Manufacturers were further required to maintain a Quality System Record including or referring to the location of records concerning management responsibility. *Id.* § 820.186

No genuine issue of material fact exists that Mextel breached ¶ 6.1(b) by failing to comply with the verification and validation obligations of the QS regulation, particularly with respect to generating and maintaining appropriate documentation. First, Mextel admits that Hill-Rom continued to place orders for, and that Mextel continued to manufacture, controllers after June 1, 1997. (*See* First Skulic Declaration, at ¶

10). Second, the contract mandated that Mextel comply with all GMPs, which, after June 1, 1997, included the QS regulations and its verification and validation requirements. (*See* Agreement, at ¶ 6.1(b)). Third, a body of evidence confirms that Mextel did not comply with these requirements. Hill-Rom sent letters on June 30, 1998 and April 27, 1999 demanding verification and validation documentation for the manufacture of controllers and reiterating Mextel's failure to implement design controls pursuant to 21 CFR § 820.30. (*See* June 30, 1998 Letter and April 27, 1999 Letter, attached as Ex. 4D and 4G to Def. Mot. For SJ.). James Utterback, Jan Wenstrup, and Doug Spencer testify that Mextel failed to provide Hill-Rom with verification and validation information for the controller, that Hill-Rom needed to employ, albeit unsuccessfully, a fixture test to validate incoming controllers against design specifications, and that failure to verify and validate the controller's design led to the 1998 and 1999 recall of the C2000 incubator. (*See* Utterback Aff., at ¶ 3(a)-(d); Wenstrup Aff., at ¶¶ 6-16; Spencer Aff., at ¶ 7). CriTech indicated in its March 9, 1998 Software Verification and Validation Assessment Report and in its November 10, 1999 Proposal that a design history file, as required by § 820.30(j), was lacking for the controller. (*See* CriTech Report, attached as Ex. 28 and 30 to Pl. Mot. For SJ.). Finally, documentation from the FDA, including the March 26, 1998 and the February 19, 1999 letters, observed that verification and validation data, including a DHR, was lacking for the controller. (*See* March 26, 1998 and February 19, 1999 Letters, attached as Ex. 14 to Def. Br.).

***33** Mextel fails to rebut this evidence, and, by relying on the misapprehension that it was not bound by the verification and validation requirements of the GMPs, concedes its failure to comply. For instance, Skulic admits throughout his Third Declaration that Mextel did not believe that it was contractually or legally responsible for generating or supplying verification and validation documentation, and that Mextel never generated or supplied such documentation. (*See* Third Skulic Declaration, at ¶¶ 7-9). Specifically, Mextel admits that it did not have "information relating to the design of the electronic controller," but that Hill-Rom continued to demand such information. (*Id.*). Accordingly, Hill-Rom is entitled to summary judgment on counterclaims 39(b), (h) and (j) with respect to Mextel's failure to comply with the verification and validation requirements of the QS regulation and to provide the appropriate verification and validation documentation to Hill-Rom.

2. Quality Audits

Paragraph 9.4 of the Agreement states that Mextel "shall permit an Air-Shields representative to inspect the facility at which Mextel manufactures PRODUCTS to conduct an audit to ensure compliance with quality assurance protocols of Exhibit F...." (*See* Agreement, at ¶ 9.4). This paragraph further states that "within thirty (30) days of MEXTEL's receipt of AIR-SHIELD's audit report, MEXTEL shall commence and thereafter diligently complete the cure of any deficiencies noted therein." (*Id.*). Although no quality assurance protocols are listed in Exhibit F, Mextel submits that the parties meant to refer to Exhibit E as the list of the quality assurance protocols.

A quality audit was conducted in September 1998 based upon Mextel's compliance with the QS regulations. The September 1998 audit resulted in an "overall survey score" of 58.7% and a "conditional" certification level grade by Hill-Rom. (*See* September 21, 1998 Letter, attached as Ex. 4E to Def. Mot. For SJ.). However, in April 1999, Hill-Rom conducted a second audit to determine compliance with the QS regulations. The second audit demonstrated a decline in a compliance rating from 58.7% to 34%. (*See* April 1999 Results, attached as Ex. 4F to Def. Mot. For SJ.). The certification level was listed as "unacceptable," with "improvement plans" necessary. (*Id.*). In turn, Hill-Rom sent Mextel a letter demanding that Mextel cure these deficiencies immediately, particularly with respect to design controls. (*See* April 27, 1999 Letter, attached as Ex. 4G to Def. Mot. For SJ.). Hill-Rom provides affidavit testimony from James Utterback that Mextel failed to cure any of the deficiencies noted in the reports within 30 days. (*See* Utterback Aff., at ¶ 3f).

Mextel characterizes these audits as "unreasonable demands for overly-detailed written procedures." (*See* Pl. Br., at 10). Mextel contends that, pursuant to the language of ¶ 9.4, the quality audit could only be conducted to ensure compliance with the protocols listed in Exhibit E, rather than with the QS regulations, to which Mextel was not subject as a manufacturer of a component product. (*See* Pl. Disputed Facts, at ¶ 20). Accordingly, because the quality audit performed by Hill-Rom imposed the requirements of the QS regulations, Mextel contends that it did not constitute a "quality audit" within the meaning of the Agreement, and, hence, that Mextel did not breach the contract by failing to remedy the deficiencies in the April 1999 audit report within 30 days. (Pl. Br. In Opp'n., at 10).

***34** The Court agrees that the parties meant to refer to Exhibit E in ¶ 9.4 of the Agreement. The Court also agrees that ¶ 9.4 of the Agreement defined quality audit according to the specifications listed in Exhibit E, so that compliance with those specifications satisfied Mextel's obligations under ¶ 9.4. Nonetheless, because an overlap may exist between a quality audit conducted pursuant to Exhibit E and a quality audit conducted pursuant to the QS regulations, the Court concludes that a genuine issue of material fact exists as to whether Mextel met the requirements of Exhibit E during the April 1999 audit.[FN19] As such, a genuine issue of material fact exists as to whether Mextel failed to cure deficiencies identified in Exhibit E and referenced in the April 1999 audit report, particularly with respect to "in-process procedures" referenced in Exhibit E. Neither Mextel nor Hill-Rom is therefore entitled to summary judgment with respect to counterclaims based on ¶ 9.4 of the Agreement.[FN20]

FN19. Vedran Skulic testifies that Mextel always met the "assurance specifications and protocols that were identified in Exhibit E to the Agreement." (Skulic's Third Declaration, at ¶ 15).

FN20. Nonetheless, as discussed earlier, the failure to comply with QS regulations in April 1999 demonstrates a failure to comply with GMPs in breach of ¶ 6.1(b) of the Agreement.

3. Marketing Clearance

Hill-Rom asserts that Mextel breached ¶ 2.1(b) of the Agreement by failing to provide validation for the product design sufficient to obtain FDA marketing clearance. (*See* Answer, at ¶ 39(b)). Paragraph 2.1(b) of the Agreement states that Mextel shall "provide validation of the PRODUCT design sufficient to enable Air-Shields to obtain FDA marketing clearance for the infant incubators and infant radiant warmer incorporating the PRODUCT." *Id.* The Agreement does not defined the phrase "marketing clearance."

Mextel claims that a July 30, 1996 letter from the FDA provides the required "marketing clearance." The July 30, 1996 letter states:

> You may, therefore, market the device, subject to the general controls provisions of the Act. The general controls provisions of the Act [FDCA], include requirements for annual registration, listing of devices, good manufacturing practice, labeling, and prohibitions against misbranding and adulteration.

(*See* July 30, 1996 Letter, attached as Ex. 8 to Pl. Mot. For SJ.). Hill-Rom, however, interprets this letter as imposing a condition precedent to marketing clearance, so that marketing clearance could only occur upon compliance with the general control provisions of the FDCA.

This Court finds as a matter of law that the July 30, 1996 letter satisfies Mextel's obligation in ¶ 2.1(b) to provide validation of the product design sufficient to obtain "marketing clearance." The July 30, 1996 letter further states:

> This letter will allow you to begin marketing your device as described in your 510(k) premarket notification immediately. An FDA finding of substantial equivalence of your device to a legally marketed predicate device results in a classification for your device and permits your device to proceed to the market, but it does not mean that the FDA approves your device.

(*Id.*). This letter consequently constitutes an initial "marketing clearance," which satisfied Mextel's obligation under ¶ 2.1(b) of the Agreement. Thus, this Court grants summary judgment for Mextel with respect to counterclaims based on ¶ 2.1(b).

4. Remaining Counterclaims

***35** Both Hill-Rom and Mextel seek summary judgment on Hill-Rom's remaining counterclaims, including counterclaims 39(a), (d)-(g), (j), (n)-(x). Because neither Mextel nor Hill-Rom has squarely addressed the merits of these remaining counterclaims, this Court denies each party's respective motion for summary judgment on these counterclaims.

5. Damages

As a result of Mextel's breaches, Hill-Rom seeks the costs associated with recalling Mextels' controller, with developing the replacement controller, with the costs of making FDA submissions, and with a loss of reputation in the marketplace. (*See* Br. In Opp'n. to Pl. Mot. For SJ., at 19). Hill-Rom claims that these costs flow from Mextel's alleged breaches and from the mitigation doctrine. (*Id.*). On the other hand, Mextel contends that the terms of the contract limit the remedies available to Hill-Rom and that Mextel is entitled to summary judgment with respect to Hill-Rom's request for each item of damages.

"An unjustified breach of a contract does not subject the breaching party to all remedies under contract law if the contract provides otherwise." John B. Conomos, Inc. v. Sun Co., Inc., 831 A.2d 696, 708 (Pa.Super.Ct.2003); *see* 13 Pa. Cons.Stat. Ann. § 2-719 (agreement may limit or alter the measure of damages recoverable, with the underlying purpose that parties should be "left free to shape their remedies to their particular requirements"). Unless otherwise modified by contractual terms, a buyer who accepts non-conforming goods retains the right to sue for breach of contract, but must notify the seller of the breach within a reasonable time after she discovers or should have discovered the breach. *Id.* § 2-607. Upon doing so, the buyer may recover damages for any nonconformity of tender, including incidental and consequential damages. *Id.* § 2-714(a)-(b). Incidental and consequential damages are those damages that naturally and proximately flow from the breach or that were foreseeable at the time of contract formation. *Id.; see, e.g., Fran B. Bozzo, Inc. v. Electric Weld Div.*, 435 A.2d 702, 709 (Pa.Super.Ct.1980) (recoverable loss "must be one which ordinarily follows the breach of the sales contract in the usual course of events or one that reasonable men in the position of the parties would have foreseen as the probable results of that breach.")

a. Costs of FDA Submissions

In ¶ 11.1 of the Agreement, Hill-Rom agreed to "make, at its sole costs and expense, all necessary submissions to the FDA...." (*Id.*). However, in the same paragraph, Mextel agreed to provide Hill-Rom "with any assistance reasonably requested by Hill-Rom in connection with the generation of any such test data [necessary for filings] as well as the preparation of the FDA and comparable foreign submissions." (*Id.*).

Hill-Rom claims that because Mextel's breaches led to FDA submissions, including submissions in response to agency inquiries, 483 observations, and warning letters, Mextel may not take advantage of Hill Rom's contractual obligation to pay for such submissions. (*See* Def. Br. In Opp'n., at 18). Mextel, on the other hand, contends that Mextel had no obligation to pay any costs of any regulatory event pursuant to the allocation of expenses within ¶ 11.1. (*See* Pl. Mot. For SJ., at 19).

***36** The language of ¶ 11.1 clearly states that Hill-Rom was required to pay for all "necessary" submissions to the FDA. *Id.* Hill-Rom does not argue that the FDA submissions in response to various inquiries were not "necessary" within the meaning of ¶ 11.1. Nor does the language of ¶ 11.1 give Hill-Rom the discretion to limit this financial obligation to certain factual scenarios. Finally, Hill-Rom fails to cite applicable case law to support its view that ¶ 11.1's contractual allocation of the costs of regulatory submissions is voided by Mextel's breaches of the Agreement, particularly when Hill-Rom continued to reinstate the terms of the Agreement by accepting non-conforming products. Therefore, regardless of whether Mextel's failure to comply with GMPs caused Hill-Rom to make submissions to the FDA, Hill-Rom contractually agreed to assume liability for the costs of all regulatory submissions during the life of the Agreement.

b. Costs of Recalls

Hill-Rom requests summary judgment on the issue of damages for the cost of recalling Mextel's C2000 incubator. (Def. Mot. For SJ., at 19-21). Hill-Rom provides evidence that it initiated an "Urgent Medical Device Notice/Recall" pertaining to problems with the C2000 incubator in May 1998, and then issued a revised recall letter in January 2000. (*See* FDA Documentation, attached as Ex. 14 to Def. Br. In Opp'n., at FDA 00292-00295). Mextel, on the other hand, asks the Court to dismiss ¶ 40(b) of Hill-Rom's counterclaim on the basis of the allocation of costs in ¶ 10.2. (Pl. Mot. For SJ., at 19-20).

Although the Agreement does not define the term "recall," the Court finds from the language of the Agreement, from the context of the contractual arrangement, and from the objective of the arrangement that the parties intended to adopt the FDA's definition of "recall." *See, e.g.,* Bethlehem Steel Corp. v. MATX, Inc., 703 A.2d 39, 42 (Pa.Super.Ct.1997) ("intention of parties paramount and the Court will adopt an interpretation which under all circumstances ascribes the most reasonable, probable, and nature conduct of the parties, bearing in mind the objects manifestly to be accomplished") (internal quotations omitted). According to the FDA, most "recalls" of medical devices are voluntarily conducted by the manufacturer in accordance with 21 CFR Part 7. *See* FDA, *Medical Device Recalls and Corrections and Removals,* available at *h ttp:// www.fda.gov/cdrh/devadvice/51.html# 3* (as of January 25, 2005). This type of voluntary "recall" is defined as a "firm's removal or correction of a marketed product that the Food and Drug Administration considers to be in violation of the laws it administers and against which the agency would initiate legal action, e.g., seizure." 21 CFR § 7.3 (West) According to this definition, a "recall does not include a market withdrawal or a stock recovery." *Id.*

The Agreement contains a provision that applies to recalls of the controller:

> *37 RECALLS: In the event of a recall of any AIR-SHIELDS products that use PRODUCT supplied by MEXTEL hereunder, when it is determined that such an event is caused by PRODUCT malfunction and not by specification or requirement change, MEXTEL shall repair or replace all such PRODUCTS. Whether it is claimed that PRODUCT is causing such an event or not, AIR-SHIELDS will indemnify, defend, and hold MEXTEL, its current directors, officers, employees, and agents harmless from and against any and all claims, liability, product and warranty liability, loss, damages, costs, or expenses.

(*See* Agreement, at ¶ 10.2).

Paragraph 10.2 of the Agreement allocates contractual risk and identifies that the appropriate remedy in the event of a recall is replacement or repair of the products. *Id.* In contrast to Hill-Rom's assertions, the "event" described in the Agreement refers to any form of a recall, rather than to a recall based expressly upon a product malfunction. *Id.* Thus, regardless of whether the controller caused the recall (ie., regardless of whether the recall was for a malfunction or not), Hill-Rom agreed to indemnify Mextel for the costs associated with that recall through ¶ 10.2.

Problematically, however, the remedy available to Hill-Rom pursuant to ¶ 10.2 is expanded by ¶ 21.2 of the Agreement. Rather than the replacement or repair of malfunctioning controllers, Mextel in ¶ 21.2 agreed to indemnify Hill-Rom for the costs of recalls that Hill-Rom incurred as a result of any "hardware failure" within the controller. (*See* Agreement, at ¶ 21.2). Thus, to the extent that ¶ 21.2 requires indemnification for the costs of recalls associated with hardware failures within the controller, it contradicts ¶ 10.2's obligation of Hill-Rom to indemnify Mextel for any costs incurred in connection with the recall of the controller.

Despite these two seemingly contradictory provisions, one harmonizing principle can be devised: Hill-Rom was required to indemnify, defend, and hold Mextel harmless for all damages or costs associated with the recall of the controller, when the recall was not caused by a hardware failure within the controller. In other words, Mextel is entitled to summary judgment on this issue of damages if the recall was not caused by a hardware failure; on the other hand, Hill-Rom *may* be entitled to summary judgment on the issue of damages if the recalls were caused by a hardware failure. With this interpretative overlay in mind, the Court finds several genuine issues of material fact that preclude granting summary judgment on this issue.

First, the Court finds that a genuine issue of material fact exists as to whether the May 18, 1998 urgent medical device notice was a "recall" within the meaning of ¶ 10.1 of the Agreement and FDA regulations.FN21 It is true that a memorandum from the Philadelphia Branch of the FDA refers to the May 18, 1998 notice as a "recall notification." (*See* October 3, 2001 Memorandum Concerning Recall Termination Recommendation, at FDA 00292-00295). Nonetheless, the parties have failed to provide the Court with an appropriate factual or legal framework, including citations to the appropriate regulatory authority, to determine whether the May 18, 1998 urgent medical device notice and any accompanying action was a voluntarily "recall," as defined by the FDCA and within the meaning of ¶ 10.1 of the Agreement.

FN21. Mextel implicitly challenges the categorization of the May 18, 1998 notice as a "recall," noting that "this FDA 'recall' did not require Air-Shields [Hill-Rom] to reissue or replace its products as is classically understood by this term." (Pl. Mot. For SJ., at ¶ 20).

***38** Second, a genuine issue of material fact exists as to whether the process by which Hill-Rom replaced controllers in every C2000 incubator in January 2000 was a "recall." While providing affidavit testimony to indicate that Hill-Rom commenced the process to replace C2000 incubators using the Mextel controller in January 2000, Hill-Rom has failed to provide information relevant to that process, such as the alleged agreement with the FDA to replace such controllers, the procedures by which the event was accomplished, and the results of the process. (*See* Spencer Aff., at ¶ 8). As such, a genuine issue of material fact exists as to whether the January 2000 event meets the definition of "recall" within the meaning of the FDCA and ¶ 10.1 of the Agreement.

Finally, assuming *arguendo* that the May 18, 2000 urgent medical device notice and the January 2000 event that led to the replacement of controllers in the C2000 incubator were "recalls," the Court finds that a genuine issue of material fact exists as to whether the two recalls were caused by a hardware failure in the controller. Hill-Rom provides evidence that the controller suffered from a failure rate of 21.8% for 1997 and 1998, and from a field replacement rate of 15% between November 1996 and October 1999. (*See* Ferrante Aff., at ¶ 5-7). Furthermore, an October 3, 2001 Memorandum concerning the termination of the recalls, approved by the director of the Philadelphia Investigations Branch for the FDA, stated that the FDA issued to Hill-Rom a recall recommendation for the C2000 incubator in May 1998 and that the reason for the recall recommendation was the product's potential to cause serious injuries and deaths." (*See* October 3, 2001 Concerning Recall Termination Recommendation, attached as Ex. 14 to Def. Br. In Opp'n., at FDA 00292-00295). The October 3, 2001 Memorandum further states that "the unresolved problems were with regard to the controller and the humidity module," and particularly with regard to their failure to meet QS/GMP requirements. (*Id.*).

On the other hand, as Mextel points out, FDA inspection reports and 483 letters throughout 1998 and 1999 listed problems with components of the C2000 incubator independent of the controller and with deficiencies in Hill-Rom's manufacturing process. (*See id .*). For instance, the November 30, 1999 inspection report lists specific problems with Hill-Rom's complaint handling procedures, and documents complaint occurrence for the humidity system as well as the controller. (*See* November 30, 1999 483 Letter, attached as Ex. 14 to Def. Br. In Opp'n., at FDA 00179-181). The March 26, 1998 inspection report, which precipitated the May 1998 notice, lists problems with the C2000's simulator, with Hill-Rom's complaint handling procedures and documentation, with a lack of oversight when problems are detected in the manufacturing of the C2000 incubator, and with Hill-Rom's quality system compliance. (*See* March 26, 1998 483 Letter, attached as Ex. 14 to Def. Br. In Opp'n., at FDA 00286-291). Furthermore, the requisite link between the malfunction of the incubator and the recalls is undermined by Mextel's contradictory position that the recall was not initiated because the controller failed to work properly, or "malfunctioned," but, instead, because Mextel failed to comply with regulatory requirements to verify that the controller would not malfunction. (*See* Def. Mot. For SJ., at 20).

***39** Accordingly, because genuine issues of material fact exist as to whether Hill-Rom conducted recalls within the meaning of the FDCA, and, if so, as to whether the recalls were caused by a malfunction or hardware failure with the controller, neither party is entitled to summary judgment on the issue of recall damages.

c. Cost of Developing a Replacement Controller

Plaintiff contends that no basis exists for the recovery of costs incurred to develop and design a replacement controller. (*See* Pl. Mot. For SJ. For. SJ., at 20). However, the Agreement does not limit Hill-Rom's right to seek the costs of developing a replacement controller in the event of Mextel's material breach of the Agreement. Furthermore, pursuant to the Pennsylvania UCC, a buyer, such as Hill-Rom, who accepts a non-conforming product, such as a controller that lacks DMR documentation and verification and validation analysis, may seek damages for the non-conformity, as well as incidental damages, which include "any commercially reasonable charges, expenses in connection with effecting cover," and consequential damages, which include damages that were "reasonably foreseeable" at the time of contract formation. *See* 13 Pa. Cons.Stat. Ann. § 2714; *AM/PM Franchise Ass'n v. Atlantic Richfield Co.* ., 526 Pa. 110, 584 A.2d 915, 921 (Pa.Super.Ct.1990) (defining consequential damages).

Nonetheless, a genuine issue of material fact exists as to whether the costs associated with the development of a replacement controller flow from Mextel's breaches of the Agreement, particularly because Hill-Rom started soliciting proposals for a replacement controller in 1998 and has not documented the timing of particular expenses for the replacement controller. (*See* Comtec and Battelle Proposals, attached as Ex. 26-27 to Pl. Br. In Opp'n.). A genuine issue of material fact also exists as to whether Hill-Rom complied with the provisions of the Pennsylvania UCC permitting a recovery of incidental damages in such a situation. *See* 13 Pa. Cons.Stat. Ann. § 2-607 (requiring buyer who accepts goods and who seeks to recover for breach to notify seller of breach within reasonable time after she discovers or should have discovered breach). Accordingly, neither Hill-Rom nor Mextel is entitled to summary judgment on ¶ 40(d) of Hill-Rom's counterclaim.

d. Lost Profits From Reputation Damage

The Agreement does not limit Hill-Rom's right to recover consequential damages, including reputation damages. Section 2-715 of the Pennsylvania UCC permits the recovery of loss of good will, including damage to reputation, and the loss of future profits as a result of that loss of good will. *See, e.g., AM/PM Franchise Assoc. v. Atlantic Richfield Co.*, 526 Pa. 110, 584 A.2d 915, 926 (Pa.1990) (holding that good will damages, including loss of business reputation, is available as consequential damages under sections 2-714 and 2-715 of the Pennsylvania UCC).

Hill-Rom offers only conclusory and speculative statements, without specific evidentiary support, that Hill-Rom's reputation suffered because of the problems with the Mextel controller and the process of replacing all C2000 incubators that contained a Mextel controller in 2000. (*See* Johnson Aff., at ¶ 8; Wenstrup Aff., at ¶ 3). Genuine issues of material fact therefore exist as to whether Hill-Rom suffered loss of reputation due to the alleged "recalls" of the C2000 incubator, and whether this loss of reputation flowed from Mextel's breaches of ¶ 6.1(b) and ¶ 8.2 of the Agreement. A genuine issue of material fact also exists as to the amount of such damages. *See, e.g., Glenn Distributors Corp. v. Carlisle Plastics, Inc.*, 297 F.3d 294, 305 (3d Cir.2002) (evidence of lost profits must be demonstrated to a fair degree of probability). Accordingly, neither Hill-Rom nor Mextel is entitled to summary judgment on ¶ 40(c) of Hill-Rom's counterclaim.

B. Counts II and III: Quantum Meruit and Unjust Enrichment

***40** Counts II and III of the Mextel's complaint seek damages on the legal theories of quantum meruit and unjust enrichment. Hill-Rom seeks summary judgment on these claims, asserting that they may not survive because of the existence of the written contract.

Claims for quantum meruit and unjust enrichment presuppose the absence of a valid contract. *See, e.g., Hershey Foods Corp v. Ralph Chapek*, Inc., 828 F.2d 989, 1000 (3d Cir.1987) (applying Pennsylvania law); *Villoresi v. Femminella*, 856 A.2d 78, 84 (Pa.Super.Ct.2004) ("Where an express contract already exists to define the parameters of the parties' respective duties, the parties may avail themselves of contract remedies and an equitable remedy for unjust enrichment cannot be deemed to exist."). Mextel admits that the written agreement covers the electronic controller. However, Mextel contends that the sensor modules were not covered by the Agreement, and, thus, that Mextel's quantum meruit and unjust enrichment claims should survive with respect to the shipment of sensor modules.

The Agreement permitted Hill-Rom to submit purchase orders for the sale and purchase of "products." (*See* Agreement, at ¶ 9.1). The Agreement defines "products" as "the electronic controller" for Hill-Rom's infant incubators and infant radiant warmers. (*Id.*, at ¶ 1.17). Thus, Mextel's production and shipment of the sensor modules to Hill-Rom was not expressly covered by the Agreement. Nor has Mextel identified any other contract, written or oral, for the design and supply of sensor modules to Hill-Rom.

Hill-Rom is therefore not entitled to summary judgment with respect to Mextel's quantum meruit and unjust enrichment claims regarding the sensor modules.

C. Count IV: Breach of Implied Covenant of Good Faith and Fear Dealing

In its opposition brief, Mextel voluntarily withdraws Count IV of its amended complaint. (*See* Pl. Br. In Opp'n. to Def. Mot, at 1 n. 1). Accordingly, this Court grants Hill-Rom's motion for summary judgment with respect to Mextel's claim for breach of the implied covenant of good faith and fear dealing.

D. Count VI: Misappropriation of Trade Secrets

Count VII of the amended complaint alleges that Hill-Rom misappropriated plaintiffs' source code that formed the software template for the plaintiffs' controller. (Am. Compl., at ¶¶ 48-52). In their opposition brief, plaintiffs further allege that Hill-Rom stole the executable code and trade secrets relating to the sensor module. (Pl. Br. In Opp'n. to Def. Mot. For SJ., at 21-24).

A trade secret can be "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." Prudential v. Stella, 994 F.Supp. 318, 323 n. 2 (E.D.Pa.1998). In order to prevail on a claim for misappropriation of trade secrets, plaintiffs must establish: (1) the existence of a trade secret; (2) which was communicated in confidence to Hill-Rom; (3) used by Hill-Rom in breach of that confidence; (4) to the detriment of the plaintiff. *See, e.g., Moore v. Kulicke & Soffa Industries, Inc.,* 318 F.3d 561, 566 (3d Cir.2003); *Pennfield Precision, Inc. v. EF Precision, Inc.,* 2000 WL 1201381, at *3 (E.D.Pa. Aug.15, 2000) (outlining elements).

1. Source Code

***41** Hill-Rom implicitly agrees that the executable component of the source code for the controller, that hidden portion of the code encoded by the source code, is a "trade secret." (Def. Mot. For SJ ., at 22-23; Def. Reply Br., at 6). However, Hill-Rom claims that there is no evidence to support the remaining elements of plaintiffs' cause of action-that plaintiffs communicated the source code to Hill-Rom and that Hill-Rom used that source code without plaintiffs' permission in its new incubator products. (*Id.*).

This Court agrees. Hill-Rom presents the testimony of Colin Jackson, the software project engineer for Comtec Systems, Inc. ("Comtec"), the company that contracted with Hill-Rom for the design and development of the replacement controller. (*See* Jackson Aff., attached as Ex. 8 to Def. Mot. For SJ.). According to Jackson, neither he nor anyone else at Comtec ever used or had access to plaintiffs source code. (*Id.,* at ¶¶ 3-5). Jackson further testifies that Comtec did not reverse engineer the replacement controller from plaintiffs' executable code and that Comtec never received a copy of plaintiffs' executable code from Hill-Rom. (*Id.*).

Jackson's testimony is reinforced by the testimony of Michael Mountain, Hill-Rom's in-house software engineer who amended the Comtec source code prior to its inclusion in the new C2000 incubator. (*See* Mountain Aff., attached as Ex. 9 to Def. Mot. For SJ.). Mountain's affidavit avers that work performed on the replacement controller was "done totally independent of any source code generated by Mextel." (Id., at ¶ 4). Specifically, Mountain testifies that neither he nor anyone working on the replacement controller software used any source code language from the original controller, reverse engineered any source code or executable code from the original controller, or used the source code from the original controller in designing the replacement controller. (*Id.,* at ¶¶ 2-4).

Plaintiffs have failed to present any evidence to rebut this testimony, let alone to articulate a coherent theory as to how Hill-Rom misappropriated the source code.[FN22] Instead, plaintiffs attempt to establish the existence of a genuine issue of material fact by arguing: (i) that Hill-Rom has not produced the source code for the replacement controller in discovery, despite plaintiffs' production of the source code to Hill-Rom; and (ii) that plaintiffs worked directly with Hill Rom's engineers during the production of the plaintiffs electronic controllers. (Pl. Br. In Opp'n., at 21-23).

FN22. Plaintiff seems to have withdrawn from its earlier position that CriTech's representative took plaintiffs source code for the

> controller on behalf of Hill-Rom. (*See* Answer to Interrogatory, attached as Ex. 5 to Def. Mot. For SJ., at 4). Nonetheless, Hill-Rom includes an affidavit from CriTech's president, who categorically denies misappropriating the source code. (*See* Rajewski Aff, attached as Ex. 23 to Def. Mot. For SJ., at ¶¶ 2-5).

Plaintiffs' factual disputes are not material to the elements necessary to establish a cause of action for trade secret misappropriation. *See* Jersey Central Power & Light Co. v. Lacey Township, 772 F.2d 1103, 1109 (3d Cir.1985) (summary judgment motion not defeated by existence of factual dispute, but, instead, by existence of factual dispute *material* to resolution of claims). First, regardless of the veracity of plaintiffs' allegations concerning the production of the new source code during discovery, plaintiff has failed to put forth any evidence indicating that Hill-Rom used plaintiffs' source code to create the replacement controller. In fact, plaintiffs' admission that it failed to obtain Hill-Rom's source code for the replacement controller despite nearly two years of discovery is fatal to plaintiffs' cause of action; it reveals that plaintiffs will not be able to present evidence at trial, in the form of comparative analysis, that Hill-Rom used plaintiffs' trade secrets, indeed, that the new source code is identical to, or shares similar characteristics with, plaintiffs source code. *See, e.g.,* Block v. Blakely, 2004 WL 1902520, at *2 (E.D.Pa. Aug.24, 2004) (summary judgment appropriate when plaintiff fails to make sufficient showing as to element of claim for trade secret misappropriation). Second, the fact that Hill-Rom's engineers worked with Skulic and Mextel's engineers to develop the controller does not establish that Hill-Rom's engineers had access to the source code, nor that they communicated the source code to a third-party to develop the replacement controller. Based upon the record before the Court, no reasonable juror could conclude that Hill-Rom misappropriated plaintiffs' source code.

2. Sensor Module

***42** Plaintiffs argue in their opposition brief that Hill-Rom misappropriated trade secrets related to the sensor module. (*See* Pl. Br. In Opp'n. to Def. Mot. For SJ., at 22-23). Hill-Rom claims that this argument is impermissible at this stage in the litigation because these factual allegations were never articulated in the amended complaint. (*See* Def. Reply Br., at 6-7). Hill-Rom further asserts that the record is devoid of any support for these allegations. (*Id.*).

This Court agrees that plaintiffs never asserted that Hill-Rom misappropriated trade secrets related to the sensor module in the amended complaint. *See, e.g.,* Conley v. Gibson, 355 U.S. 41, 47-48, 78 S.Ct. 99, 2 L.Ed.2d 80 (1957) (complaint must "give the defendant fair notice of what the plaintiff's claim is and the grounds upon which it rests"). Nonetheless, assuming *arguendo* that plaintiffs were entitled to raise this additional misappropriation claim at this point in the litigation, plaintiffs have failed to identify any evidence in support of their claim. Plaintiffs rely upon 48 documents produced by Hill-Rom to Da-Tech, the third party engaged by Hill-Rom to manufacture the new sensor module, to support their misappropriation claim. (*See* Da-Tech Documents, attached as Ex. 38 to Pl. Mot. For SJ., at DA 01513-27, DA 01550-75, and DA 02551-57). According to plaintiffs, these documents demonstrate that Hill-Rom provided and used plaintiffs' trade secrets, such as specifications, drawings, and other information, to manufacture the new sensor modules. (*Id.*).

These documents fail to support plaintiffs' misappropriation claim. Plaintiffs fail to document its ownership of the allegedly confidential information in the Da-Tech documents, such as by providing testimony or documentation that the material within the Da-Tech documents was used in the design, production, or manufacture of the original sensor modules. Indeed, many of the Da-Tech documents themselves indicate that the information is the property of Hill-Rom. (*See* Da-Tech Documents, at DA01513, DA01550, DA01559, DA02551). Nor do plaintiffs identify what information contained in the Da-Tech documents is a trade secret and what alleged trade secrets were used by Hill-Rom and Da-Tech to produce the replacement sensor module. Plaintiffs, as the ultimate bearers of proof, have failed to meet their burden at the summary judgment stage of demonstrating a genuine issue for trial. Accordingly, this Court grants Hill-Rom's summary judgment motion as to the misappropriation claim with respect both to the sensor module and the controller.

E. Count VIII: Trade Dress Infringement

Plaintiffs voluntarily withdraw Count VIII of their amended complaint. (*See* Pl. Br. In Opp'n. to Def. Mot, at 1 n. 1). Accordingly, this Court grants Hill Rom's motion for summary judgment with respect to plaintiffs' trade dress infringement claim.

F. Count IX: Unfair Competition

Plaintiffs do not identify the basis of their claim for unfair competition. Presumably, plaintiffs proceed on the theory that Hill-Rom was "passing off" plaintiffs' controller, trade secrets, and/or trademarks as that of Hill-Rom in the marketing and sale of the C2000 incubator. *See, e.g.,* Restatement (Third) of Unfair Competition § 5 (1995) (liability for deceiving or misleading prospective purchasers by causing mistaken belief that defendant is manufacturer, producer, or supplier of plaintiff's goods or services); *see also* *Scott Fetzer Co. v. Gehring,* 288 F.Supp.2d 696, 703 (E.D.Pa.2003) (to prove unfair competition concerning trademarks under Pennsylvania common law, plaintiff must show that trademark is valid and legally protectable, that trademark is owned by plaintiff, and that defendant's use of the mark to identify goods and services is likely to create confusion concerning the origin of goods or services); *Haymond v. Lundy,* 2001 WL 15956, at *2-3 (E.D.Pa. Jan.5, 2001) (outlining elements). Under Pennsylvania common law, the "essence" of the claim lies in the "deception practiced in 'passing off' the goods of one for that of another." *Pennsylvania State Univ. v. Univ. of Orthopedics, Ltd.,* 706 A.2d 863, 870 (Pa.Super.Ct.1998). Indeed, the underlying purpose motivating the law of unfair competition is to prevent "substitution by deception." *Id.*

***43** Hill-Rom offers evidence that there were never visible markings on the C2000 that identified Mextel as the manufacturer or designer of the controller or its software, therefore making it impossible for consumers to be confused as to the source of the replacement controller. (*See* Boone Aff., attached as Ex. 6 to Def. Mot. For SJ., at ¶¶ 3-5). Plaintiffs lone response to this argument is that the "misappropriation of Mextel's trade secrets also renders Air-Shields liable for unfair competition." (*See* Pl. Br. In Opp'n., at 24).

This Court has already granted Hill Rom's summary judgment motion on plaintiffs' claim for misappropriation of trade secrets, concluding that plaintiffs failed to establish Hill-Rom's impermissible use of plaintiffs' trade secrets in the design, manufacture, and sale of the new C2000 incubator. With respect to the unfair competition claim, plaintiffs have also failed to create a genuine issue of material fact that Hill-Rom unfairly passed off plaintiffs' products, trade secrets, or trademarks as its own. Nor have plaintiffs put forth any evidence of consumer confusion as to the origin or source of the replacement controller or of any other components of the new C2000 incubator. *See, e.g., Haymond,* 2001 WL 15956, at *3-4 (summary judgment appropriate when plaintiff fails to demonstrate likelihood of confusion among consumers); *Polymer Dynamics, Inc. v. Bayer Corp.,* 2000 WL 1146622, at *8 (E.D.Pa. Aug.14, 2000) (consumer confusion essential element of unfair competition claim under Pennsylvania common law). Consequently, the Court grants Hill Rom's motion for summary judgment with respect to the unfair competition claim in Count IX of the amended complaint.

G. Count VI: Patent Infringement

Defendant moves for summary judgment on plaintiffs' patent infringement claim. (Def. Mot. For SJ., at 18-22). A determination of patent infringement requires a two-step analysis. *See PSC Computer Products, Inc. v. Foxconn Int'l., Inc.,* 355 F.3d 1353, 1357 (Fed.Cir.2004). The court must first interpret the claims to determine their scope and meaning. *Id.* The court must then compare the properly construed claims to the allegedly infringing device. *Id.*

The burden is on the plaintiff to prove infringement by a preponderance of the evidence. *Advanced Cardiovascular Sys., Inc. v. Scimel Like Sys. Inc.,* 261 F.3d 1329, 1336 (Fed.Cir.2001). To establish infringement of a patent, "every limitation set forth in a claim must be found in an accused product or process exactly or by a substantial equivalent." *Johnston v. Ivac Corp.,* 885 F.2d 1574, 1577 (Fed.Cir.1989). An accused infringer is therefore "entitled to summary judgment, on the ground of non-infringement, by pointing out that the patentee failed to put forth evidence to support a finding that a limitation of the asserted claim was met by the structure in the accused devices." *Johnston,* 885 F.2d at 1578. General denials and conclusory statements are insufficient to meet the non-movant's burden. *See Hodash v. Black Dog Drug Co.,* 786 F.2d 1136, 1141 (Fed.Cir.1986).

***44** Hill-Rom argues that it is entitled to summary judgment on plaintiffs' patent infringement claim for several reasons. First, Hill-Rom argues that the Court need not perform an initial claim construction of the '006 and '083 patents because the record lacks a basis for a reasonable juror to find by a preponderance of the evidence that a product possessed by Hill-Rom infringes on plaintiffs' patented devices. (*See* Def. Mot. For SJ., at 12-14, 18-19). Second, assuming that claim construction is necessary, Hill-Rom specifically contends that the '006 patent is not infringed because the heater assembly in the C2000 lacks a mounting bushing. (*Id.*, at 19-20). Third, Hill-Rom contends that even if the '830 patent is infringed, it is invalid because it was "on sale" more than one year prior to the filing of the patent application. (*Id.*, at 20).

Hill-Rom first argues that the record fails to identify any basis to support plaintiffs' infringement claim-that Hill-Rom's sensor module and heater assembly in the new C2000 incubator infringe upon each and every limitation in various claims of the '006 and the '830 patents. Hill-Rom emphasizes that plaintiffs failed to provide answers to interrogatories, which asked plaintiff Skulic to identify the products that he contends infringe upon the '006 and '830 patents, to specify the claims of those patents that are infringed, and to explain how, on an element-by-element basis, those claims read on the accused products. (*See* Hill-Rom's Interrogatory Requests, attached as Ex. 14-15 to Def. Mot. For SJ.). Furthermore, Hill-Rom contends that because plaintiffs failed to inspect the replacement controller and sensor module during the requisite discovery period, despite numerous opportunities to do so, plaintiffs cannot identify what elements of Hill-Rom's new incubator are infringing. (*See* Letters to Plaintiffs' Counsel, attached as Ex. 16-19 to Def. Mot. For SJ.).

This Court agrees. Plaintiffs' lone response to Hill-Rom's motion is the testimony of the patentee. According to Skulic's Third Declaration, he inspected an Isolette C2000 incubator with replacement versions of the heater assembly, the controller, and the sensor module in a hospital in Evanston, Illinois. (*See* Vedran Skulic's Third Declaration, at ¶¶ 22-23). Skulic asserts that the inspected incubator "is consistent with all the documents produced in this case indicating that it is the current version of the C2000 being commercialized by Air-Shields." (*Id.*, at 23). Skulic testifies that he was able to take apart the infringing C2000 incubator, and to review and photograph the internal mechanisms of the sensor module and the heater assembly. Skulic concludes that the Isolette C2000 Incubator included "all the elements of one or more claims of both of my patents." (*Id.*, at ¶¶ 25-26).

Skulic's testimony fails as a matter of law to overcome Hill-Rom's summary judgment motion. *See, e.g., Johnson,* 885 F.2d at 1578 (affidavit stating that grip mechanism of accused thermometer infringes upon claims 1, 2, 3, 4, 5, and 6 of the patent constitutes conclusory statement and fails to raise a genuine evidentiary dispute for jury). First, plaintiffs offer no specific evidence that the C2000 incubator inspected by Skulic was in fact the incubator sold by Hill-Rom. Rather than inspecting products that Hill-Rom made available, plaintiff investigated an incubator in a hospital that appeared "consistent" with what the exchanged documents indicated was Hill-Rom's product. (*See* Letters to Plaintiffs' Counsel For Scheduling of Inspection, attached as Ex. 16-19 to Def. Mot. For SJ.). Second, Skulic's photographs of the accused products are not accompanied by a factual description of the elements in the accused sensor module and heater assembly, of where these elements are located, or of their relationship to claims in the plaintiffs' patents. Third, Skulic's testimony relies upon conclusions without factual support. *See, e.g., TechSearch LLC v. Intel Corp.,* 286 F.3d 1360, 1372 (Fed.Cir.2002) ("infringement must be shown literally or equivalently for each limitation; general assertions of facts, general denials, and conclusory statements are insufficient to shoulder the non-movant's burden"). Specifically, Skulic's Third Declaration fails to provide any fact-based analytical comparison between the accused and patented products, let alone any evidence demonstrating how each limitation in the relevant claims for both the '006 patent and '863 patent is found in the accused products. *See, e.g., McKeown v. Bayshore Concrete Products Cor.,* 2002 WL 914339, at *2 (Fed.Cir. May 7, 2002) (granting summary judgment to defendant when plaintiff patentee relies on broad statements in his own affidavit alleging, without factual support, that "he has personally inspected [defendant's] products, compared them to the '020 patent, and found that the accused structures contain every element" of the infringed upon claim). In fact, with the exception of Claim 1 of the 006 patent, [FN23] Skulic fails to identify which claims are being infringed. What Skulic does present is the naked conclusion that the C2000 incubator "includes all the elements of one or more claims of both of my patents." (*See* Third Skulic Declaration, at ¶ 24). Such a statement, without more, fails to raise a genuine issue of material fact. *McKeown,* 2002 WL 914339, at *2 (unsupported, conclusive statements on the issue of infringement "are wholly insufficient to raise a genuine evidentiary dispute for trial"); *see* Fed.R.Civ.P. 56(e) (nonmoving party must "set forth *specific facts* showing that there is a genuine issue of trial") (emphasis added).

FN23. Claim 1 of the '006 patent reads as follows:

1. An infant incubator heater assembly comprising:

a mounting plate adapted for attachment to a base of an incubator;

a mounting bushing mounted to said mounting plate;

a heat radiator removably attached to said mounting bushing and having a plurality or radially extending fins; and

a cartridge heater extending through said heat radiator in heat transfer relationship with said heat radiator and mounted to said mounting bushing.

(*See* '006 Patent, attached as Ex. 2 to Second Skulic Declaration and as Ex. 11 to Def. Mot. For SJ.).

***45** It is true that this Court has yet to offer a formal claim construction of the two patents. It is also true that an infringement analysis typically begins with claim construction. *See, e.g., PSC Computer Products,* 355 F.3d at 1357. However, the sequence of this process is not absolute, and, in an effort to avoid advisory opinions, only terms that are disputed, thereby placing such terms actually in controversy in the infringement litigation, are construed. *See, e.g., Unitherm Food Systems, Inc. v. Swift-Eckrich, Inc.,* 375 F.3d 1341, 1350 (Fed.Cir.2004) (district court not obligated to construe undisputed claim terms prior to issuing summary judgment on invalidity); *PSC Computer Products,* 355 F.3d at 1357 (affirming district court's decision to not construe claims as first step of infringement analysis because their meaning was not disputed); *Westvaco Corp. v. Viva Magnetics Ltd.,* 2002 WL 31052870, at *2 (S.D.N.Y.2002).FN24 Furthermore, the lack of an express claim construction by the Court does not absolve plaintiffs of their burden at the summary judgment stage to provide factual support for the conclusion that each and every limitation in the germane claims of the two patents reads on the accused devices. *See Linear Tech. Corp. v. Impala Linear Corp.,* 379 F.3d 1311, 1325-1326 (Fed.Cir.2004) (because patent holder bears the burden of establishing infringement at trial, defendant need only establish a deficiency concerning an element of plaintiff's claim). Indeed, without this evidence, the Court's initial claim construction is superfluous, as there is no description of the specific product, let alone its elements, with which to compare the claims of plaintiffs' patents. *See, e.g., Techsearch,* 286 F.3d at 1369 ("Summary judgment of non-infringement is also appropriate where the patent owner's proof is deficient in meeting an essential part of the legal standard for infringement, because such failure will render all other facts immaterial.").

FN24. The Court notes that in this instance, plaintiffs dispute only one term-the phrase "mounting bushing" in claim 1 of the '006 patent. (*See* Third Skulic Declaration, at ¶ 28-29). Resolution of this disputed construction is immaterial because plaintiffs have not met their burden of providing a factual analysis that the limitations in claim 1 of the '006 patent are infringed by Hill-Rom's heater assembly. Furthermore, Hill-Rom offers evidence, including an affidavit from Ronald Kolarovic, the senior electrical engineer of the new C2000 incubator, along with technical drawings of the new heater assembly unit, that the heater assembly for the new C2000 incubator lacks a mounting bushing, and, in fact, was purposefully designed to eliminate such an element. (*See* Kolarovic Aff., attached as Ex. 21 to Def. Mot. For SJ.). This analysis is also confirmed by U.S. Patent 6,646,232 (" '232 patent"), which was issued for Hill-Rom's new heater assembly unit and which does not claim a mounting bushing for the device. (*See* Claim 1 of '232 Patent, attached as Ex. 13 to Def. Mot. For SJ.). Once again, plaintiffs fail to present any factual evidence to challenge this showing, with the exception of Skulic's general conclusions that the new heater assembly unit possesses a "mounting bushing" and that, even if it does not, the new heater assembly unit is substantially equivalent to the '006 patent. (*See* Third Skulic Declaration, at ¶¶ 28-29) ("As described in Mr. Kolarovic's affidavit and the one drawing that he produced, and based on my inspection of the new incubator, the revised heater assembly still does the same thing, the same way, and achieves the same results as the heater assembly that is described in the 006 patent and in my patent claims.").

In summary, plaintiffs have failed to make the requisite showing to defeat summary judgment. The discovery period in this litigation lasted more than 15 months, and has been closed for an additional ten months. *See, e.g.,* Spectra Corp. v. Lutz, 839 F.2d 1579, 1581 (Fed.Cir.1988) (thirteen months of discovery to pursue patent infringement claims constitutes reasonable discovery period). Despite this time, plaintiffs never inspected the allegedly infringing products in Hill Rom's possession, and have only identified one specific patent claim that was infringed. Moreover, with respect to this claim, plaintiffs rely upon conclusory allegations, without factual support, that each limitation in claim 1 of the '006 patent is found in the new heater assembly for the C2000 incubator. Plaintiffs provide no testimony comparing in a comprehensive manner the patented devices and the accused devices, nor does plaintiff identify with clarity the elements of the accused devices that are allegedly infringing. Finally, plaintiffs never filed a Rule 56(f) affidavit requesting a delay in the resolution of Hill-Rom's summary judgment motion and additional time to pursue discovery on its infringement claims so that it could "present by affidavit *facts* essential to justify the party's opposition." Fed.R.Civ.P. 54(f) (emphasis added). Accordingly, this Court finds that Hill-Rom is entitled to summary judgment on plaintiffs' infringement claim as a matter of law. FN25

FN25. As a result of this holding, the Court need not address plaintiffs' motion for summary judgment as to the dismissal of Hill-Rom's patent defenses and counterclaims.

IV. Conclusion

***46** For the preceding reasons, the Court GRANTS in part and DENIES in part the plaintiffs' first motion for summary judgment. The Court GRANTS the following aspects of plaintiffs' first motion for summary judgment: (i) liability for Hill Rom's failure to pay for shipped but accepted controllers in Count I of the amended complaint; (ii) dismissal of all counterclaims based on Mextel's alleged breach of ¶ 2.1(b) of the Agreement; and (iii) dismissal of damages requested in ¶ 40(a) in Hill Rom's breach of contract counterclaim. All other aspects of defendants' summary judgment motion are DENIED.

For the preceding reasons, the Court GRANTS in part and DENIES in part Hill Rom's summary judgment motion. The Court GRANTS the following aspects of Hill Rom's summary judgment motion: (i) dismissal of Counts IV-IX of the amended complaint; (ii) dismissal of plaintiffs' breach of contract claims for the recovery of damages both from ordered, but unshipped controllers and from unordered controllers; and (iii) liability for all counterclaims based on plaintiffs' breaches of ¶ 6.1(b) and ¶ 8.2 of the Agreement. All other aspects of Hill Rom's summary judgment motion are DENIED.

For the preceding reasons, the Court DISMISSES plaintiffs' second motion for summary judgment as moot.

An appropriate ORDER follows.

ORDER

AND NOW, this ____ day of January 2005, upon consideration of Plaintiffs' Motion for Partial Summary Judgment In Favor of Plaintiffs' Contract Claims and Dismissal of Defendants' Contract Counterclaims (Doc. No. 64), filed on April 14, 2004, and all responses and supplemental briefs thereto; Plaintiffs' Second Motion for Partial Summary Judgment With Respect to the Dismissal of Patent Defenses and Counterclaims (Doc. No. 66), filed on April 14, 2004, and all responses and supplemental briefs thereto; and Defendants' Motion for Summary Judgment on Plaintiffs' Amended Complaint and Count IX of Defendants' Counterclaim (Doc. No. 74), filed on April 14, 2004, and all responses and supplemental briefs thereto, it is hereby ORDERED as follows:

1. Plaintiffs' First Motion For Summary Judgment (Doc. No. 64) is GRANTED in part and DENIED in part according to the following formula:

a. Plaintiffs are entitled to summary judgment on Count I of the amended complaint with respect to Defendants' liability for failure to pay for shipped and accepted controllers;

b. Plaintiffs are entitled to summary judgment on Defendants' breach of contract counterclaim with respect to Plaintiffs' liability for allegedly breaching ¶ 2.1(b) of the Agreement;

c. Plaintiffs are entitled to summary judgment on damages requested pursuant to ¶ 40(a) in Defendants' breach of contract counterclaim.

d. Plaintiffs' first motion for summary judgment motion is denied in all other respects.

2. Plaintiffs' Second Motion For Summary Judgment (Doc. No. 66) is DISMISSED as moot.

3. Defendants' Motion For Summary Judgment (Doc. No. 74) is GRANTED in part and DENIED in part according to the following formula:

***47** a. Defendants are entitled to summary judgment on Count I of the amended complaint with respect to Defendants' liability both for ordered, but unshipped controllers and for unordered controllers;

b. Defendants are entitled to summary judgment as to Counts IV-IX of the amended complaint;

c. Defendants are entitled to summary judgment on their breach of contract counterclaim with respect to Plaintiffs' liability for breaching ¶ 6.1(b) and ¶ 8.2 of the Agreement; and

d. Defendants' summary judgment motion is denied in all other respects.

4. The Affidavit of Susan Reilly is stricken pursuant to Federal Rule of Civil Procedure 56.

E.D.Pa.,2005.
Mextel, Inc. v. Air-Shields, Inc.
Not Reported in F.Supp.2d, 2005 WL 226112 (E.D.Pa.), 56 UCC Rep.Serv.2d 6

END OF DOCUMENT

TAB 11

Only the Westlaw citation is currently available.

UNPUBLISHED OPINION. CHECK COURT RULES BEFORE CITING.

Superior Court of Delaware.
SAVOR, INC., a Michigan corporation, Plaintiff,
v.
FMR CORP., a Massachusetts corporation and Upromise, Inc., a Delaware corporation, Defendants.
No. Civ.A. 00C-10-149JRS.

Submitted June 29, 2004.
Decided July 15, 2004.
Redacted Aug. 16, 2004.

Upon Defendants' Motions for Summary Judgment. Granted.
William M. Aukamp, Harvey Pennington, Ltd, Wilmington, Delaware, Howard M. Cyr, III, and Paul M. Quinones, Harvey Pennington, Ltd, Philadelphia, Pennsylvania, for Plaintiff, Savor, Inc.

Jeffrey L. Moyer, and Alyssa M. Schwartz, Richards, Layton & Finger, P.A., Wilmington, Delaware, John D. Donovan, Jr., and Emily C. Shanahan, Ropes & Gray, LLP, Boston, Massachusetts, for Defendant, FMR, Corp.

Anthony W. Clark, and James A. Whitney, Skadden, Arps, Slate, Meagher & Flom, LLP, Wilmington, Delaware, Irwin B. Schwartz, Petrie, Bauer, Schwartz, LLP, Boston, Massachusetts, for Defendant, Upromise, Inc.

MEMORANDUM OPINION

SLIGHTS, J.

I.

*1 In this misappropriation of trade secrets case, the Court must determine whether a reasonable jury could conclude: (1) that the plaintiff possessed a trade secret and, if so, (2) that the defendants misappropriated the secret. Although such fundamental inquiries are standard fare in the realm of motions for summary judgment, they are complicated in this case by the nature of the alleged trade secret-a purportedly "unique" compilation of publically available or arguably commonsense ideas-and also by the highly circumstantial nature of the evidence regarding the alleged illegal transmission of the trade secret-both the alleged transmitter and the alleged recipient of the trade secret deny knowing anything about it.

The plaintiff correctly observes that it may, as a matter of law, seek trade secret protection for a unique compilation of otherwise publicly known ideas or information. And it also correctly observes that it may, as a matter of law, prove misappropriation of the trade secret through circumstantial evidence, notwithstanding the defendant's denials of wrongdoing. The plaintiff's *allegation* of a "compilation" trade secret, and its *allegation* of a misappropriation of that secret, however, are not sufficient to overcome properly supported motions for summary judgment. When defendants support their motions for summary judgment with competent evidence indicating that the alleged trade secret was generally well known in the relevant industry and couple that showing with sworn, unrebutted denials of knowledge, much less misappropriation of plaintiff's particular idea, the plaintiff is obliged to answer with evidence in the record that, at least, creates a material issue of fact as to these fundamental elements of its claim. As discussed below, plaintiff has failed to carry this burden with respect to the misappropriation element of its *prima facie* claim for misappropriation of trade secrets. Consequently, the motions for summary judgment must be GRANTED.

II.

The age of this case is a reflection of its rather involved procedural history. Plaintiff, Savor, Inc. ("Savor"), initiated this action in October, 2000 against Fidelity Investment Corp. and defendant, Upromise, Inc. ("Upromise"). After determining that it had sued the wrong Fidelity entity, Savor amended its complaint and then amended it again to name the proper Fidelity entity, defendant, FMR Corp. ("FMR"), as the party to whom Savor initially communicated its alleged trade secret. Both defendants then moved to dismiss the second amended complaint on the ground, *inter alia,* that Savor had not adequately identified its alleged trade secret in the pleading. Savor acknowledged that its complaint did not identify its trade secret and offered to amend its complaint again, this time under seal, so that the trade secret could properly be disclosed. The Court dismissed the second amended complaint with leave to amend .[FN1]

FN1. *Savor, Inc. v. Upromise, Inc.,* 2001 WL 541484 (Del.Super.).

Savor's third amended complaint included an additional description of the alleged trade secret and attached a compilation of documents as "Exhibit A" in which it alleged that the trade secret was described in detail. The Court disagreed and dismissed the third amended complaint with prejudice.[FN2] Savor appealed and the Supreme Court of Delaware reversed this Court's order dismissing the case by opinion and order dated November 12, 2002.[FN3]

FN2. *Savor, Inc. v. Upromise, Inc.,* 2002 WL 393056 (Del.Super.).

FN3. *Savor, Inc. v. Upromise, Inc.,* 812 A.2d 894 (Del.2002).

*2 Approximately two months after the case was remanded to this Court, Upromise moved for dispositive relief again, this time recasting the arguments raised in its motions to dismiss against the backdrop of the more rigorous scrutiny contemplated by Del.Super. Ct. Civ. R. 56. The Court denied the motion for summary judgment as premature since the discovery contemplated by the Supreme Court had not yet been initiated in earnest.[FN4] Nevertheless, the Court appreciated that the issues that continued to surface in the defendants' dispositive motions-did Savor have a trade secret and was it misappropriated-would likely be raised again. Accordingly, recognizing that these were threshold issues, the Court bifurcated the litigation so that "phase 1" discovery would encompass only the alleged existence of the trade secret and the alleged misappropriation.[FN5]

FN4. *Savor, Inc. v. Upromise, Inc.,* 2003 WL 21054394 (Del.Super.).

FN5. *Id.*

During the course of phase 1 discovery, Savor propounded interrogatories and requests for documents that sought information regarding Upromise's trade secrets. Upromise sought protection from the Court. In keeping with well-settled case law that requires the plaintiff in a misappropriation of trade secrets case adequately to identify its own trade secret before seeking discovery of the defendant's trade secret,[FN6] the Court ordered Savor to prepare and file with the Court an Identification of Trade Secret ("ITS") in which it was to describe its trade secret in detail. By order dated January 20, 2004, the Court concluded that Savor's ITS identified its alleged trade secret with sufficient detail to justify its discovery of Upromise's trade secret information.[FN7] Contrary to Savor's characterizations in its brief on the motions *sub judice,* the Court did not conclude as a matter of fact or law that Savor had a trade secret worthy of legal protection. Indeed, the Court expressly stated: "whether [the Savor] program ... is entitled to trade secret protection [is an] issue[ ] for another day." [FN8] That day has come.

FN6. *See Englehard Corp. v. Savin Corp.,* 505 A.2d 30, 33 (Del.Ch.1986).

FN7. *See Savor, Inc. v. FMR Corp.,* C.A. No. 00C-10-249 JRS, Slights, J. (Del.Super.Jan. 20, 2004)(Letter Op.).

FN8. *Id.* at 3.

III.

A. The Development of the Savor Program

In 1994, Savor developed a program by which consumers could purchase goods or services from specified vendors and, in return, receive from the vendors rebates in various amounts depending on the nature of the goods or services acquired. The rebates, in turn, would automatically be applied by Savor to savings accounts for the benefit of the consumer and ultimately deposited into tax-deferred, state-sponsored college tuition savings accounts referred to as "529 accounts," named after the applicable provision of the Internal Revenue Code that recognized the tax deferred status of these funds.[FN9] Savor's program was the brainchild of its founder, Dennis A. Doyle, an entrepreneur whose experience was primarily in the development of marketing initiatives within the automotive and telecommunications industries.FN10 Prior to Savor, he had little to no experience in the financial services industry. FN11

FN9. *See* 26 U.S.C.A. § 529 (2001).

FN10. D.I. 180, Ex. 19, at U00416.

FN11. *Id.*

*3 At its inception, the Savor program focused primarily on providing a means for consumers to initiate or enhance retirement savings.FN12 Over time, Savor turned its [REDACTED]

FN12. D.I. 180, Ex. 2, at 24-25.

Although it is unclear in the record [REDACTED]

B. Savor Shares Its Idea With FMR

[REDACTED]

The State Treasurer of New Hampshire, a state targeted by Savor because of its successful state-sponsored college tuition savings program, suggested to Mr. Doyle that he contact a representative at FMR with whom the New Hampshire Treasurer's office had been working in the management of its program. Mr. Doyle made the initial contact with FMR's Abram Claude by telephone in early September, 1998. Mr. Claude was a Vice President for Business Development within FMR's college savings group.FN13 There is no dispute that Mr. Doyle contacted Mr. Claude in the hopes that FMR would serve as the exclusive fund manager for the Savor 529 accounts. Mr. Claude expressed interest in the Savor program and encouraged Mr. Doyle to send him some materials so that he could better understand the idea.FN14 Mr. Doyle requested a confidentiality agreement but Mr. Claude declined to give one. According to Mr. Doyle, Mr. Claude stated that a formal confidentiality agreement would simply delay the process. In its place, Mr. Claude allegedly made an oral commitment to Mr. Doyle to keep the information he received from Savor confidential. FN15

FN13. D.I. 180, Ex. 7, at 30.

FN14. D.I. 180, Ex. 2, at 181-84.

FN15. *Id.* at 194-95, 201-06. Mr. Claude does not recall that he made any such commitment to Mr. Doyle. D.I. 180, Ex. 7, at 71, 88-89. The Court's recitation of the facts casts the record in the light most favorable to Savor; it is not intended to represent the Court's findings of fact.

By letters dated September 15 and September 30, 1998, Mr. Doyle forwarded to Mr. Claude information which Savor contends comprised its trade secret. FN16 According to Mr. Doyle, he also had several telephone conversations with Mr. Claude during which he explained the Savor program to Mr. Claude in more detail.FN17 Mr. Claude acknowledged that upon receipt of Savor's information he treated it as confidential by keeping it locked in a file cabinet and by showing it only to the supervisor within his group to whom he presented Savor's idea.FN18

FN16. D.I. 180, Ex. 48, Savor 014-15, Savor 044-46.

FN17. D.I. 180, Ex. 2, at 209-10.

FN18. D.I. 180, Ex. 7, at 74-75, 97.

Significantly, Mr. Claude claims that he did not discuss the Savor program with his immediate supervisor, James Fadule, or with any of the other subordinate members of the college savings group. Instead, he presented the idea directly to the head of the group, Steve Mitchell.FN19 According to Mr. Claude, FMR's college savings group was in some turmoil at the time of the discussions with Savor because the group and its programs seemed to be attracting undesirable low balance accounts. Mr. Mitchell was assigned by FMR to the college savings group specifically to address this phenomenon. Accordingly, Mr. Claude thought it best to present the Savor idea directly to the man who would be most likely to have concerns about it.FN20 As Mr. Claude expected, Mr. Mitchell was not interested in Savor and directed Mr. Claude to communicate as much to Mr. Doyle. Mr. Claude complied.FN21 Despite Mr. Doyle's effort to address FMR's concerns, FMR held firm that it was not interested in pursuing a partnership with Savor.[FN22]

FN19. *Id.* at 97-104.

FN20. *Id.* For his part, Mr. Mitchell did not recall discussing the Savor program with Mr. Claude and had only recently heard of Savor at the time of his deposition. D.I. 180, Ex. 12, at 35-37. Each of Mr. Claude's colleagues within the college savings group, including Mr. Fadule, likewise denied knowing anything about the Savor program during the time Mr. Doyle and Mr. Claude were discussing the idea. D.I. 173, Ex. 6, at 98-99, 105-06; Ex. 7, at 47; Ex. 8, at 50; Ex. 9, at 26-27; Ex. 12, at 48.

FN21. D.I. 180, Ex. 7, at 102-103, 106-107.

FN22. *Id. See also* D.I. 180, Ex. 2, at 231-34.

C. The Development of the Upromise Program

*4 In 1999, Michael Bonner, an executive with a Boston-based marketing firm, developed a college savings program that would eventually become Upromise.[FN23] Like Mr. Doyle, Mr. Bonner had no experience with marketing or developing financial products prior to the creation of Upromise.[FN24]

FN23. D.I. 180, Ex.17, at 19-21, 40.

FN24. *Id.* at 20-21.

During 1999, Mr. Bonner began to assemble a management team and further refine his idea.[FN25] By February, 2000, Upromise had determined that it would focus its efforts on college savings through an affinity marketing program that would target vendors in designated industries to provide rebates to consumers for ultimate deposit into 529 accounts.[FN26] Upromise's July 13, 2000 Business Plan describes a web-based program whereby consumers would enroll in the Upromise plan, set up their Upromise account, and then purchase goods or services from Upromise's "commerce partners" by any means allowed by the vendor (not limited to credit card purchases) in exchange for cash rebates. [FN27] The rebate funds then would be deposited into a 529 account managed by any one of several "financial services partners" with whom Upromise had an arrangement.[FN28] Upromise would be paid a commission by commerce partners based on member spending, a sponsorship fee by commerce partners based on their level of participation in the Upromise program, an administrative service fee from financial service partners based on a predetermined percentage of assets under management, and a customer acquisition fee from selected commerce and financial service partners based on new customer acquisitions.[FN29] The Upromise plan was introduced to the public in April, 2001.[FN30]

FN25. D.I. 180, Ex. 18, at 15-18.

FN26. D.I. 180, Ex. 40, 41, 43.

FN27. DI 180, Ex. 35. The form in which the rebate would appear in the member's Upromise account, along with other components of the Upromise program, evolved as the idea itself evolved. The Upromise rebate began as a points system that would eventually be converted into cash, then a hybrid rebate system was contemplated, and then (and finally) a straight cash rebate system was adopted. D.I. 180, Ex. 17, at 56, 58-59, 77-78.

FN28. D.I. 180, Ex. 35.

FN29. *Id.*

FN30. D.I. 180, Ex. 11, Resp. No. 20.

D. The Alleged Misappropriation of the Savor Trade Secret by FMR and Upromise

James Fadule worked at FMR until October, 1998. At the time Savor was in discussions with FMR, Mr. Fadule was an executive in FMR's college savings group and a direct supervisor of Abram Claude. From October, 1998 through April, 2000, Mr. Fadule worked with Merrill Lynch. In April, 2000, Mr. Fadule joined Upromise as Vice President of Financial Services.[FN31] Although Mr. Bonner had already begun to focus Upromise on 529 college savings plans, Mr. Fadule's initial mission with Upromise was to assist in linking these plans with customer loyalty initiatives.[FN32]

FN31. D.I. 180, Ex. 10, at 125, 178.

FN32. *Id.* at 179.

While employed with Merrill Lynch, Mr. Fadule arranged a meeting with Mr. Claude (FMR) and other competitors in the 529 market to discuss regulatory compliance and other process issues.[FN33] It is possible that he spoke with Mr. Claude on other occasions as well during this time frame, including to discuss possible employment opportunities for Mr. Claude in the financial services industry.[FN34] When Mr. Fadule joined Upromise, he spoke with Mr. Claude about his new role there and described what Upromise was trying to do. [FN35] It was Mr. Fadule's hope that he could plant the seed for a future business relationship between Upromise and FMR.[FN36] This relationship would later come to fruition in the form of a Marketing and Service Agreement, although the principal architects of the deal were not Claude or Fadule. [FN37] Mr. Claude joined Fleet Boston in 2002 and was instrumental in bringing about an unspecified "business relationship" between Fleet Boston and Upromise later that year.[FN38]

FN33. *Id.* at 114-15.

FN34. *Id.* at 117; D.I. 180, Ex. 7, at 120-23, 127, 156.

FN35. D.I. 180, Ex. 10, at 161-63.

FN36. *Id.*

FN37. *Id. See also* D.I. 180, Ex. 11, Resp. No. 76, 78.

FN38. *Id.* Resp. No. 70. *See also* D.I. 180, Ex. 7, at 41.

***5** According to Savor, the details of its program were transmitted by Mr. Claude to Mr. Fadule. Mr. Fadule, in turn, misappropriated the trade secret for Upromise's benefit.[FN39] As discussed below, the details surrounding the alleged transmission of the secret are murky at best.

FN39. D.I. 179, at 27-28.

IV.

When considering a motion for summary judgment, the Court's function is to examine the record to determine whether genuine issues of fact exist.[FN40] A dispute about a material fact is genuine "if the evidence is such that a reasonable jury could return a verdict for the non-moving party." [FN41] It has been said, then, that "the availability of summary judgment turn[s] on whether a proper jury question ... [has been] presented." [FN42]

FN40. *Oliver B. Cannon & Sons, Inc. v. Dorr-Oliver, Inc.,* 312 A.2d 322, 325 (Del.Super.Ct.1973).

FN41. *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 248, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986).

FN42. *Id.* at 249.

In reviewing a motion for summary judgment, the Court's function "is not ... to weigh the evidence and [itself] determine the truth of the matter, but [rather] to determine whether there is a genuine issue for trial." [FN43] Since the grant of summary judgment will deny the non-moving party his day in court, the Court must view the record in a light most favorable to the party opposing the motion.[FN44] The moving party bears the initial burden of establishing the absence of any genuine issues of material fact.[FN45] If the moving party carries its initial burden, then the burden will shift to the non-moving party to demonstrate the existence of material issues of fact. [FN46] When the party opposing summary judgment is the party who will bear the burden of persuasion at trial, that party is obliged to point to facts in the record that will support its *prima facie* case at trial.[FN47]

FN43. *Id.*

FN44. *Id.*

FN45. *Moore v. Sizemore,* 405 A.2d 679, 680 (Del.1979).

FN46. *Id.* at 681.

FN47. *Celotex Corp. v. Catrett,* 477 U.S. 317, 322, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986).

"[A] complete failure of proof concerning an essential element ... necessarily renders all other facts immaterial." FN48 Even a "scintilla of evidence in support of the nonmovant's position will not defeat a motion for summary judgment." FN49 The record on summary judgment must contain "sufficient evidence favoring the nonmoving party for a jury to return a verdict for that party. If the evidence is merely colorable, or is not significantly probative, summary judgment may be granted." FN50

FN48. *Id.* at 323.

FN49. *Detrick v. Panalpina, Inc.,* 108 F.3d 529, 536 (4th Cir.), *aff'd sub nom, Gold v. Panalpina, Inc.,* 522 U.S. 810, 118 S.Ct. 52, 139 L.Ed.2d 17 (1997).

FN50. *Anderson,* 477 U.S. at 249-50.

The Court does not expect, nor does it require, that a party opposing summary judgment shall present its entire case to the court in every detail. But the law does require and, therefore, the court does expect that the nonmoving party will do more than simply rest on the allegations in the pleadings or new-found allegations that it raises in its summary judgment papers with hopes that evidence may surface at trial to support them.FN51 The time and place for coming forward with appropriately authenticated and admissible evidence to rebut a properly supported motion for summary judgment is in the papers and record submitted in opposition to the motion.FN52

FN51. *See Liboff v. Allen,* 1975 WL 1961, at *4 (Del.Ch.)("[I]t [is] incumbent on plaintiff to come forward with proof on which she relies to dispute the evidence on which defendants premise their motions. She is not entitled to await trial so as to see if she can find any.") (citation omitted); *Conaway v. Smith,* 853 F.2d 789, 793 (10th Cir.1988)("In a response to a motion for summary judgment, a party cannot rely on ignorance of facts, on speculation, or on suspicion, and may not escape summary judgment in the mere hope that something will turn up at trial."); Adv. Comm. Note to Proposed Amendments to Rule 56(e)("The very mission of the summary judgment procedure is to pierce the pleadings and to assess the proof in order to see whether there is a genuine issue for trial.").

FN52. *See Monsanto Co. v. Aetna Casualty and Surety Co.,* 1993 WL 563246, at *1 (Del.Super.)(emphasizing that "a party cannot oppose a motion for summary judgment on the basis of unauthenticated and inadmissible documents.") (citations omitted).

V.

The only claim still remaining in this case is misappropriation of trade secrets. The claim is governed by statute FN53 and implicates the following inquiries: "(1) Does a trade secret exist, *i.e.,* have the statutory elements-commercial utility arising from secrecy and reasonable steps to maintain secrecy-been shown; (2) has the secret been communicated by plaintiff to the defendant; (3) was such communication pursuant to an express or implied understanding that the secrecy of the matter would be respected; and (4) has the secret information been improperly (*e.g.,* in breach of the understanding) used or disclosed by the defendant to the injury of the plaintiff?" FN54 The Court will address the elements of the claim *seriatim.*

FN53. DEL.CODE ANN. tit. 6, § 2001 (1999) *et seq.* The parties have not specifically addressed the choice of law but appear to assume that Delaware's Uniform Trade Secret Act (the "Act") applies to this controversy. The only state with an arguably more significant relationship with this dispute is Massachusetts and it too has adopted the Uniform Trade Secrets Act. *See* MASS. GEN. LAWS ANN. ch. 93, § 1 (2004) *et seq. See also Travelers Indem. Co. v. Lake,* 594 A.2d 38, 47 (Del.1991)(adopting RESTATEMENT (SECOND) OF CONFLICTS OF LAWS, § 145's "most significant relationship" test); *Merck & Co. v. SmithKline Beecham Pharm. Co.,* 1999 WL 669354, *14-15 (Del.Ch.), *aff'd,* 766 A.2d 442 (Del.2000)(noting that both Delaware and Maryland bore an equally significant relationship to the controversy and that both states applied the Uniform Trade Secrets Act, the Court adopted the Act as the governing law and considered all decisions interpreting the Act to be persuasive authority); *Rohm & Haas Co. v. Adco Chem. Co.,* 689 F.2d 424, 429 (3d Cir.1992)(noting that when a "false conflict" exists, the court need not resolve the choice of law issue). The Court will apply the Act and cases interpreting the Act.

FN54. *Wilimington Trust Co. v. Consistent Asset Mgt. Co.,* 1987 WL 8459, at *3-4 (Del.Ch.).

A. Does a Trade Secret Exist?

***6** "Trade secret" is defined in the Act as: "Information, including a formula, pattern, *compilation,* program, device, method, technique or process that [d]erives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use and [i]s the subject of efforts that are reasonable under the circumstances to maintain its secrecy." FN55 "A party alleging misappropriation of a trade secret has the burden of proving the existence of the trade secret." FN56 And, at the summary judgment stage, the plaintiff must do more than allege it has a trade secret, it must describe its trade secret with a "reasonable degree of precision and specificity ... such that a reasonable jury could find that plaintiff established each statutory element of a trade secret." FN57

FN55. DEL.CODE ANN. tit. 6, § 2001(4) (1999)(emphasis supplied).

FN56. *Dionisi v. DeCampli,* 1995 WL 398536, at *11 (Del.Ch.). *See also* *ID Biomedical Corp. v. TM Technologies, Inc.,* 1995 WL 130743, at *14 (Del.Ch.)(same).

FN57. *IDX Systems Corp. v. Epic Systems, Corp.,* 165 F.Supp.2d 812, 816-17 (W.D.Wisc.2001). *See also* *Glynn Interactive, Inc. v. Itelehealth, Inc.,* 2004 WL 439236, at *5 (D.Md.)(plaintiff must describe trade secret with particularity); *AMP Inc. v. Fleischhacker,* 823 F.2d 1199, 1203 (7th Cir.1987)("courts have warned plaintiffs of the risks they run by failing to identify specific trade secrets and instead producing long lists of general areas of information which contain unidentified trade secrets.") (citation omitted); *Callaway Golf Co. v. Dunlop Slazenger Group Americas, Inc.,* 2004 WL 1124758, at *4 (D.Del.)("the plaintiff should describe the subject matter of the trade secret with sufficient particularity to separate it from matters of general knowledge in the trade or of special knowledge of those persons ... skilled in the trade.").

In this case, Savor has alleged that its trade secret is "a unique combination of unified characteristics, components, applications, compilations [sic] of business information, methods, techniques, processes, and operations of marketing, monitoring and administration of a college savings program." FN58 Savor acknowledges, albeit reluctantly, FN59 that its so-called "compilation" trade secret is comprised in large part of publicly available information and ideas but points the Court to the legion of cases that hold that a unique combination of public information and ideas can be worthy of trade secret protection. FN60 When the plaintiff claims a "compilation" trade secret, courts generally require that the trade secret be identified with even greater specificity. FN61

FN58. D.I. 180, Ex. 29, Resp. No. 1.

FN59. *See, e.g.,* D.I. 180, Ex. 2, at 27-29 (at first Mr. Doyle suggests that the idea for applying rebates to college savings was confidential and then, on further questioning, acknowledges that the idea was not confidential at the time it was communicated to FMR); *id.* at 99-100 (at first Mr. Doyle suggests that use of credit card to accomplish rebates for college savings was confidential, then he acknowledges that the idea was not confidential).

FN60. *See* *Merck & Co., Inc.,* 1999 WL 669354, at *15 ("A commercial production process consisting of a 'combination of the principles and details used to make a product' can be a trade secret, as can elements of the process ... [t]he combination of steps into a process is a trade secret, even if all the component steps are known, so long as it is a 'unique process which is not known in the industry." ') (citations omitted); Callaway Golf Co., 2004 WL 1124758, at *6 ("trade secret misappropriation can ... be based on a combination of otherwise public domain information."); Harbor Software, Inc. v. Applied Systems, Inc., 887 F.Supp. 86, 90 (S.D.N.Y.1995)("A trade secret can exist in a combination of characteristics and components, each of which, by itself, is in the public domain, but the unified process, design and operation of which in unique combination affords a competitive advantage and is a protectable trade secret.") (citations omitted).

FN61. *See, e.g.*, Struthers Scientific & International Corp. v. General Foods Corp., 51 F.R.D. 149, 153 (D.Del.1970)(requiring greater specificity in interrogatory answers regarding alleged trade secret comprised of a combination of elements.)

Defendants have contended throughout this litigation that the Savor program is nothing more than a business-school model for affinity marketing utilizing rebates to generate customer loyalty. They also contend that the idea of marrying affinity marketing with college savings and 529 plans cannot rise to the level of a trade secret because there was nothing secret about it as of the time Mr. Doyle disclosed the Savor program to Mr. Claude.FN62 Indeed, among the information supplied by Mr. Doyle to Mr. Claude was an article published in *American Banker,* a daily financial newspaper, that described the Savor concept of college savings through consumer rebates in significant detail.FN63 The article described the Savor credit card, the consumer rebates that would fund the state-sponsored college tuition savings plans, the marketing ideas promoting the plan (*e.g.*, "It's found money"), and the research supporting the need for the plan (*e.g.*, data on rising tuition costs) that make up a large part of Savor's alleged trade secret.FN64 This information clearly was in the public domain by the time Mr. Doyle first approached FMR with his idea.FN65

FN62. *See* CVD Inc. v. Raytheon Co., 769 F.2d 842, 850 (1st Cir.1985)("The cornerstone of a trade secret ... is secrecy.").

FN63. *See* D.I. 180, Ex. 48, at Savor 016-19.

FN64. *Compare id. with* D.I. 180, Ex. 29, Resp. No. 1 (Savor's description of its trade secret).

FN65. *See* CVD, Inc., 769 F.2d at 850 ("Once a trade secret enters the public domain, the possessor's exclusive rights to the secret are lost.").

But, according to Mr. Doyle, there was more to the Savor trade secret than was published in the *American Banker* article.

[REDACTED]

[REDACTED]

*7 Although the subject of some debate, it is generally recognized that "[t]he existence of a trade secret is a question of fact for determination by the jury." FN66 And, in this regard, the Court must recognize that it will often "lack[ ] the technical expertise to evaluate on its own whether the information plaintiff claims is secret is, in fact, not generally known in the industry." FN67

FN66. CALLMAN, UNFAIR COMPETITION, TRADEMARKS & MONOPOLIES § 53.3 at 390 (3d ed. Supp.1973). *See also* SmithKline Beecham Pharm. Co. v. Merck & Co., 766 A.2d 442, 448 (Del.2000)(same). *But see* FMC Corp. v. Spurlin, 596 F.Supp. 609, 613 (W.D.Pa.1984)("While the question of whether plaintiff possesses a trade secret is ultimately a question of law, there must be a factual predicate for resolving that question.") (citation omitted).

FN67. Harbor Software, Inc., 887 F.Supp. at 90.

In this case, Savor has managed through much of the litigation to skirt the question of whether it, in fact, possesses a trade secret by describing its alleged secret with elastic terms and phrases that track, in large part, the statutory definition of "trade secret" but do little meaningfully to explain how the Savor program works or how its combination of components is unique. FN68 Savor correctly notes that its interrogatory response did attempt to describe the trade secret with more detail than the incantation of statutory language that had been a feature of its prior disclosures. But even there Savor made no attempt to articulate why or in what manner the compilation of "ideas, methods, processes, techniques, etc." was secret.FN69

FN68. *See, e.g.,* D.I. 180, Ex. 30, at ¶ 6 (Savor's third amended complaint describes the trade secret as "marketing strategies, methods, techniques, and processes for extracting payments from program participants, aggregating the funds until they met minimum payment requirements under a State Qualified Tuition Plan, and then paying them over to the plan."); D.I. 180, Ex. 29, Resp. 1 (Savor's interrogatory response describes the trade secret as a "unique combination of unified characteristics, components, applications, compilations of business information, methods, techniques, processes, and operations of marketing, monitoring and administration of a college savings program."); D.I. 180, Ex. 26 (Savor's expert relies upon description of the trade secret set forth in Savor's interrogatory response and then continues to refer to the "unique marketing strategies, methods, techniques and processes" throughout the balance of the report).

FN69. D.I. 180, Ex. 29, Resp. 1. *See Struthers Scientific & Int'l Corp.,* 51 F.R.D. at 153 (to describe the trade secret adequately, plaintiff was ordered to disclose not only the "unique combination of components" it claimed constituted its trade secret, but also "how these components are combined, and how they operate in a unique combination.").

When read in a light most favorable to Savor, however, the Court is satisfied that the interrogatory response, coupled with Savor's ITS, verified by Mr. Doyle, and Mr. Doyle's deposition, provide enough information to allow a reasonable fact-finder to conclude that Savor's college savings program was a trade secret worthy of statutory protection. Clearly, neither the idea of linking college savings with an affinity marketing program nor the use of a credit card for doing so were secret. Nevertheless, a reasonable jury could conclude that the means by which the program would be implemented, [REDACTED] in the mind of a reasonable juror, be a trade secret, *i .e.,* the entire program could "[d]erive[ ] independent economic value, actual or potential, [for Savor] from not being generally known to, and not being readily ascertainable by proper means by, other persons who [might] obtain economic value from its disclosure or use." FN70

FN70. DEL.CODE ANN. tit. 6, § 2001(4) (1999). *See Nilssen v. Motorola, Inc.,* 963 F.Supp. 664 (N.D.Ill.1997).

The "trade secret" inquiry does not end here. The defendants have argued that Savor did not take reasonable steps to maintain the secrecy of the Savor program as required by statute.FN71 Specifically, they contend that Savor's failure to secure a confidentiality agreement from Mr. Claude (who refused to give one) prior to supplying its alleged secret to FMR is fatal to Savor's trade secret argument. Clearly, a plaintiff claiming a misappropriation of its trade secrets must establish that it took reasonable steps to protect the secrecy of its idea.FN72 The proof offered to satisfy this element of the claim, however, need not take the form of an express confidentiality agreement.FN73 "Rather, a duty of confidentiality may be implied from the circumstances surrounding the parties' relationship." FN74 And the duty of confidentiality is not destroyed merely because the holder "disclosed its trade secrets to 'a limited number of outsiders for a particular purpose....' " FN75 "On the contrary, such disclosure, which is often necessary to the efficient exploitation of a trade secret, imposes a duty of confidentiality on the part of the person to whom the disclosure is made." FN76 Whether the party in possession of the alleged trade secrets used reasonable efforts to maintain its secrecy is a question of fact.FN77

FN71. *Id.*

FN72. *See Merck & Co., Inc.,* 1999 WL 669354, at *19; *Rypac Packaging Machinery Inc. v. Coakley,* 2000 WL 567895, at *9 (Del.Ch.).

FN73. *See* Nilssen, 963 F.Supp. at 679 ("While an express confidentiality agreement may certainly suffice to define the duty of confidentiality necessary for action under [the Act], the existence of such an agreement is not a prerequisite to such an action.") (citation omitted).

FN74. *Id.* (citation omitted). *See also* Smith v. Dravo Corp., 203 F.2d 369, 376 (7th Cir.1953)(party may take reasonable efforts to maintain confidentiality of trade secret information without express confidentiality agreement.).

FN75. *Rockwell Graphic Systems, Inc. v. DEV Indus., Inc.*, 925 F.2d 174, 177 (7th Cir.1991).

FN76. *Id.*

FN77. *Id.* at 180.

***8** Here, defendants make much of the fact that Savor not only supplied its information to FMR with no written express agreement of confidentiality, it also supplied the same information to several other third parties, including vendors (such as Ford Motor Co.), and state treasurers' offices (such as New Hampshire's, Ohio's and Delaware's), also with no written commitment of confidentiality in hand. Mr. Doyle testified that he secured oral commitments from these third parties that the information would be kept confidential. [FN78] Such limited disclosures under these circumstances do not *ipso jure* destroy the trade secret status of the information.[FN79]

FN78. D.I. 180, Ex. 2, at 27. He also testified that he did not supply all of the details of the Savor program to these third parties. *Id.* at 44-45.

FN79. *See* *Rockwell Graphic Systems, Inc.*, 925 F.2d at 177.

Moreover, Mr. Doyle also testified that he extracted an oral commitment from Mr. Claude that FMR would keep the materials it received from Savor confidential.[FN80] Although Mr. Claude does not recall this discussion with Mr. Doyle,[FN81] whether it occurred and, if so, whether the oral commitment of confidentiality obtained by Savor was a "reasonable" measure to maintain the secrecy of the Savor program, would both be questions of fact for the jury to decide.

FN80. D.I. 180, Ex. 2, at 203-06.

FN81. D.I. 180, Ex. 7, at 71.

B. Was the Trade Secret Misappropriated?

"Unauthorized use of trade secret information and unauthorized disclosure of trade secret information constitutes misappropriation." [FN82] Misappropriation includes not only the wholesale pirating of an idea, but also the unauthorized utilization of an idea "as a starting point or guide in developing a process," or as a means "to understand 'what pitfalls to avoid." ' [FN83]

FN82. *Merck & Co.*, 1999 WL 669354, at *19 (citing DEL.CODE ANN. tit. 6, § 2001(2) (1999)). *See also* *Pulsecard, Inc. v. Discover Card Services, Inc.*, 1996 U.S. Dist. LEXIS 3660, at *30, 1996 WL 137824 (D.Kan.) ("Under the Act, misappropriation may occur under either of two general sets of circumstances: (1) improper acquisition, or (2) improper disclosure or use.").

FN83. *Merck & Co., supra,* at *20 (citations omitted). *See also* *Mangren Research & Dev. Corp. v. Nat'l Chemical Co., Inc.*, 87 F.3d 937, 944 (7th Cir.1996)("the user of another's trade secret is liable even if he uses it with modifications or improvements upon it effected by his own efforts, so long as the substance of the process used by the actor is derived from the other's secret.") (citation omitted). In this case, the defendants argue that because Savor has insisted that its trade secret is comprised of all of the elements of its Savor program, and that none of the elements can be separated from the whole, Savor must establish a misappropriation of the entire program to prevail. D.I.. 183, at 12 (citing *Vital State Canada, Ltd. v. Dreampak, LLC*, 303 F.Supp.2d 516, 529 (D.N.J.2003)(an "assertion that the trade secret is the combination of the elements is crucial ... since it means that to prove use of the trade secret, [plaintiff] must prove use of each and every element in combination."). Given the Court's conclusion that the undisputed evidence does not support a claim that the defendants misappropriated *any* element of the Savor program, the Court need not address this potential inconsistency in the case law.

Rarely will the plaintiff in a misappropriation of trade secrets case discover the "needle" in his opponent's "hay stack" of documents. Nor is it likely that plaintiff's counsel will enjoy the "Perry Mason moment" when the defendant's chief executive officer buckles under the weight of cross examination and admits that his company has misappropriated the plaintiff's trade secret. Consequently, it is now well-settled that the plaintiff may prove misappropriation of trade secrets with circumstantial evidence.FN84 Nevertheless, "[a]gainst this often delicate construct of circumstantial evidence there frequently must be balanced defendants and defendants' witnesses who directly deny everything." FN85

FN84. *See Merck & Co., supra,* at *20 (" 'Misappropriation of trade secrets may be proven by circumstantial evidence,' and more often than not, 'plaintiff must construct a web of perhaps ambiguous circumstantial evidence from which the trier of fact may draw inferences which convince him that it is more probable than not that what plaintiffs allege happen did in fact take place.") (citations omitted); *SI Handling Systems, Inc. v. Heisley,* 753 F.2d 1244, 1261 (3d Cir.1985)(same) (citation omitted); *Computer Sciences Corp. v. Computer Assoc. International, Inc.,* 1999 U.S. Dist. LEXIS 21803, 1999 WL 675446, (C.D.Cal)("a number of cases have 'rejected the notion that only a smoking gun will suffice to defeat a motion for summary judgment' in a trade secret action.") (citations omitted).

FN85. *SI Handling Systems, Inc.,* 753 F.2d at 1261 (citation omitted).

Savor acknowledges that it has no direct evidence that the defendants misappropriated its trade secrets. It seeks, therefore, to prevail on its claim of misappropriation by attacking the credibility of the defendants' witnesses, all of whom have flatly denied in sworn testimony that any misappropriation of Savor's trade secret has occurred here.FN86 Although Savor contends that there is ample fodder with which to attack the credibility of the defendants' sworn denials of misappropriation, this alone will not suffice to defeat a properly supported motion for summary judgment or to carry Savor's *prima facie* burden at trial.FN87 In the face of this realization, Savor has contended that it will prove with circumstantial evidence that the defendants had "motive and opportunity" to misappropriate its trade secret and that the Upromise program is sufficiently similar to the Savor program to give rise to an inference of misappropriation.

FN86. *See, e.g.,* D.I. 180, Ex.7, 10, 12, 17, 20, 49.

FN87. *See Vantage Point, Inc. v. Parker Brothers, Inc.,* 529 F.Supp. 1204, 1213-14 (E.D.N.Y.1981)("If the most that can be hoped for is the discrediting of the defendants' denials at trial, no question of material fact is presented.") (citations omitted); *Harbor Software, Inc. v. Applied Systems, Inc.,* 887 F.Supp. 86, 89 (S.D.N.Y.1995)("An issue of credibility is insufficient to preclude the granting of a motion for summary judgment.")(citing *Matsushita Elec. Indus., Inc. v. Zenith Radio Corp.,* 475 U.S. 574, 587, 106 S.Ct. 1348, 89 L.Ed.2d 538 (1986)).

***9** As discussed below, Savor's theory of misappropriation, like its trade secret argument, is elastic; the theory expands and contracts with each defense argument indicating that dispositive relief is appropriate. This time, however, even the deference to which Savor is entitled as the non-moving party cannot save its ill-conceived and unsupported theory of misappropriation. The undisputed evidence of record simply does not provide a reasonable basis upon which a jury could find for Savor on this fundamental element of its *prima facie* case.

The link between Savor and Upromise, at least for purposes of Savor's misappropriation claim, is FMR. Savor alleges that Mr. Doyle disclosed the trade secret to Mr. Claude while Mr. Claude was employed with FMR. Mr. Claude, in turn, disclosed the trade secret to Mr. Fadule. Savor's various arguments regarding the timing of this latter disclosure-Claude to Fadule-are perhaps the best illustrations of the moving target that is its misappropriation theory.

In its interrogatory responses, Savor argued that FMR could have disclosed Savor's trade secret to Upromise during the negotiation of what would eventually become the Marketing and Services Agreement.[FN88] The participants in the misappropriation are not specifically identified under this theory. Alternatively, Savor alleged that the disclosure could have occurred when Upromise hired one of several former employees of FMR.[FN89] Once again, the participants are not specifically identified. In its briefing on this motion, Savor suggested that it would prove circumstantially that Mr. Claude transmitted the secret to Mr. Fadule while both worked at FMR and that Mr. Fadule shared the secret with Upromise upon his employment there in April 2000.[FN90] At oral argument, when confronted with FMR's argument that it could not be held responsible for Mr. Fadule's conduct after he left FMR, counsel for Savor contended that the transmission between Claude and Fadule could have occurred after Fadule had joined Upromise and while Claude was still employed with FMR.[FN91] Under this theory, Claude, not Fadule, transmitted the secret to Upromise (through Fadule).

FN88. *See* D.I. 180, Ex. 4, Resp. 23.

FN89. *Id.*

FN90. D.I. 179, at 27.

FN91. Transcript of oral argument unavailable as of this writing.

In the absence of *any* evidence of disclosure-from Claude to Fadule, from Fadule to Upromise, or from FMR to Upromise-Savor is left to argue that transmission *must have occurred* because the relevant players had access to each other and because the Savor and Upromise programs are so similar. Clearly, the opportunity to acquire information is not the same as actually acquiring it. Savor cannot withstand the defendants' motions for summary judgment with a mere showing that the defendants had the opportunity to misappropriate.[FN92] It must couple this showing with a showing that the Upromise program "bears a substantial identity" with its own program.[FN93] Accordingly, a comparison of the two college savings programs, as they existed before and after Mr. Fadule's arrival at Upromise, must be undertaken in order to evaluate the viability of Savor's misappropriation claim.[FN94]

FN92. *See* SEC v. Truong, 98 F.Supp.2d 1086, 1101 (N.D.Cal.2000)("opportunity" to acquire knowledge insufficient to support inference of knowledge). *See also* Greenberg v. Cryodon Plastics Co. ., 378 F.Supp. 806, 812 (E.D.Pa.1974)(plaintiff does not prove misappropriation when evidence establishes that defendant could have developed similar method independently).

FN93. *See* Callaway Golf Co., 2004 WL 1124758, at *8 ("In order to prove that a defendant's use of a trade secret or confidential material constitutes misappropriation, the ... plaintiff must show 'that defendant's product bears a substantial identity with [its] secrets.").

FN94. According to Savor, Mr. Fadule either transmitted information to Upromise that he acquired from Mr. Claude while both were employed at FMR, or he received information from Mr. Claude after joining Upromise. Either way, Mr. Fadule is the ultimate transmitter of the information to Upromise and his arrival there in April 2000 marks time when the "opportunity" for misappropriation would begin.

***10** The Court begins its analysis by identifying those elements of the Upromise program that could not, as a matter of pure timing, be the product of misappropriation of Savor's program, *i.e.,* elements that existed long before Mr. Fadule or any other FMR employee arrived on the Upromise scene. First and foremost, the core concept animating both programs-marrying college savings with affinity marketing (rebates)-was part of the Upromise program from the time it first graced a drawing board in 1999.[FN95] The research suggesting the need for the program was also in Upromise's hands as of 1999.[FN96] The use of computers to support the program, the use of scholarships to promote the program, and the use of research to target the program all were part of the Upromise program in 1999.[FN97] The program was designed as a web-based service; the use of a credit card to facilitate the purchases and rebates apparently was not considered.FN98

FN95. D.I. 180, Ex. 45.

FN96. *Id.*

FN97. *Id.*

FN98. *Id.* Indeed, the Court has found no reference in the entire record that would suggest that Upromise ever seriously considered using a credit card as the means to facilitate its program.

[REDACTED]

It had also developed a critical component of the program-its name, "Upromise." FN99

FN99. *Id.*

[REDACTED]

Significantly, Savor contends that all of these prominent features of the Upromise program were also features of its program and were misappropriated by FMR and Upromise.FN100 Yet all of these components were developed by Upromise well before the time frame in which the transmission of the trade secret could have occurred. While there may be some similarities, no reasonable juror could conclude that the similarities are anything but coincidental. The undisputed evidence, viewed in a light most favorable to Savor, demonstrates that Upromise came up with these ideas on its own.

FN100. *See* D.I. 179 at 18-27.

The Court next considers the impact of the article published in *American Banker* describing the Savor program. As discussed above, many of the details of the Savor program were disclosed in that article, including: paying cash (as opposed to other currency) as rebates for purchases, using state-run college tuition savings plans as investment vehicles for the rebates, identifying State treasurers as partners for the program, describing the restricted access to the funds until it is time to pay for college, identifying the need for the program, and even identifying a marketing slogan ("It's found money"). FN101 Although the Court already has determined that the combination of these published components with others not published could qualify as a trade secret, the comparison of these published components of the Savor program with similar components of the later-developed Upromise program cannot, without more, give rise to a reasonable inference of misappropriation.FN102

FN101. D.I. 180, Ex. 48, at Savor 016-18.

FN102. *See* Callaway, 2004 WL 1124758, at *8 (highlighting similarities between the allegedly offending product and the plaintiff's product based on information "well known in the public domain" or "commonly known in the industry" will not provide a basis to defeat summary judgment). *See also Destination Marketing, Inc. v. Kessler Financial Services, L.P.,* 00-CV-11775-MEL, Lasker, J. (D.Mass. Nov. 2, 2001)(Mem. Op. at 7, 12-13)(granting Upromise's motion for summary judgment as to a misappropriation of trade secrets claim brought by another competitor, the Court noted that the information in the *American Banker* article was well-known among the general public and within the credit card and financial services industries at the time the Upromise program was conceived).

Savor also seeks to compare basic features of the two programs-features that are so fundamental to any modem business organization that to be without them would be more remarkable. For instance, Savor points to the fact that Upromise offers a "toll-free 800" customer service line for customer support.FN103 Not surprisingly, the Savor program would also provide similar customer support. Except perhaps for the corner lemonade stand, it is likely that every other customer-based business in this country offers direct-access customer support similar to Savor and Upromise. This is hardly a novel idea. Savor also identifies the fact that both its program and Upromise's program are supported by computer technology.FN104 Again, the corner lemonade stand comes to mind. It would be more appropriate to compare the specific aspects of the computer technology used to support the two programs. This comparison yields nothing for Savor; the two systems are vastly different.

FN103. D.I. 179, at 26.

FN104. *Id.* at 25.

*11 Finally, the Court must return to the fundamental differences between the Savor program and the Upromise program. These undisputed differences cannot be ignored and they are fatal to Savor's effort to attempt to prove misappropriation with circumstantial evidence.[FN105]

FN105. *See Destination Marketing, Inc., supra,* at 13-14 ("Upromise's business plan is so significantly different from Destination Marketing's business plan that no reasonable jury could conclude that Upromise misappropriated the Destination Marketing plan.").

[REDACTED]

Indeed, in all of the voluminous information the Court has reviewed regarding the Savor program, there does not appear to be any direct explanation of how Savor is to be paid.[FN106] As best as the Court can discern from Savor's ITS (a document not supplied to Claude or FMR) [REDACTED]

FN106. At oral argument, Plaintiff's counsel was unable to direct the Court to any portion of the information supplied to FMR that describes this aspect of the Savor program.

While both programs share the goal of marrying college savings with affinity marketing, the manner in which they accomplish that goal is fundamentally different.[FN107] These fundamental differences do not allow an inference of misappropriation.[FN108]

FN107. Interestingly, the program alleged to be unique and secret by the plaintiff in *Destination Marketing* as of December, 1998 (three months after the first disclosure of the Savor program to FMR) looks much more similar to the Savor program than the Upromise program has ever looked.

FN108. *See, e.g.,* Calloway Golf Co., 2004 WL 1124758, at *8-9 (granting summary judgment on a misappropriation claim on the ground, *inter alia,* that plaintiff could not prove up a viable circumstantial claim for misappropriation); *First Federal Savings Bank v. CPM Energy Systems Corp.,* 1993 WL 138986, at *9 (Del.Super.)(same); *Storage Technology Corp. v. Cisco Systems, Inc.,* 2003 WL 22231544, at *6, 9 (D.Minn.)(same); *Computer Sciences Corp., supra,* at *39 (same).

VI.

The Court has extended all due deference to Savor on summary judgment and has concluded, in this context, that it has a viable claim that its "Savor program" constitutes a "compilation" trade secret. The same cannot be said, however, for Savor's claim that defendants misappropriated this secret. Even when viewing the evidence in a light most favorable to Savor, it is clear that no reasonable jury could conclude that either FMR or Upromise misappropriated the Savor program. Indeed, no reasonable juror could conclude that Upromise was ever even made aware of the Savor program prior to the development of its own college savings program. Consequently, defendants' motions for summary judgment must be GRANTED.

IT IS SO ORDERED.

Del.Super.,2004.
Savor, Inc. v. FMR Corp.
Not Reported in A.2d, 2004 WL 1965869 (Del.Super.)

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TAB 12

28 S.W.3d 345, 16 IER Cases 1071
(Cite as: 28 S.W.3d 345)

Missouri Court of Appeals,
Eastern District,
Division Two.
SCHMERSAHL, TRELOAR & CO., P.C., Plaintiff/Appellant,
v.
Tim McHUGH, Defendant/Respondent.
No. ED 76363.

Aug. 1, 2000.
Motion for Rehearing and/or Transfer to Supreme Court Denied Sept. 7, 2000.
Application for Transfer Denied Oct. 31, 2000.

Employer, an accounting firm, filed suit against former at-will employee, seeking liquidated and actual damages for alleged breach of a non-solicitation agreement. The Circuit Court, City of St. Louis, Thad F. Niemira, J., entered judgment for employee. Employer appealed. The Court of Appeals, Crane, P.J., held as a matter of first impression that former employee's covenant not to solicit or encourage other employees to terminate their employment was a restrictive covenant in restraint of trade, and thus was unenforceable.

Affirmed.

West Headnotes

[1] Contracts 95 ⚷116(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases

Contracts 95 ⚷118

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k118 k. Preventing Disclosure of Trade Secrets. Most Cited Cases
Former at-will employee's covenant not to solicit or encourage his former co-workers to terminate their employment was a restrictive covenant in restraint of trade that did not protect trade secrets or customer contacts, and thus was unenforceable.

[2] Contracts 95 ⚷116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases
A promise is in restraint of trade if its performance would limit competition in any business or restrict the promisor in the exercise of a gainful occupation. Restatement (Second) of Contracts § 186(2).

[3] Contracts 95 ⚷116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases
Every promise that relates to a business dealing or to a professional or other gainful occupation operates as a restraint in the sense that it restricts the promisor's future activity. Restatement (Second) of Contracts § 186 comment.

[4] Contracts 95 ⚷116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases

Restrictive covenants limiting individuals in the exercise or pursuit of their occupations are in restraint of trade.

[5] Contracts 95 116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases

Post-employment restrictions are generally considered restraints of trade.

[6] Contracts 95 116(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases

Contracts 95 118

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k118 k. Preventing Disclosure of Trade Secrets. Most Cited Cases

A restrictive covenant in an employment agreement is only valid and enforceable if it is necessary to protect one of two well-defined interests, trade secrets and customer contacts, and if it is reasonable as to time and place.

[7] Labor and Employment 231H 305

231H Labor and Employment
231HV Intellectual Property Rights and Duties
231Hk304 Trade Secrets or Confidential Information
231Hk305 k. In General. Most Cited Cases
(Formerly 255k60 Master and Servant)

Labor and Employment 231H 307(3)

231H Labor and Employment
231HV Intellectual Property Rights and Duties
231Hk304 Trade Secrets or Confidential Information
231Hk307 Particular Trade Secrets or Information Protected
231Hk307(3) k. Customer Information. Most Cited Cases
(Formerly 255k60 Master and Servant)

An employer may only fairly require the protection of certain narrowly defined and well recognized interests against possible appropriation by a former employee; these protectable interests are limited to trade secrets and customer contacts, the latter being essentially the influence an employee acquires over his employer's customers through personal contact.

[8] Contracts 95 116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases

The purpose of the restrictive covenant is to protect an employer from unfair competition.

[9] Contracts 95 116(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases
With respect to its employees, an employer has a proprietary right in its stock of customers and their goodwill which can be protected in a reasonable covenant not to compete.

[10] Contracts 95 ⚷116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases

Labor and Employment 231H ⚷122

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk120 Post-Employment Duties
231Hk122 k. Duty Not to Solicit Customers. Most Cited Cases
(Formerly 255k50 Master and Servant)
The employee owes his relationship with the client to the employer, and he holds the relationship in a kind of fiduciary capacity for the employer, and thus, it is perfectly fair, for a limited time after the termination of the employment, to prohibit his using that relationship for his own benefit and for the benefit of a competitor of the employer, to the employer's detriment.

[11] Contracts 95 ⚷118

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k118 k. Preventing Disclosure of Trade Secrets. Most Cited Cases
An employer's trade secrets are proprietary and can be protected in a reasonable covenant not to compete where they have been disclosed to the employee in confidence under circumstances giving rise to a fiduciary relationship.

[12] Labor and Employment 231H ⚷70

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk70 k. In General. Most Cited Cases
(Formerly 255k60 Master and Servant)
An employer does not have a proprietary interest in its employees at will or in their skills.

[13] Contracts 95 ⚷116(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases
The normal skills of a trade are not included in an employer's protectable interest; thus, the basic skill of a craftsman will not support a restrictive covenant.

[14] Labor and Employment 231H ⚷121

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk120 Post-Employment Duties
231Hk121 k. In General. Most Cited Cases
(Formerly 255k60 Master and Servant)
An employer cannot prevent or inhibit its former employees from using the normal skills of their trade. Restatement (Second) of Contracts § 188 comment.

[15] Labor and Employment 231H ⚷306

231H Labor and Employment
231HV Intellectual Property Rights and Duties

231Hk304 Trade Secrets or Confidential Information
231Hk306 k. What Are Trade Secrets or Confidential Information of Employer. Most Cited Cases
(Formerly 255k60 Master and Servant)
The fact of an employer-employee relationship, standing alone, is not sufficient to cause a confidential relationship to exist as to knowledge which is the natural product of the employment.

[16] Labor and Employment 231H ⚷121

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk120 Post-Employment Duties
231Hk121 k. In General. Most Cited Cases
(Formerly 255k60 Master and Servant)

Labor and Employment 231H ⚷123

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk120 Post-Employment Duties
231Hk123 k. Duty Not to Compete in General. Most Cited Cases
(Formerly 255k60 Master and Servant)
An employee after leaving the service of an employer may carry on the same business on his own and use for his own benefits the things he had learned while in the earlier employment.

[17] Labor and Employment 231H ⚷121

231H Labor and Employment
231HIII Rights and Duties of Employers and Employees in General
231Hk120 Post-Employment Duties
231Hk121 k. In General. Most Cited Cases
(Formerly 255k60 Master and Servant)
Necessarily a former employee may use what he learned in the former employer's business while engaged in business for himself or some business competing with the former employer.

[18] Labor and Employment 231H ⚷908

231H Labor and Employment
231HIX Interference with the Employment Relationship
231Hk907 Enticing Employee to Leave Employment
231Hk908 k. In General. Most Cited Cases
(Formerly 255k339 Master and Servant)
Soliciting another's at-will employees does not constitute unfair competition; there is no wrong in making an offer of employment to an at-will employee, even though the employee and his new employer may compete with the former employer.

[19] Labor and Employment 231H ⚷908

231H Labor and Employment
231HIX Interference with the Employment Relationship
231Hk907 Enticing Employee to Leave Employment
231Hk908 k. In General. Most Cited Cases
(Formerly 255k339 Master and Servant)
The conduct of soliciting another's at-will employee only becomes culpable where it is done for a wrongful purpose, such as to destroy another's business, to misappropriate the employer's trade secrets, or to induce breach of a covenant not to compete.

[20] Contracts 95 ⚷116(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases

Contracts 95 ⚷118

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k118 k. Preventing Disclosure of Trade Secrets. Most Cited Cases
The employer can protect itself against competition

from its remaining employees by entering into restrictive agreements with those employees to prohibit the solicitation of clients or the disclosure of trade secrets.

[21] Contracts 95 ⚷116(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases

An employer's interest in protecting the stability of its at-will workforce is not one of the interests which may be protected by a restrictive covenant in Missouri.

*347 Charles S. Kramer, Michael A. Ellenhorn, Riezman Berger, P.C., St. Louis, for appellant.

Stuart R. Berkowitz, Platke and Berkowitz, L.L.P., St. Louis, for respondent.

KATHIANNE KNAUP CRANE, Presiding Judge.

This case involves an attempt by an employer to recover liquidated and actual damages against its former employee for breach of a covenant not to "solicit, persuade, induce or encourage" employer's employees to terminate their employment for a period of three years after the former employee's termination. Twenty-one months after leaving employer, the former employee told one of employer's employees about a job opportunity, but that employee remained with employer with no change in compensation. Following a bench trial, the trial court found the covenant and liquidated damages clause were not enforceable and entered judgment in the former employee's favor. On appeal employer argues that the covenant and liquidated damages clause are enforceable contract provisions. We affirm for the reason that the covenant restrains trade and does not fall within the class of restrictive covenants which may be enforced in Missouri because it is not directed to the protection of trade secrets or customer contacts.

Plaintiff, Schmersahl, Treloar & Co., P.C., an accounting firm, required all of its employees, both professional and clerical, to sign a Confidentiality and Non-Solicitation Agreement which contained a non-solicitation covenant that prohibited plaintiff's employees, first, from soliciting business from its clients and, second, from soliciting or encouraging its employees to terminate their employment:

> 2. *Non-Solicitation Covenant.* In consideration of Employee's employment and/or continued employment, Employee agrees that during the term of the employment and for a period of three (3) years following termination of employment (regardless of which party terminates the employment), Employee will not, directly or indirectly, as an employee, employer, consultant, agent, sole proprietor, principal, associate, partner, stockholder, corporate officer, director, or in any other individual or representative capacity:
>
> a). Solicit, service, refer, attempt to divert, take away, or accept business from, any clients of S & A for any purpose that is in anyway competitive with S & A, or supply any information to any other person, firm, or corporation for such purpose; or
>
> b). Solicit, persuade, induce, or encourage any other employees or agents of S & A to terminate employment with the Company.

The agreement provided for stipulated damages "for violations of paragraph 2(b) above, 30% of the gross salary of each person that the Employee solicits, persuades, induces or encourages to terminate employment with S & A in violation of paragraph 2(b) at the time of said solicitation." All of plaintiff's employees were employees at will.

Defendant, Tim McHugh, an accountant hired by plaintiff in 1994, signed this agreement on April 18, 1996. Defendant left plaintiff to take a position with a different accounting firm in December, 1996. Approximately one year and nine months later, defendant contacted plaintiff's employee, Mark Graves, with whom defendant had previously worked, and had lunch with him. During the lunch defendant indicated that his current employer, Lopata Flegel, was looking for an accountant with Graves's type of experience and that it would be a good opportunity for him.

Graves approached his supervisor and told him that he had talked to defendant about an opportunity at Lopata Flegel. Graves indicated that he planned to stay with plaintiff, but did not ask for a raise. Plaintiff did not give Graves a raise or promise Graves any additional compensation***348** for staying in plaintiff's employ. Lopata Flegel never made a job offer to Graves.

Plaintiff subsequently filed a lawsuit against defendant seeking liquidated and actual damages for breach of the non-solicitation agreement. At trial James Schmersahl, plaintiff's president, testified that the covenant was to keep former employees, who had developed a bond with co-workers as a result of plaintiff's efforts to create camaraderie among employees, from using that relationship to entice the former co-workers to either leave plaintiff's employ or to question whether plaintiff was compensating them sufficiently. He opined that plaintiff would give Graves bigger raises in the future because of Graves's knowledge of the market for his services as a result of the solicitation, but admitted that, as of the time of trial, plaintiff had not given Graves any additional compensation.

The trial court entered judgment for the defendant on the grounds that the covenant sought to be enforced was a restrictive covenant which was broader than was needed to protect client needs and identities and extended to interests which were not properly the subject of a covenant not to compete. It further held that the liquidated damage clause was not a reasonable forecast of the harm caused by the breach but purported to award damages even in situations in which the employer was not entitled to damages and was in the nature of a penalty.

[1] In its four points on appeal, plaintiff contends that the trial court misapplied and misdeclared the law in entering judgment against it. It first argues that its non-solicitation of employees clause is not a restrictive covenant. It next argues that, even if it is a restrictive covenant, it should be upheld because it protects a legitimate business interest, it was reasonable as to time, and the damages were a reasonable forecast of the harm caused by the breach.

DISCUSSION

I. *Enforceability of the Non-Solicitation of Employees Clause*

A. *Is the Non-Solicitation Clause a Restrictive Covenant?*

The threshold question is whether a former employee's covenant not to solicit or encourage other employees to terminate their employment is a restrictive covenant. No Missouri court has determined this issue. In *Universal Underwriters Ins. Co. v. Lyon*, 896 S.W.2d 762 (Mo.App.1995), the contract contained a covenant by which an ex-employee agreed not to "employ" any other employee of employer for two years after termination. The court affirmed the judgment in defendant's favor on the grounds that there was no evidence that the ex-employee had "employed" one of employer's employees and did not reach the question of whether the employer had a protectable interest in its workforce. *Id.* at 764.

[2][3][4][5] Because Missouri courts have not addressed this issue, we must look at the underlying principles governing agreements which restrain trade to determine if this kind of non-solicitation agreement falls thereunder. Contracts in restraint of trade are unlawful in Missouri. Section 416.031 RSMo (1994). "A promise is in restraint of trade if its performance would limit competition in any business or restrict the promisor in the exercise of a gainful occupation." RESTATEMENT (SECOND) OF CONTRACTS Section 186(2) (1981). "Every promise that relates to a business dealing or to a professional or other gainful occupation operates as a restraint in the sense that it restricts the promisor's future activity." *Id.*, cmt. a. Restrictive covenants limiting individuals in the exercise or pursuit of their occupations are in restraint of trade. *Sturgis Equip. Co., Inc. v. Falcon Indus. Sales Co.*, 930 S.W.2d 14, 16 (Mo.App.1996). Post-employment restrictions are generally considered restraints of trade. ***349***House of Tools & Engineering, Inc. v. Price*, 504 S.W.2d 157, 159 (Mo.App.1973).

Competition in the marketplace encompasses competition in the labor market, including an employer's ability to solicit and hire the at-will employees of another and an at-will employee's ability to seek employment at better terms. The policy in favor of free competition allows an employer to make an offer of employment to a competitor's at-will employee and allows an at-will employee to leave employment and compete with a former employer. Dwyer, Costello and Knox, P.C. v. Diak, 846 S.W.2d 742, 747 (Mo.App.1993). In Triangle Film Corp. v. Artcraft Pictures Corp., 250 F. 981 (2d Cir.1918), Judge Learned Hand wrote that it was universally accepted that, absent some monopolistic purpose, everyone has the right to offer better terms to another's employee, as long as the latter is free to leave. *Id.* at 982. He concluded that a contrary result would be "intolerable" both to other employers who could use the employee more effectively and to the employees who might receive added pay. *Id.* To hold otherwise would "put an end to any kind of competition." *Id.* The argument "[t]hat nobody in his own business may offer better terms to an employe[e], himself free to leave, is so extraordinary a doctrine, that we do not feel called upon to consider it at large." *Id.* at 983.

Having considered these principles, we conclude that this covenant is in restraint of trade. It can be used to restrict the employee's post-employment ability to solicit employees for himself, his new employer, or anyone else. It restricts the flow of competitive information about the labor market, including the availability of opportunities and offers of employment to an employer's at-will workforce. It thus has the effect of reducing competition in the labor market.

B. *Does It Protect Trade Secrets or Customer Contacts?*

[6] A restrictive covenant in an employment agreement is only valid and enforceable if it is necessary to protect one of two well-defined interests, trade secrets and customer contacts, and if it is reasonable as to time and place. Easy Returns Midwest, Inc. v. Schultz, 964 S.W.2d 450, 453 (Mo.App.1998). Plaintiff challenges the trial court's finding that the non-solicitation agreement was unenforceable because it did not seek to protect trade secrets or customer contacts. We agree with the trial court.

[7] "[A]n employer may only 'fairly require' the protection of certain narrowly defined and well recognized interests against possible appropriation by a former employee. These protectable interests are limited to trade secrets and customer contacts, the latter being essentially the influence an employee acquires over his employer's customers through personal contact." Continental Research Corp. v. Scholz, 595 S.W.2d 396, 400 (Mo.App.1980).

In Renwood Food Products v. Schaefer, 240 Mo.App. 939, 223 S.W.2d 144 (1949), the court adopted the rationale for this rule from an English case:

> Lord Atkinson, in Herbert Morris, Ltd. v. Saxelby, [1916, 1 A.C. 688] 702, summarized the modern rule as follows: 'He (employer) is undoubtedly entitled to have his interest in his trade secrets protected, such as secret processes of manufacture which may be of vast value. And that protection may be secured by restraining the employee from divulging these secrets or putting them to his own use. He is also entitled not to have his old customers by solicitation or such other means enticed away from him. But freedom from all competition per se apart from both these things, however lucrative it might be to him, he is not to be protected against. He must be prepared to encounter that even at the hands of a former employee.'

Id. at 151.

Missouri courts continue to follow *Renwood* and *Continental Research* and limit ***350** the interests which may be protected by a restrictive covenant to trade secrets and customer contacts. *See* Osage Glass, Inc. v. Donovan, 693 S.W.2d 71, 73-75 (Mo. banc 1985); Easy Returns, 964 S.W.2d at 453; West Group Broadcasting, Ltd. v. Bell, 942 S.W.2d 934, 937 (Mo.App.1997).

On its face this covenant does not protect trade secrets or customer contacts. Plaintiff seeks to extend an employer's protectable interests to its interest in maintaining a stable workforce. It argues that it is necessary to protect the employer from the use of the employee's "influence" with former co-workers to unfairly compete with the employer. We disagree. The rationale for protecting trade secrets and customer contacts does not extend to protecting an employer's interest in keeping at-will employees from leaving their employment.

[8][9][10][11] The purpose of the restrictive covenant is to protect an employer from unfair competition. Continental Research, 595 S.W.2d at 400. With respect to its employees, an employer has a proprietary right in its stock of customers and their goodwill which can be protected in a reasonable covenant not

to compete. *Schott v. Beussink*, 950 S.W.2d 621, 625 (Mo.App.1997).

> The employee's relationship with the client he owes to the employer, and he holds it in a kind of fiduciary capacity for the employer. *Mills v. Murray*, 472 S.W.2d 6, 12 (Mo.App.1971). It is perfectly fair, for a limited time after the termination of the employment, to prohibit his using that relationship for his own benefit, and for the benefit of a competitor of the employer, to the employer's detriment.

Property Tax Representatives, Inc. v. Chatam, 891 S.W.2d 153, 158 (Mo.App.1995). Further, an employer's trade secrets are likewise proprietary and can be protected where they have been disclosed to the employee in confidence under circumstances giving rise to a fiduciary relationship. *National Rejectors, Inc. v. Trieman*, 409 S.W.2d 1, 35-36 (Mo. banc 1966); *Pony Computer, Inc. v. Equus Computer Systems of Missouri, Inc.*, 162 F.3d 991, 997-98 (8 th Cir.1998) (applying Missouri Law). Because an employer's interests in customer contacts and trade secrets are proprietary, the courts will, in appropriate circumstances, protect them against unfair competition.

[12][13][14][15][16][17] However, an employer does not have a proprietary interest in its employees at will or in their skills. In *Triangle Film* the court rejected the argument that an employer's reasonable expectation that his employees at will will stay with him is part of "goodwill" and is protectable. 250 F. at 982. The normal skills of a trade are not included in an employer's protectable interest. Thus, the basic skill of a craftsman will not support a restrictive covenant. *Osage Glass*, 693 S.W.2d at 74. An employer cannot prevent or inhibit its former employees from using the normal skills of their trade. RESTATEMENT (SECOND) OF CONTRACTS Section 188, cmt. b. The fact of an employer-employee relationship, standing alone, is not sufficient to cause a confidential relationship to exist as to knowledge which is the natural product of the employment. *National Rejectors*, 409 S.W.2d at 35. It is a well-established principle that:

> "[A]n employee after leaving the service of an employer may carry on the same business on his own and use for his own benefits the things he had learned while in the earlier employment. If this were not so an apprentice who has worked up through the stages of journeyman and master workman could never become an entrepreneur on his own behalf. Any such system of quasi-serfdom has long since passed away. Necessarily the former employee may use what he learned in the former employer's business while engaged in business for himself or some business competing with the former employer."

***351** *Id.* at 41 (quoting *Midland-Ross Corp. v. Yokana*, 293 F.2d 411, 412-13 (3 rd Cir.1961)).

[18] Further, soliciting another's at-will employees does not constitute unfair competition. There is no wrong in making an offer of employment to an at-will employee, even though the employee and his new employer may compete with the former employer. *Dwyer*, 846 S.W.2d at 747. The law's policy favors free competition when no agreement provides otherwise. *Id.* at 747-48.

> The employees of the firm, whether CPAs or not, were as free as the defendant to leave the plaintiff corporation's employ and to enter into competition. They could do so in association with the defendant, and the defendant could advise them of his decision to leave the plaintiff. If the plaintiff sensed the need to protect itself against competition from its accounting employees, it could have sought covenants restricting their competition, for which it would presumably have to offer some consideration.

Id. at 748.

[19] The conduct only becomes culpable where it is done for a wrongful purpose, such as to destroy another's business, to misappropriate the employer's trade secrets, *National Rejectors*, 409 S.W.2d at 34, to induce breach of a covenant not to compete, *Mills v. Murray*, 472 S.W.2d 6, 13 (Mo.App.1971). *See* RESTATEMENT (SECOND) OF TORTS, Section 768(1) (1979).

[20][21] The employer can protect itself against competition from its remaining employees by entering into restrictive agreements with those employees to prohibit the solicitation of clients or the disclosure of trade secrets. *Dwyer*, 846 S.W.2d at 748. How-

TAB 13

H Only the Westlaw citation is currently available.

United States District Court,
W.D. Washington.
STONCOR GROUP, INC., Plaintiff,
v.
Christopher CAMPTON, et al., Defendants.
No. C05-1225JLR.

Feb. 7, 2006.

Medora A. Marisseau, Shawn M. Yates, Brian K. Keeley, Pamela Salgado, Bullivant Houser Bailey, Seattle, WA, William G. Wright, Farr Burke Gambacorta & Wright, Bellmawr, NJ, for Plaintiff.

Boris Gaviria, Rhys M. Farren, Rhys M Farren, Davis Wright Tremaine, Bellevue, WA, for Defendants.

ORDER

ROBART, J.

I. INTRODUCTION

*1 This matter comes before the court on Defendants' motion for a judgment on the pleadings (Dkt.# 98) and Defendants' second (Dkt.# 100) and third (Dkt. # 104) motions to compel discovery.[FN1] Having read the papers filed in support and in opposition, the court GRANTS in part and DENIES in part Defendants' second motion to compel, DEFERS consideration of Defendants' third motion to compel, and DENIES Defendants' motion to dismiss for the following reasons.

FN1. In the future, the court requests that the parties take note of the following alteration to the Electronic Filing Procedures for all cases before Judge Robart: when the aggregate submittal to the court (i.e., the motion, any declarations and exhibits, the proposed order, and the certificate of service) exceeds 50 pages in length, a paper copy of the documents (with tabs or other organizing aids as necessary) shall be delivered to the Clerk's Office for chambers, in addition to electronically filing the document. The paper copy must be clearly marked with the words "Courtesy Copy of Electronic Filing for Chambers."

II. BACKGROUND & ANALYSIS

Plaintiff StonCor Group, Inc. (a/k/a "Stonhard") [FN2] filed suit against Christopher Campton and his new employer, Hi-Tech Interiors, Inc. ("Hi-Tech"). Both Stonhard and Hi-Tech engage in the business of polymer floor installation. Mr. Campton left Stonhard to work for Hi-Tech in April of 2005. Stonhard alleges, among other claims, that Defendants misappropriated trade secrets and that Mr. Campton breached his employment contract's non-compete provision.

FN2. Although StonCor Group, Inc. filed this suit, Plaintiff's claims relate to its Stonhard division.

The parties began discovery in July of 2005 on an expedited basis and the court recently extended the cut-off date to February 17, 2006 (Dkt.# 121). Defendants now move this court to compel Stonhard to respond to various discovery requests, most of which relate to Stonhard's alleged trade secrets. In the alternative, Defendants move to dismiss Stonhard's trade secrets claim under Fed.R.Civ.P. 12(c) ("Rule 12(c)").

A. Defendants' Second Motion to Compel

In their second motion to compel, Defendants have organized Stonhard's alleged deficient responses by topic and corresponding interrogatory ("ROG") or request for production ("RFP") number, as directed in the court's prior minute order (Dkt. # 94 at 2). The court takes each alleged deficiency in turn, but addresses only those interrogatories or RFPs actually briefed by Defendants.

1. Trade Secrets

Defendants served Stonhard with interrogatories requesting that it identify each trade secret allegedly misappropriated by Defendants. Defs.' 2nd Mot. at 2 (citing Mr. Campton's First Discovery Request, ROG no. 11; Hi-Tech's First Discovery Request, ROG no. 1). In response to Mr. Campton's interrogatory, Stonhard referenced its complaint [FN3] and then listed generic categories of trade secrets: "installer list/network," "pricing strategy and policies," and "customer lists." In November of 2005, Stonhard objected to Hi-Tech's more detailed question on the same subject on the grounds that the question sought information containing, of all things, trade secrets.[FN4] Stonhard also objected on grounds that Hi-Tech's question was compound.

FN3. The court notes that Stonhard's reference to its pleading is an improper interrogatory response. *See, e.g.,* Smith v. Logansport Cmty. School Corp., 139 F.R.D. 637, 650 (N.D.Ind.1991) (an interrogatory "should be complete in itself and should not refer to the pleadings, or to depositions or other documents ...") (citing 4A J. Moore, J. Lucas, MOORE'S FEDERAL PRACTICE § 33.25[1] (2d ed.1991).

FN4. In response to the second motion to compel, Stonhard appears to have thought better than to reassert its objection to Hi-Tech's interrogatory on grounds that the question sought trade secrets information-in the context of its *trade secrets* lawsuit. Indeed, as of the date of Stonhard's response, the parties had been operating under a stipulated protective order for approximately four months. (Dkt. # 23; signed July 30, 2005).

Notwithstanding its prior objections, Stonhard contends that it has now complied with Defendants' discovery requests by revealing the pertinent information via other sources. Stonhard's Resp. at 6 (citing the declaration of Rick Neill, Sonhard's Vice President of Sales). Stonhard also argues that it sufficiently identified the trade secrets at issue in this case when, in its answer to Mr. Campton's interrogatory no. 11, it named three categories of its alleged trade secrets: installer network/list, pricing strategies and policies, and customer lists. Meanwhile, Defendants contend that they have "not received an answer to this very fundamental interrogatory."

*2 The court is not persuaded that Stonhard's reference to other sources of information indicates a full and complete written response to Defendants' interrogatories. Even if Stonhard has disclosed information relevant to the three categories of alleged trade secrets cited above, the following statement is at least one indication that Stonhard must do more: "StonCor's response to interrogatory 11 ... identified the trade secrets that are at issue in this case: StonCor's installer network and list, its pricing strategies and policies, and its customer lists, *among other things.*" Stonhard's Resp. at 6 (emphasis added). Defendants are entitled to discovery related to all of the so-called "other things" allegedly misappropriated.[FN5]

FN5. Without belaboring the point, the court notes that failure to identify trade secrets with some level of specificity could have grave consequences for Stonhard in the future. *Cf.* *Imax Corporation v. Cinema Technologies, Inc.,* 152 F.3d 1161, 1165-68 (9th Cir.1998) (exclusion of manufacturer's evidence was appropriate sanction where manufacturer continually failed to identify trade secrets with particularity in response to interrogatories). Although *Imax* involves California trade secrets law (which required plaintiff to identify with "sufficient particularity" its trade secrets prior to opening discovery), the sanction imposed by the trial court and upheld by the Ninth Circuit is equally available to this court.

The court directs Stonhard to provide a full and complete written response to Mr. Campton's interrogatory no. 11 and Hi-Tech's interrogatory no. 1 within fourteen (14) days from the date of this order subject to the following limitations. If Stonhard contends that such information has otherwise been fully disclosed via other sources, it is free to say so in its responses; however, if Stonhard chooses to do so, it must indicate the precise location of such information (e.g., by exhibit number and paragraph), the nature of the trade secret at issue, and whether the information constitutes its full and complete response. As to the allegedly compound nature of Hi-Tech's interrogatory no. 1, the court considers the question to contain two discreet sub-parts and thus, the question counts as two interrogatories. Stonhard should provide a full and complete answer to the first question, which the court construes as ending with "and all efforts to keep that Trade Secret confidential." Stonhard must also provide a full and complete answer to the second question, which should now read: "Identify and describe ... the nature, amount and computation of damages arising from a misappropriation of [each and every] Trade Secret."

2. "P-File" and Customer List Information

Defendants requested that Stonhard produce a copy of the "P-File" which contains Stonhard's customer list that Defendants allegedly misappropriated. Defs.' 2nd Mot. at 3 (citing Mr. Campton's First Discovery Request, RFP no. 5(m)). Initially, Stonhard objected on the grounds that the request sought confidential and trade secret information. Stonhard subsequently produced various documents relating to the customer files and continues to do so. Defendants do not dispute this fact; rather, Defendants contend that the disclosed documents contain updates and amendments to the customer list that occurred after Mr. Campton's departure. The court is persuaded that the relevant alleged trade secret is the data that Mr. Campton possessed or had access to at the time he left Stonhard. Defendants are entitled to discovery of the unchanged, unaltered data as of April 2005. The court directs Stonhard to produce a copy of the P-File as it existed on or near April 15, 2005 within fourteen (14) days from the date of this order. If such an unaltered copy has already been produced or is unavailable, Stonhard should so indicate.

3. Pricing Strategies and Policies

*3 Defendants requested that Stonhard disclose its pricing strategies and policies allegedly misappropriated by Defendants. Defs.' 2nd Mot. at 3 (citing Mr. Campton's First Discovery Request, ROG nos. 12, 18, 22, 24; RFP no. 4). In their briefing, Defendants only address Stonhard's allegedly deficient response with respect to interrogatory no. 24. Defs.' 2nd Mot. at 3; Defs.' 2nd Reply at 6. In their Reply, Defendants indicate that they seek any "written policies" in existence. Stonhard contends that it has supplemented its response to Defendants' request in January of 2006. The court is not prepared to grant a motion to compel on grounds that may or have become moot given Stonhard's most recent production. If the matter remains unresolved, Defendants may renew their motion following a meet and confer with opposing counsel.

As to the remaining discovery requests that allegedly relate to pricing strategies and policies (ROG nos. 12, 18, 22, and RFP no. 4), the court declines to consider Defendants' motion without some briefing as to why Stonhard's responses are deficient. Indeed, as pointed out by Stonhard, interrogatory nos. 12 and 18 do not appear to even relate to pricing policies.

4. Cost Book

Defendants requested that Stonhard produce its "Cost Book." Defs.' Mot at 3-4 (citing Mr. Campton's First Discovery Request, RFP no. 5(n)). Defendants contend that the Cost Book contains a pre-market "material list price" used in calculating profits, which in turn, allows Defendants to test Stonhard's damages computations. Stonhard originally objected on confidentiality-related grounds. Stonhard now contends that it has disclosed to Defendants' counsel the cost of materials used by Stonhard in transactions with Costco from its computer system. Given that Stonhard alleges that Mr. Campton used confidential and trade secret information to obtain *other* Stonhard customers, and not just Costco, the court cannot conclude that Stonhard's production is full and complete. Thus, the court grants Defendants' motion to compel production of the Stonhard Cost Book. Stonhard has fourteen (14) days from the date of this order to supplement its document production.

5. Identity of Managers

The court denies Defendants' motion to compel Stonhard to identify its list of managers. Defs.' 2nd Mot. at 4 (citing Mr. Campton's First Discovery Request ROG nos. 4-6). Stonhard contends that it has supplemented its discovery response in order to provide the identity and contact information of the relevant company managers; Defendants do not indicate otherwise in their Reply.

The court strongly cautions the parties that bringing discovery disputes to the court that become moot over the course of the briefing is a sure way to try the court's patience and increase the likelihood of sanctions against both parties in the future.

6. Warranty Claims

Defendants contend that Stonhard has failed to produce communications related to Costco regarding warranty claims. Defs.' 2nd Mot. at 4 (citing Mr. Campton's First Discovery Request, RFP no. 18). Stonhard contends that it has provided Defendants with significant electronic communications between Costco and Stonhard employees that would necessarily include warranty-related information. Defendants claim otherwise and point to the declaration of Howard Ackerman, a previous Stonhard employee, who cites to other documents potentially containing such information, besides electronic correspondence. Decl. Ackerman ¶ 6 (stating that, in response to finding a "field problem," Stonhard managers prepared a "Report of Complaint," followed up by a "No Charge Repair"). Accordingly, the court is not persuaded that Stonhard has provided a full and complete response to RFP no. 18, which is not limited to electronic communications. Stonhard has fourteen (14) days from the date of this order to supplement its document production.

B. Defendants' Third Motion to Compel

***4** In their third motion to compel, Defendants claim deficiencies with respect to "each and every" response of Stonhard to Hi-Tech's First Discovery Requests and Mr. Campton's Third Discovery Requests, issued on November 4, 2005. Defs.' 3rd Mot. at 1. Defendants contend that they have received "no answers" and thus, move for a blanket order compelling full and complete responses to all requests as well as for sanctions in the form of attorneys' fees or dismissal under Fed.R.Civ.P. 37(d). Prior to furnishing any response to Defendants' discovery requests, Stonhard attempted to meet with Defendants to narrow the scope and volume of requests. Keeley Decl. at 1, 2. Defendants declined and asked opposing counsel to simply provide answers to as many questions as possible. Farren Decl. at 5. With the discovery cut-off looming and without an indication of when (or if) Stonhard would supplement its responses, Defendants filed their second and third motions to compel.

In this third motion to compel, the court faces a global discovery dispute that overlaps with the particulars already addressed in the court's ruling on the second motion to compel and resurfaces again in Defendants' motion to dismiss, discussed below. Although the court disfavors Defendants' scatter-gun approach to gaining the court's attention, it is even more discouraged by Stonhard's pattern of boilerplate objections to Defendants' routine-enough discovery requests. In particular, the court considers Stonhard's objections on confidentiality-related grounds improper where the parties have stipulated to a protective order that affords attorney-eyes-only designations. At the same time, the court is dismayed to learn that Hi-Tech propounded a number of interrogatories which exceeds the 25-count allowance under the federal rules without leave of the court. Moreover, of the first 25 interrogatories, at least a few appear to contain sub-parts-although not nearly as many as Stonhard contends.

The court is unwilling, at this time, to sift through some 100 discovery requests and responses/objections where some disputes have become moot by the parties' own resolution or by the court's ruling on the second motion and where it is far from clear that the parties attempted to resolve *each issue* at their meet and confer. Thus, the court DEFERS consideration of Defendants' third motion to compel and directs the parties as follows.

The parties shall meet and confer, preferably in person, by February 13, 2006. For the second time over the course of this lawsuit, the court directs the parties to submit a letter to the court confirming that they have indeed participated in a conference. Prior to conferring with opposing counsel, Defendants shall weed out duplicative discovery requests as between Mr. Campton and Hi-Tech. Defendants shall not bring to the conference more than 25 interrogatories.[FN6] At the conference, the parties should address and attempt to resolve, in good faith, each and every remaining discovery dispute. The court urges Defendants to prepare an item-by-item chart of outstanding discovery requests in order to facilitate such a discussion. If any *specific* discovery matter remains unresolved after the parties confer, Defendants may submit a revised motion to compel, organized by interrogatory number or request for production number. The court strongly cautions Stonhard that its failure to identify objections with sufficient particularity will likely result in the court overruling such objections and awarding sanctions in Defendants' favor.

FN6. If Defendants wish to propound more than 25 interrogatories, they must obtain leave of the court.

C. Defendants' Motion to Dismiss

*5 Lastly, Defendants move for a Rule 12(c) dismissal of Stonhard's trade secrets claim. Defendants contend that they are entitled to judgment as a matter of law because Stonhard fails in its complaint to describe with particularity the information that constitutes a trade secret. In support of their argument, Defendants also refer to the above discovery dispute to suggest that Stonhard's trade secrets claim lacks merit based on their contention that Stonhard is "hiding the ball" in discovery. In doing so, Defendants present matters outside of the pleadings, which, if considered by the court, would convert their motion into a summary judgment motion governed by Fed.R.Civ.P. 56 ("Rule 56"). Fed.R.Civ.P. 12(c).

Defendants' motion fails whether considered under Rule 12(c) or Rule 56. First, because the court has already determined that Defendants are entitled to further discovery on the trade secrets claim, the court considers a motion for summary judgment as premature. Second, the court is satisfied that Stonhard's complaint meets the low threshold required to survive a Rule 12(c) motion. On Defendants' 12(c) motion, the court accepts all of Stonhard's allegations of fact as true, and construes them in the light most favorable to Stonhard. *Conference Corp. of Seventh-Day Adventists v. Seventh-Day Adventist Congregational Church*, 887 F.2d 228, 230 (9th Cir.1989). Dismissal should not be granted "unless it appears beyond a reasonable doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Wyler Summity P'ship v. Turner Broad. Sys., Inc.*, 135 F.3d 658, 661 (9th Cir.1998) (internal quotations and citations omitted).[FN7]

FN7. As both parties indicate, the standard for dismissal for failure to state a claim under Rule 12(c) is the same as under Fed.R.Civ.P. 12(b)(6).

Here, construing the facts in the light most favorable to Stonhard, the court is satisfied that Stonhard states a claim upon which relief could be granted under Washington's Uniform Trade Secrets Act, RCW § 19.108.010 *et seq.* [FN8] Stonhard's complaint includes allegations that: Mr. Campton had "unique access" to "proprietary and confidential information concerning StonCor's sales and marketing strategies, pricing and pricing policies, and customer lists and installers ..."; Mr. Campton had a duty to keep such information confidential under his employment agreement; and Mr. Campton abruptly resigned from Stonhard, signed with Hi-Tech, and actively solicited Stonhard customers using Stonhard's confidential and trade secrets information. Amended Compl. at ¶¶ 9-12, 21, 25, 27. To be sure, Stonhard's pleading could have been more carefully drawn to incorporate its factual allegations in the subsequent discussion of specific causes of action. Still, Stonhard's complaint need not be a model of clarity to survive dismissal. *See, e.g., Alnwick v. European Micro Holdings, Inc.*, 281 F.Supp.2d 629, 638 (E.D.N.Y.2003) (denying motion to dismiss where plaintiff alleged that defendant improperly used a variety of secret information including its customer and supplier contacts and lists); *A & G Healthplans v. Nat'l Network Services*, No. 99-cv-12153(GBD), 2003 WL 1212933, at *3 (S.D.N.Y. Mar. 24, 2003) (denying motion to dismiss a trade-secret counterclaim where the defendant alleged that plaintiffs wrongfully used its confidential business relationships with medical providers to obtain discounts from those providers).

FN8. In general terms, a trade secret includes information that has independent economic value, is not generally known, and is the subject of reasonable efforts to maintain its secrecy. RCW § 19.108.010(4). Misappropriation includes the improper acquisition, disclosure, or use of such information. *Id.* at 19.108.010(2).

III. CONCLUSION

*6 For the foregoing reasons, the court GRANTS in part and DENIES in part Defendants' second motion to compel and DENIES Defendants' motion to dismiss. The court DEFERS consideration of Defendants' third motion to compel until further notice.

W.D.Wash.,2006.
StonCor Group, Inc. v. Campton
Not Reported in F.Supp.2d, 2006 WL 314336 (W.D.Wash.)

END OF DOCUMENT

TAB 14

United States District Court,
C.D. Illinois.
UNISOURCE WORLDWIDE, INC., Plaintiff,
v.
Chester D. CARRARA, Richard W. McCormick, Michael J. McCormick, Daniel J. Cady, David M. Schaidle, Paul F. Hetman, Jeffrey W. Lichtenberger, and Brenda L. Baker, Defendant.
No. 03-1015.

Feb. 19, 2003.

Former employer, a distributor of printing and paper products, sued former employees, who went to work for competitor, alleging breach of contracts and misappropriation of trade secrets. On employer's motion for preliminary injunction barring employees from breaching non-competition provisions in contracts and providing confidential information to competitor, the District Court, Mihm, J., held that: (1) employer could enforce restrictive covenants contained in its predecessor's employment agreements with former employees; (2) two year and 18-month restrictions imposed on employees' postemployment activities contained in non-competition covenants in agreements were unreasonable; (3) restrictive covenants prohibiting employees from doing business, upon their termination, not only with customers they worked with, but also with customers and products they never dealt with before, were unreasonable in terms of scope; (4) restrictive covenant which prohibited employee from doing business with two competitors for six months following his termination was reasonable in time and scope; (5) non-competition clauses, which restricted employees from engaging in postemployment activities of soliciting or inducing other employees to leave distributor's employment, were invalid restraints on trade; and (6) none of the information that employer sought to protect through its restrictive covenants was confidential, and thus covenants were not enforceable against employees.

Motion denied.

West Headnotes

[1] Corporations 101 589

101 Corporations
101XIV Consolidation
101k589 k. Succession to Rights of Original Corporations. Most Cited Cases
Successor employer could enforce restrictive covenants contained in predecessor's employment agreements with former employees, although agreements were allegedly never assigned to successor, and agreements were silent on issue; employees would not be prejudiced by having agreements assigned to successor, since restrictive covenants were scrutinized closely and upheld only to extent they were reasonable and necessary to protect employer's legitimate business interest.

[2] Contracts 95 116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases
Generally, restrictive covenants must be reasonable in terms of time and scope in order to be enforceable.

[3] Contracts 95 9(1)

95 Contracts
95I Requisites and Validity
95I(A) Nature and Essentials in General
95k9 Certainty as to Subject-Matter
95k9(1) k. In General. Most Cited Cases
To enforce contract under Illinois law, essential terms of contract must be intelligible.

[4] Contracts 95 116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Considera-

tion
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(1) k. In General. Most Cited Cases
Under Illinois law, where employment contract was ambiguous and unintelligible, non-compete clause in agreement was unenforceable because there was no definite agreement on essential terms of restrictive covenant.

[5] Contracts 95 ⚷117(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k117 General or Partial Restraint
95k117(2) k. Limitations as to Time and Place in General. Most Cited Cases
Two year restriction imposed on employees' postemployment activities contained in non-competition covenants in employment agreements with employer, a distributor of printing and paper products, constituted unreasonable restraint on trade, under Illinois law; any inside information former employees might have upon leaving employer would not serve to give employees competitive edge for longer than six to twelve months, because information would become stale after that time.

[6] Contracts 95 ⚷117(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k117 General or Partial Restraint
95k117(1) k. Nature of Business to Which Contract Relates. Most Cited Cases
Under Illinois law, restrictive covenants in employment agreements prohibiting employees from doing business, upon their termination, not only with customers they worked with while employed with distributor of printing and paper products, but also with customers and products they never dealt with before, were unreasonable in terms of scope, and thus were unenforceable.

[7] Contracts 95 ⚷117(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k117 General or Partial Restraint
95k117(2) k. Limitations as to Time and Place in General. Most Cited Cases
Restrictive covenant, which prohibited employee from doing business with two competitors for six months following his termination, was reasonable in time and scope under Illinois law.

[8] Contracts 95 ⚷116(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases
Non-compete provisions in employment agreements, which restricted distributor's employees from engaging in postemployment activities of soliciting or inducing other employees to leave distributor's employment, were invalid restraints on trade, in that, provisions did not serve to protect any legitimate business interest recognized under Illinois law.

[9] Contracts 95 ⚷116(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases

95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases

Contracts 95 118

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k118 k. Preventing Disclosure of Trade Secrets. Most Cited Cases

For information to be "confidential," so that employer has legitimate business interest, under Illinois law, in protecting information from disclosure by former employee through postemployment restrictive covenant, information must not be generally known, must be valuable to competitors, and must be protected or kept secret by business claiming that it is confidential.

[15] Contracts 95 116(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases

Information that is generally known by persons in trade or that could easily be duplicated by reference to telephone directories or industry publications is not "confidential" information, and is thus not protectable, under Illinois law, through covenant not to compete.

[16] Contracts 95 118

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k118 k. Preventing Disclosure of Trade Secrets. Most Cited Cases

Distributor's customer information, such as the name and purchase history of specific customers, prices charged, and profit margin from sales to those customers was not "confidential" information under Illinois law, and thus restrictive covenant prohibiting disclosure of such information by distributor's former employee was not enforceable; identity of potential customers and suppliers was readily available in marketplace, and distributor had no proprietary interest in customer's purchase history, needs and preferences.

[17] Antitrust and Trade Regulation 29T 413

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(A) In General
29Tk413 k. What Are "Trade Secrets" or Other Protected Proprietary Information, in General. Most Cited Cases
(Formerly 382k984 Trade Regulation, 379k10(5))

Antitrust and Trade Regulation 29T 421

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(A) In General
29Tk421 k. Customer Lists and Information. Most Cited Cases
(Formerly 382k991 Trade Regulation, 379k10(5))

Items such as customer lists, pricing information, and business techniques can be trade secrets, under Illinois law, if employer has developed information over number of years at great expense and kept it under tight security.

[18] Contracts 95 118

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k118 k. Preventing Disclosure of

Trade Secrets. Most Cited Cases
Distributor's price information was not "confidential," under Illinois law, and thus restrictive covenant, prohibiting former employee from disclosing such information to competitor, was not enforceable; competitors could obtain distributor's price information directly from distributor's customers, and sharing of such information was common event in industry.

[19] Contracts 95 ⚷118

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k118 k. Preventing Disclosure of Trade Secrets. Most Cited Cases
Distributor's information concerning its profit margins, costs, and markups was not "valuable" enough to competitors to constitute "confidential" information, under Illinois law, as would support enforcing restrictive covenant prohibiting distributor's former employee from disclosing such information to competitors.

[20] Contracts 95 ⚷118

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k118 k. Preventing Disclosure of Trade Secrets. Most Cited Cases
Information regarding distributor's key personnel, including what they did, what they cost, and how effective they were, could not be protected, under Illinois law, by restrictive covenant prohibiting distributor's former employee from disclosing such information to competitors; such information was not type that was intended to be protected by covenants not to compete.

[21] Contracts 95 ⚷118

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k118 k. Preventing Disclosure of Trade Secrets. Most Cited Cases
General information regarding customer coverage, staffing, and how distributor conducted its business was not "confidential" information, under Illinois law, and thus restrictive covenant prohibiting former employee from sharing such information was unenforceable.

[22] Antitrust and Trade Regulation 29T ⚷414

29T Antitrust and Trade Regulation
29TIV Trade Secrets and Proprietary Information
29TIV(A) In General
29Tk414 k. Elements of Misappropriation. Most Cited Cases
(Formerly 382k984 Trade Regulation, 379k10(5))
To set forth violation of the Illinois Trade Secrets Act, plaintiff must establish that the information at issue was (1) trade secret, (2) misappropriated, and (3) used in defendant's business. S.H.A. 765 ILCS 1065/2(d).
***979** Michael Levinson,Charles Chejfec, Andy Clark, Seyfarth & Shaw, Chicago, IL, for Plaintiff.

***980** John Dickman,Kevin Cloutier, William Miossi, Winston & Strawn, Chicago, IL, J. Reed Roesler, Davis & Campbell, Peoria, IL, for Defendants.

ORDER

MIHM, District Judge.

Plaintiff Unisource Worldwide, Inc. (Unisource) has sought a preliminary injunction in this case to prevent the Defendants from breaching their covenants not to compete with Unisource and disclosing Unisource's trade secrets and confidential information.

A preliminary injunction is warranted if the movant can demonstrate: (1) a reasonable likelihood of success on the merits, (2) no adequate remedy at law, (3) irreparable harm if preliminary relief is denied that outweighs the irreparable harm the nonmoving party will suffer if the injunction is granted, and (4) public interest. *Mil-Mar Shoe Co., Inc. v. Shonac Corp.,* 75

F.3d 1153, 1156 (7th Cir.1996).

The Court finds that Unisource has not established a reasonable likelihood of success on the merits. Therefore, the other factors are moot, and the Motion for a Preliminary Injunction [# 3-2] is DENIED, and the Temporary Restraining Order previously entered by the Court is dissolved.

Background

Unisource is a national distributor of printing and imaging papers, packaging, and facility supplies and equipment with over two hundred locations. It operates a sales facility in Morton, Illinois, and a customer service facility in St. Louis, Missouri.

The printing and paper products sales business is intensely competitive. Many companies offer products and services similar to Unisource. Unisource relies upon its sales force to provide face-to-face service to its customers before and after the sale. Unisource's sales representatives and customer service employees develop personal acquaintances with Unisource's current and prospective customers. The sales representatives analyze the customers' unique printing and paper needs, and tailor their services to solve each individual customer's needs.

Defendants Chester Carrara (Carrara), Richard McCormick, and Michael McCormick were Unisource sales representatives employed at Unisource's Morton, Illinois facility. Their duties included soliciting existing and prospective Unisource customers to determine their needs, generating new sales opportunities, tracking customer purchasing over time to anticipate customers' future requirements, and following up with customers after sales.

Defendants David Schaidle (Schaidle) and Daniel Cady (Cady) were Unisource customer service employees operating out of Unisource's St. Louis, Missouri facility. They were responsible for executing orders generated by Unisource's sales representatives. Unisource customers frequently call customer service employees directly with their paper and printing needs.

Defendant Jeffrey Lichtenberger (Lichtenberger) was a Unisource product specialist operating out of Unisource's St. Louis, Missouri, facility. He was responsible for dealing with the vendors from whom Unisource purchased many of its products.

Defendant Paul Hetman (Hetman) was a Unisource packaging equipment technician operating out of Unisource's Morton, Illinois, facility. His primary responsibility was to visit Unisource customers to ensure that their Unisource products were functioning properly.

Finally, Defendant Brenda Baker (Baker) was a Unisource administrative assistant*981 at Unisource's Morton, Illinois, facility. She assisted Carrara and others.

Baker resigned from Unisource effective December 20, 2002. Carrara, Richard McCormick, and Michael McCormick resigned from Unisource effective December 31, 2002. Cady and Schaidle resigned from Unisource effective January 3, 2003. Each of these Defendants subsequently commenced working for Midland Paper Company-a competitor of Unisource in Bloomington, Illinois-where at least some of the Defendants, including Carrara, Michael McCormick, and possibly Richard McCormick, began soliciting and calling upon customers they had worked with while employed at Unisource.

Each of the Defendants had signed employment agreements with Unisource. Four contained covenants not to compete. All eight contained provisions restricting disclosure of Unisource' confidential information. Two contained provisions prohibiting the Defendants from soliciting or hiring Unisource employees.

Unisource asserts that the Defendants' conduct is in breach of their respective employment contracts. Unisource also argues that all eight of the Defendants were privy to confidential information and trade secrets while employed at Unisource, which they are now misappropriating to obtain the business of Unisource's former customers.

On January 21, 2003, this Court entered a temporary restraining order prohibiting the Defendants from soliciting business or taking new orders from certain customers. On February 11-12, 2003, the Court held a preliminary injunction hearing. This Order follows.

Discussion

I. Defendants' Employment Contracts with Unisource

A. Choice of Law

The parties agree that Illinois law governs the contracts with Carrara, Richard McCormick, David Schaidle, Daniel Cady, Jeff Lichtenberger, and Paul Hetman. The parties agree that Missouri law governs the contract with Michael McCormick. Finally, the parties agree that Georgia law governs the contract with Baker.

B. Assignability

[1] Carrara and Michael McCormick each had an employment contract with a company called Distribix, which subsequently merged with Unisource. They argue that their contracts with Distribix were never assigned to Unisource, and therefore that Unisource cannot enforce them.

The Court adopts the rationale regarding this issue applied in AutoMed Technologies, Inc. v. Eller, 160 F.Supp.2d 915, 924 (N.D.Ill.2001). In that case, Judge Moran noted that, since courts scrutinize restrictive covenants closely and will uphold them only to the extent they are reasonable and necessary to protect an employer's legitimate business interest, an employee will not be prejudiced by having the contract assigned to a successor business.

Carrara and Michael McCormick are primarily concerned with the fact that Unisource has a vastly greater number of product lines and locations than Distribix had, which would impose much greater limitations on their freedom to compete under the terms of their contracts.[FN1] Because this Court will only uphold the provisions to the extent they are reasonable and ***982** necessary, however, Carrara's and Michael McCormick's concern is adequately addressed.

FN1. According to Carrara's testimony, Distribix had fifteen product lines and seven locations, while Unisource has over fifty product lines and over two hundred locations.

Furthermore, where an employment contract is silent on this issue-as Carrara's and Michael McCormick's are-courts generally find that an acquiring corporation can enforce the acquired company's restrictive covenants. *See* Hexacomb Corp. v. GTW Enter., 875 F.Supp. 457, 464 (N.D.Ill.1993). Therefore, the Court finds that Unisource can enforce Carrara's and Michael McCormick's contracts with Distribix.

C. Enforceability of Covenants Not to Compete

[2][3] The employment agreements of four Defendants-Carrara, Richard McCormick, Michael McCormick, and Hetman-contain covenants not to compete. As a general rule, restrictive covenants must be reasonable in terms of time and scope in order to be enforceable. *Eichmann v. Nat'l Hosp. and Health Care Services, Inc.,* 308 Ill.App.3d 337, 241 Ill.Dec. 738, 719 N.E.2d 1141, 1148 (1999); *Schmersahl, Treloar & Co. v. McHugh,* 28 S.W.3d 345, 349 (Mo.Ct.App.2000). Furthermore, the essential terms of a contract must be intelligible. *Anderson v. Fel-Pro Chem. Prod.s,* 1996 U.S. Dist. LEXIS 19551, *20-*21 (N.D.Ill.1997); *see Pearson Bros. Co. v. Pearson,* 113 B.R. 469, 475 (C.D.Ill.1990); *Xu Liu v. Price Waterhouse,* 1999 WL 1012456, *4, 1999 U.S. Dist. LEXIS 16559, *13-*14 (N.D.Ill.1999).

1. Carrara's Contract

[4] Carrara's contract contains a restrictive covenant prohibiting him from selling, soliciting, or in any way doing business, "on a direct or indirect basis with any of the product lines, customers or accounts of the Employer within a 25 mile radius of the cities and towns in which Employer's Division or Subsidiary does business" for two years following termination. (Pl.'s Ex. 1, ¶ 1(B)(1)(b).) Immediately following this provision is the following:

(2) (Continued)

do business with any of Employer's product lines to any customers or accounts assigned to him/her by Employer during the one (1) year period prior to Employee's termination. Moreover, Employee agrees to be bound by all the other provisions of this agreement other than subparagraph (1) above.

There is no transitional language explaining of what this sentence fragment is a "continuation," nor is there any language explaining how this provision fits in with the preceding provision. On the contrary, the provision indicates that Carrara does not agree to be bound by the previous provision. Given its literal meaning, this would mean that Carrara did not agree to be bound by the covenant not to compete.

To say the least, the contract is ambiguous and unintelligible. Since there is no definite agreement on the essential terms of the restrictive covenant, it is unenforceable. *Anderson,* 1996 U.S. Dist. LEXIS 19551, *20-*21; *see* Pearson Bros. Co. v. Pearson, 113 B.R. 469, 475 (C.D.Ill.1990); *Xu Liu,* 1999 WL 1012456, **4-5, 1999 U.S. Dist. LEXIS 16559, *13-*14.

[5] Even if the contract was not ambiguous, it would still not be enforceable. The Court finds that, as applied to the industry at issue in this case, two years is an unreasonable period of time to impose in a covenant not to compete. This is because the prices, costs, and customer information governing Unisource's operations at any particular time are volatile. While some products' prices are more volatile than others, Unisource's Regional Vice President testified that changes are made within Unisource's price books about every six months, and internal pricing information is stale after twelve months. Therefore, any inside information a former employee***983** may have upon leaving Unisource would not serve to give that employee a competitive edge for longer than six to twelve months, because the information would become stale after that time. The record indicates that a twelve month restriction would be the outside limit to protect any legitimate interest Unisource may have in this respect. Therefore, the Court finds that the restrictive covenant in Carrara's contract constitutes an invalid restraint on trade.

[6] Furthermore, the restrictive covenant contained in paragraph 1(B)(1)(b) is overbroad in that it seeks to prohibit Carrara from doing business not only with the customers he worked with while employed at Unisource, but also with customers and products he never dealt with before. "Courts are hesitant to enforce prohibitions against employees servicing not only customers with whom they had direct contact, but also customers they never solicited or had contact with while employed by plaintiff." *Lawrence and Allen, Inc.,* 226 Ill.Dec. 331, 685 N.E.2d at 442. Since both covenants are unreasonable in terms of time and scope, they are invalid.

2. Richard McCormick's Contract

Richard McCormick's contract contains three non-compete provisions. (Pl.'s Ex. 6.) The first and third provisions prohibit him from directly or indirectly soliciting, selling to, providing services, or in any way doing business with Archer Daniels Midland (ADM) and all divisions, subsidiaries and affiliates of Tate and Lyle in any of the product lines offered by Unisource, or competitive with any product lines offered by Unisource, for six months following termination.

[7] The Court finds that the six month time limitation is reasonable. The Court also finds that the narrow restriction prohibiting Richard McCormick from doing business with only two of the customers he worked with while employed at Unisource is reasonable.

[8] The second non-compete provision prohibits Richard McCormick from inducing or encouraging any employee of Unisource to leave the employment of Unisource, or otherwise soliciting or hiring any such employee for six months following termination. In support of this provision, Unisource cites to *Arpac Corp. v. Murray,* 226 Ill.App.3d 65, 168 Ill.Dec. 240, 589 N.E.2d 640, 650 (1992), which upheld a restrictive covenant prohibiting a former employee from inducing the employer's other employees to quit. The court in *Arpac Corp.* reasoned that an employer has a "legitimate business interest" in maintaining a stable work force. *Id.*

[9] This Court finds that *Arpac Corp.* represents a misapplication of Illinois law. As discussed later in this Order, the only two "legitimate business interests" that may give rise to a covenant not to compete in Illinois are "near permanent" relationships with customers, and confidential information or trade secrets. *Lawrence and Allen, Inc. v. Cambridge Human Res. Group,* 292 Ill.App.3d 131, 226 Ill.Dec. 331, 685 N.E.2d 434, 443 (1997). Therefore, the Court rejects the reasoning applied in *Arpac Corp.,* and finds that the covenant restricting Richard McCormick from soliciting or hiring other Unisource em-

ployees is an invalid restraint on trade. *See* Schmersahl, Treloar & Co. v. McHugh, 28 S.W.3d 345, 351 (Mo.Ct.App.2000) (finding that "an employer's interest in protecting the stability of its at-will workforce is not one of the interests which may be protected by a restrictive covenant in Missouri").FN2

> FN2. Although Missouri law does not govern the contract in question, the Court finds the reasoning in *Schmersahl* to be persuasive and equally applicable under Illinois law. This Court is not bound by the Illinois appellate court's decision in *Arpac Corp.,* and believes that the Illinois Supreme Court, if and when it decides this issue, will support this Court's position.

***984** [10] Because there is a severability provision in paragraph 7 of Richard McCormick's contract, the Court finds it unnecessary to invalidate the entire contract. Rather, the invalid provisions may be severed, leaving the valid provisions intact. *See* Abbott-Interfast Corp. v. Harkabus, 250 Ill.App.3d 13, 189 Ill.Dec. 288, 619 N.E.2d 1337, 1343 (1993) (finding that a trial court may sever unenforceable provisions from a contract, and stating that "[t]he existence of a severability clause in a contract certainly strengthens the case for the severance of unenforceable provisions").

3. Michael McCormick's Contract

Michael McCormick's contract contains two covenants not to compete. (Pl.'s Ex. 4.) The first covenant prohibits him from directly or indirectly soliciting, selling to, or in any way doing business with any of the customers assigned to him or in any of the product lines sold by him within twelve months preceding his termination, for a period of two years following his termination. The second covenant prohibits him from directly or indirectly soliciting, selling to, or in any way doing business with any of Unisource's customers or accounts or in any of the product lines sold by Unisource within fifty miles of any of the offices of the division where Michael McCormick was employed, or within fifty miles of his residence, for a period of two years following his termination.

As discussed in the section of this Order addressing Carrara's contract, the Court finds that two years is an unreasonable period of time for Unisource to impose in a covenant not to compete. Therefore, the Court finds that the restrictive covenants in Michael McCormick's contract constitute invalid restraints on trade.

Furthermore, the second restrictive covenant is overbroad in that it seeks to prohibit Michael McCormick from doing business not only with the customers he worked with while employed at Unisource, but also with customers and products he has never dealt with before. Since both covenants are unreasonable in terms of time and/or scope, they are invalid.

4. Hetman's Contract

[11] Hetman's contract contains three non-compete provisions. (Pl.'s Ex. 7.) The first provision prohibits him from directly or indirectly soliciting, selling to, providing services, or in any way doing business with any of the customers or accounts of Unisource with whom he had become associated during the twelve month period preceding his termination, in any of the product lines offered by Unisource to such customers or accounts during such twelve month period, for eighteen months following termination.

As discussed in the portion of this Order addressing Michael McCormick's contract, any period longer than twelve months is too long for Unisource to impose in a covenant not to compete. Therefore, the first covenant in Hetman's contract constitutes an invalid restraint on trade.

The second non-compete provision prohibits Hetman from inducing or encouraging any employee of Unisource to leave the employment of Unisource, or otherwise soliciting or hiring any such employee for eighteen months following termination. As discussed in the portion of this Order addressing Richard McCormick's contract, this type of covenant does not serve to protect any legitimate business interest recognized under Illinois law. Also, the eighteen month period is unreasonable. ***985** Therefore, the second provision constitutes an invalid restraint on trade.

The third and final non-compete provision prohibits Hetman from soliciting, selling to, providing services for, or in any way doing business with any of the customers or accounts of Unisource, in any product lines competitive with any product lines offered by

Unisource, within a fifty mile radius of any Unisource office or retail location in which Hetman was employed during the twelve month period preceding his termination, for eighteen months following termination.

As stated above, an eighteen month restriction is too long under the circumstances of this case. Furthermore, the covenant is overbroad in that it seeks to prohibit Hetman from doing business with customers he never met while at Unisource. Therefore, the third provision constitutes an invalid restraint on trade.

5. Conclusion

In sum, the restrictive covenants contained in the agreements signed by Carrara, Michael McCormick, and Hetman are invalid because they are unreasonable in terms of time, scope, and/or interest sought to be protected. [FN3] Only the first and third restrictive covenants contained in Richard McCormick's agreement have survived up to this point. The inquiry does not end here, however.

FN3. Because Carrara's and Michael McCormick's restrictive covenants have been found to be unenforceable, the Court finds it unnecessary to address the Defendants' argument that their agreements have been superceded by subsequent agreements with Unisource that do not contain any non-compete provisions.

D. Legitimate Business Interest of Employer

[12] Covenants not to compete are only valid to the extent they protect a "legitimate business interest" of the employer. *Lawrence and Allen, Inc.*, 226 Ill.Dec. 331, 685 N.E.2d at 441; *see* *Armstrong v. Cape Girardeau Physicians Assoc.s*, 49 S.W.3d 821, 825 (Mo.App.2001). Only two legitimate business interests are recognized in Illinois: 1. "near-permanent" relationships with customers, and 2. trade secrets or confidential information that a former employee has acquired through his or her employment and subsequently tried to use for his or her own benefit.[FN4] *Id.* at 443.

FN4. Missouri law also recognizes two narrowly defined interests: trade secrets and stock in customers. *Armstrong*, 49 S.W.3d at 825.

[13] Unisource has abandoned the argument that it has a near-permanent relationship with its customers. (Pl.'s Mem. at 6 n. 1.) Therefore, in order to enforce Richard McCormick's covenant not to compete, Unisource must prove that Richard McCormick has tried to use confidential information belonging to Unisource for the benefit of himself or Midland. *Lawrence and Allen, Inc.*, 226 Ill.Dec. 331, 685 N.E.2d at 445.

[14] The parties agree that in order to be "confidential," information must not be generally known, must be valuable to competitors, and must be protected or kept secret by the business claiming that it is confidential.

The information that Unisource seeks to protect in this case includes: (1) customer information, such as the name and purchase history of specific customers, prices charged, and the profit margin from sales to those customers; (2) "off book" prices, or prices charged to customers that are lower than the prices contained in Unisource's price books; (3) information regarding key Unisource personnel, including what they do, how much they cost, and how effective they are; (4) costs and margins,***986** including the "deviated" costs Unisource obtains from its vendors, the three percent "load" or "warehousing" cost, and gross trading margins; (5) information regarding customer coverage, staffing, and how Unisource conducts its business; and (6) the ten percent markup that Unisource requires in order for a sales representative to close a sale and be eligible for commission.

1. Customer Information

[15][16] The record in this case amply demonstrates that the identity of potential customers and suppliers is readily available in the marketplace. Information that is generally known by persons in the trade or that could easily be duplicated by reference to telephone directories or industry publications is not protectable. *Springfield Rare Coin Galleries, Inc. v. Mileham*, 250 Ill.App.3d 922, 189 Ill.Dec. 511, 620 N.E.2d 479, 485 (1993). This is especially true in industries such as that of Unisource, where customers do business with more than one distributor so that their identities are known to competitors. *Id.*

Furthermore, Illinois case law provides that a distributor has no proprietary interest in information belonging to the customer, such as the customer's own purchase history, needs and preferences. Delta Med. Systems v. Mid-America Med. Systems, Inc., 331 Ill.App.3d 777, 265 Ill.Dec. 397, 772 N.E.2d 768, 783 (2002) (noting that a service provider "cannot control what a customer does with its own information"); *see* Office Mates 5, North Shore, Inc. v. Hazen, 234 Ill.App.3d 557, 175 Ill.Dec. 58, 599 N.E.2d 1072, 1084 (1992) (holding that client information is not a trade secret where it can be obtained by asking questions designed to elicit the information requested); A.J. Dralle, Inc. v. Air Technologies, Inc., 255 Ill.App.3d 982, 194 Ill.Dec. 353, 627 N.E.2d 690, 697 (holding that customer information that is readily available to competitors through normal competitive means, such as placing a cold call and asking questions, is not protectable). Therefore, a customer's purchase history is not confidential information.

The record indicates that on November 20, 2002, Baker generated a "customer list" for each Unisource sales representative working out of Morton, Illinois. According to John Montgomery, the Operations Manager at Unisource's Morton, Illinois, facility, the customer list would have contained the customer number, name, address, key contact person, and telephone number of each specific sales representative's current customers. Baker mailed Carrara's customer list to him on November 20, 2002.

After conducting an investigation, Montgomery concluded that the customer lists were generated to aid the sales representatives in sending out holiday cards. Therefore, Baker's conduct in mailing a customer list to Carrara does not appear to be suspicious or improper. In any event, based on the foregoing analysis, none of information contained in the customer list is confidential.

2. Price Information

[17][18] In some circumstances, "[i]tems such as customer lists, pricing information, and business techniques can be trade secrets if the employer has developed the information 'over a number of years at great expense and kept [it] under tight security.' " Abbott-Interfast Corp., 189 Ill.Dec. 288, 619 N.E.2d at 1344. In this case, however, a customer who purchases products from both Unisource and Midland testified that, though not "standard procedure," from time to time his company would tell one distributor the price that a competing distributor had offered. He also stated that a sales representative***987** from one company would occasionally look at a competitor's price book. Furthermore, the unrebutted testimony of Carrara, Richard McCormick, and Michael McCormick was that their customers would routinely show them competitors' price books and provide them with competitive information, including prices that competitors were quoting to them.

Although the record does not indicate the exact percentage of prices shared, the Court finds that the percentage was substantial, based in part on the friendly relations between the Unisource sales people and the customer representatives. Moreover, Illinois cases hold that pricing information conveyed to a customer that the customer is at liberty to divulge is not confidential. Carbonic Fire Extinguishers, Inc. v. Heath, 190 Ill.App.3d 948, 138 Ill.Dec. 508, 547 N.E.2d 675, 678 (1989); Applied Indus. Materials Corp. v. Brantjes, 891 F.Supp. 432, 437-38 (N.D.Ill.1994) (noting that "the Illinois appellate courts which have addressed the issue have consistently held that price information which is disclosed by a business to any of its customers, unlike a unique formula used to calculate the price information which is not disclosed to [the] business's customers, does not constitute trade secret information"). The reasoning applied in *Carbonic Fire Extinguishers* is equally applicable here:

> The pricing information here, unlike a unique formula used to calculate a price but unknown to a customer or competitors (citation omitted), was available to the various customers to which it pertained. As such, those customers were at liberty to divulge such information to a competitor of plaintiff's, or to anyone for that matter. Further, there is no evidence that someone else performing this service would not have knowledge of the normal price to be charged for this service. Plaintiff does not contend that its price for a job is unique or not generally known to others in the business.

Id.

Unisource is not alleging that it had any unique pricing formula that was not disclosed to its customers. In fact, Unisource's Regional Vice President testified that the ultimate price obtained from a customer depended in large part on the sales representative. Instead, Unisource is claiming that its prices charged to customers-of which the customers were obviously aware-are confidential. However, Unisource did not require its customers to sign any confidentiality agreements or otherwise restrict the customers' freedom to disclose this information. Therefore, because competitors can obtain Unisource's price information directly from the customer, and because there is abundant evidence that sharing of information by a customer is a common event, it is not confidential.

3. Cost Information

[19] Having found that Unisource's price information is not confidential, the Court finds that information concerning Unisource's profit margins, costs, and markups is not "valuable" enough to competitors to constitute confidential information. Although this information could conceivably assist a competitor in determining the prices Unisource charges to its customers, thereby enabling the competitor to undercut Unisource, the Court has already found that Unisource's customers are at liberty to disclose information concerning Unisource's prices. Once the price of a Unisource product is known, a competitor's focus shifts to its own costs and necessary profit margins, and the competitor then determines-based on its own internal figures-whether it can undercut Unisource in price.

***988** Furthermore, Unisource does not use its cost information to derive any sort of pricing formula that, as a practical matter, strictly limits the prices for which its products are sold. Rather, the sales representatives are almost totally responsible for setting Unisource's prices. The parties do not dispute this fact.

Carrara testified that his average profit margin while at Unisource was between twentyfive and twenty-seven percent. Consequently, knowledge of Unisource's three percent markup for "load" or "warehousing" costs (which do not apply if the manufacturer ships a product directly to the customer), and ten percent markup for sales commissions, would not enable a competitor to pinpoint Unisource's prices. The final price Unisource charges a customer for a product ultimately has more to do with the sales representative's profit margin than the required warehouse cost or ten percent commission markup. In sum, information concerning Unisource's costs and markups is not confidential.

4. Personnel Information

[20] Information regarding key Unisource personnel, including what they do, what they cost, and how effective they are, is not the type of information that Illinois law intends to protect in this context. As discussed under section I(C)(2) above, Unisource does not have a protectable interest in its workforce.

Furthermore, Midland's Vice President of sales and marketing, John Millin, testified in his deposition that it is generally known in the industry who the top performers are at any company. (Millin Dep. at 41.) Therefore, although information concerning specific Unisource employees' gross trading margins may not be generally available, Midland recruiters could learn from discussions with customers who the most respected sales representatives are, and could attempt to recruit those people. (Millin Dep. at 41, 44.)

Because Unisource may not prevent its competitors from soliciting and hiring its employees, and because the reputation of sales representatives is generally known in the industry, information regarding what its employees do, how much they cost, and how effective they are is not protectable.

5. General Business Practices

[21] General information regarding customer coverage, staffing, and how Unisource conducts its business is not protectable, because "[o]ne who works for another cannot be compelled to erase from his mind all of the general skills, knowledge, acquaintances and the over-all experience" that he acquired during the course of his employment. *Revcor, Inc. v. Fame, Inc.*, 85 Ill.App.2d 350, 228 N.E.2d 742, 746 (1967). Unisource does not allege that it has any secret methods or processes for selling products that differ from the methods and processes of its competitors. Although Unisource may send its sales representatives out to meet with customers face-to-face and develop relationships with those customers, this practice does not constitute a protected trade secret or confidential information. Rather, it is the general way that business in the industry is conducted, and such general knowledge cannot be protected by a restrictive cove-

nant.

6. AS 400 Printout

On November 8, 2002, Carrara asked Baker for a printout from Unisource's AS 400 system, a database that is part of Unisource's computer network. Baker printed the requested information, which was subsequently mailed via overnight delivery to Carrara's residence on Saturday, November 9. The package mailed weighed a total of .4 pounds, which is approximately***989** equivalent to twenty-two sheets of paper plus the mailing envelope. The printout was not returned to Unisource. Rather, Carrara alleges that he threw it away.

Although no one, including Carrara and Baker, could remember or identify what was contained in the AS 400 printout, an investigation into the matter conducted by John Montgomery revealed that the printout was probably a "Customer Transaction Analysis" (CTA). A CTA contains one specific customer's purchase history, including products ordered, prices paid, and billing dates. A CTA may also contain Unisource's costs and gross trading margins, although Carrara testified that he would frequently request that these two columns be removed.

Carrara testified that he would request a CTA four or five times a year to provide to a customer for its inventory purposes, to assist a customer in obtaining a reward under various reward programs, or for "forecasting" purposes. Therefore, it would not be abnormal or improper for Carrara to receive a twenty-two page CTA on November 9, 2002. In any event, under the foregoing analysis, none of the information contained in a CTA is confidential.

7. Conclusion

In sum, it is the finding of this Court that none of the information that Unisource seeks to protect is confidential. Because the record does not show that any of the Defendants acquired confidential information through his or her employment at Unisource and subsequently tried to use that information for his or her own benefit, Unisource cannot show that its contracts with Carrara, Richard McCormick, Michael McCormick and Hetman are founded upon a "legitimate business interest." Lawrence and Allen, Inc., 226 Ill.Dec. 331, 685 N.E.2d at 443. Therefore, all four restrictive covenants are unenforceable in any event.[FN5]

> FN5. The Court notes that, if Richard McCormick's covenant not to compete was enforceable, his conduct in introducing Michael McCormick as his brother to representatives of ADM and Tate and Lyle, sitting in during Michael McCormick's meetings with those representatives, and making occasional comments during those meetings, would constitute a violation of the covenant not to compete.

Furthermore, the provisions in Unisource's employment agreements with each of the Defendants that prohibit disclosure of "confidential information" are overbroad in that they expressly cover information generally known or available in the industry.[FN6] (Pl.'s Ex.s 2-3, 5, 7-10.) *See id.; AEE-EMF, Inc. v. Passmore,* 906 S.W.2d 714, 722 (Mo.Ct.App.1995) ("Matters of general knowledge or of public knowledge in an industry cannot be appropriated by one as his secret."); *Physician Specialists in Anesthesia, P.C. v. MacNeill,* 246 Ga.App. 398, 539 S.E.2d 216, 225 (2000) ("The validity of a nondisclosure provision depends ... on two factors: (1) whether the employer is attempting to protect confidential information relating to the business, ... and (2) whether the restraint is reasonably related to the protection of the information."). Therefore, Unisource cannot rely on these provisions to prohibit the Defendants from using or disclosing the type of information at issue here.

> FN6. For instance, six of the Defendants' contracts provide that "confidential information" includes the "names, addresses and buying practices of customers, customer service requirements, ... selling processes," price lists, and suppliers. (Pl.'s Ex.s 2-3, 5, 8-10.) As discussed under section I(D) of this Order, Unisource has no proprietary interest in any of this information.

II. Illinois Trade Secrets Act

[22] The parties concede that under Illinois law, there is no apparent functional ***990** difference between "confidential information" and "trade secrets." Therefore, under the foregoing analysis, Unisource

has not shown that any of the Defendants has violated the Illinois Trade Secrets Act FN7 by disclosing or threatening to disclose any trade secrets belonging to Unisource.

FN7. To set forth a violation of the Illinois Trade Secrets Act, 765 ILCS 1065/2 *et seq.*, "a plaintiff must establish that the information at issue was (1) a trade secret; (2) misappropriated; and (3) used in the defendant's business." *Delta Med. Systems*, 265 Ill.Dec. 397, 772 N.E.2d at 780. Under section 2(d) of the Act, a trade secret is defined as follows:

> [I]nformation, including but not limited to, technical or non-technical data, a formula, pattern, compilation, program, device, method, technique, drawing, process, financial data, or list of actual or potential customers or suppliers, that:
>
> (1) is sufficiently secret to derive economic value, actual or potential, from not being generally known to other persons who can obtain economic value from its disclosure or use; and
>
> (2) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy or confidentiality.
>
> 765 ILCS 1065/2(d).

Conclusion

For the foregoing reasons, Unisource's Motion for a Preliminary Injunction [# 3-2] is DENIED. The Temporary Restraining Order entered on January 31, 2003, is hereby dissolved.

C.D.Ill.,2003.
Unisource Worldwide, Inc. v. Carrara
244 F.Supp.2d 977

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TAB 15

Court of Appeals of North Carolina.
WILMAR, INCORPORATED
v.
Leo Vander LILES.
WILMAR, INCORPORATED
v.
O. T. POLK, Jr.
No. 7126SC620.

Dec. 15, 1971.
Certiorari Denied by Supreme Court Jan. 28, 1972.

Action by employer against former employees to enforce covenant not to compete contained in employment contracts entered into between employer and employees. The Superior Court, Mecklenburg County, Frank W. Snepp, Jr., J., entered an interlocutory order restraining employees from further competition with employer, and former employees appealed. The Court of Appeals, Britt, J., held that where covenants not to compete were included in employment contracts which provided for initiation of a profit sharing plan allegedly for benefit of employees, but which was subject to amendment by employer, and which in fact was amended by employer to reduce, and for a period of two years eliminate, contributions to the plan, and employment contracts were not entered into at time employees were employed by employer and terms and conditions of employees' existing employment were not altered in any other manner, restrictive covenant not to compete was not an ancillary contract, but rather was a naked contract not to compete not protected as to enforceability by exceptions afforded ancillary contracts in restraint of trade permissible in connection with sale of a going business, a contract of employment, or a lease.

Reversed.

West Headnotes

[1] Equity 150 43

150 Equity
150I Jurisdiction, Principles, and Maxims
150I(B) Remedy at Law and Multiplicity of Suits
150k43 k. Existence of Remedy at Law and Effect in General. Most Cited Cases

While under present system the same court grants legal as well as equitable relief, this does not allow a party the option to demand either at his will; equitable relief will be granted only when legal relief is inadequate, and party must bring himself within rule by alleging and establishing facts which will warrant the equitable remedy.

[2] Contracts 95 65.5

95 Contracts
95I Requisites and Validity
95I(D) Consideration
95k65.5 k. Covenants Not to Compete. Most Cited Cases
(Formerly 95k65(2))

When employment preexists execution of employment contracts, there must be some additional consideration to employee to support his covenant not to compete.

[3] Contracts 95 116(2)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition in Trade
95k116 In General
95k116(2) k. Restriction Necessary for Protection. Most Cited Cases
(Formerly 95k16(2))

To be enforceable, a covenant not to compete must protect some substantial interest of the employer.

[4] Contracts 95 116(1)

95 Contracts
95I Requisites and Validity
95I(F) Legality of Object and of Consideration
95k115 Restraint of Trade or Competition

in Trade

95k116 In General

95k116(1) k. In General. Most Cited Cases

(Formerly 95k16(1))

Where covenants not to compete were included in employment contracts which provided for initiation of a profit sharing plan allegedly for benefit of employees, but which plan was subject to amendment by employer, and which in fact was amended by employer to reduce, and for a period of two years eliminate, contributions to the plan, and employment contracts were not entered into at time of employment and terms and conditions of employees' existing employment were not altered in any other manner, restrictive covenant not to compete was not an ancillary contract, but rather was a naked contract not to compete not protected as to enforceability by exceptions afforded ancillary contracts in restraint of trade.

***72 **279** Plaintiff instituted these two actions against defendants, former employees of plaintiff, to enforce covenants not to compete contained in employment contracts entered into between plaintiff and defendants. By agreement the cases were consolidated for hearing in the superior court and for determination in this court.

The facts pertinent to the issue raised on appeal are substantially free from dispute.

Defendants were both employed by plaintiff as salesman of its products, janitorial and automotive chemicals and supplies. They were paid on a commission basis and were assigned to sell in certain non-exclusive territories in North Carolina and Virginia. Defendant Liles became an employee of plaintiff in 1957, and defendant Polk in April 1963. Neither of defendants was asked to enter into any written agreement with plaintiff at the time they became employees. Both defendants continued to work for plaintiff without written contracts until November of 1963. On 6 November 1963 in the case of Liles, and on 7 November 1963 in the case of Polk, written employment contracts were executed with plaintiff. The contracts were similar except for the territories to be covered by defendants. Each of the contracts contained a covenant by defendants not to compete, either directly or indirectly, with plaintiff during the term of their employment or for a period of one year thereafter. The covenant was limited to the territory in which defendants worked while employed by plaintiff. The stated consideration by plaintiff for the new contracts was the initiation of a profit sharing plan for defendants and other employees to begin as of 1 December 1963. Plaintiff also agreed to reimburse the defendants for one-half of their gasoline bill for any quarter in which *73 their gross sales exceeded $9,000.00; this provision could be terminated by plaintiff at its option. There was no other change in the employment conditions or compensation of defendants.

Plaintiff instituted the profit sharing plan as agreed upon in the contracts. The plan was subject to amendment by plaintiff, but plaintiff could not disturb any contributions already made to the fund. The right to amend was exercised by plaintiff on several occasions. By two of these amendments, plaintiff reduced the minimum amount which it would contribute to the plan. Under these reductions, no contributions were made between 30 November 1967 and 30 April 1969.

Defendants continued to work for plaintiff until 1971. On 12 February 1971 defendant Polk voluntarily terminated his employment with plaintiff and on 15 February 1971 defendant Liles voluntatily terminated his employment with plaintiff.

Upon termination of their employment with plaintiff, defendants accepted positions with Palmetto Chemical Company of Cheraw, South Carolina. Palmetto was a direct competitor of plaintiff. Defendants were employed as salesman by Palmetto and serviced substantially the same territories and customers they had previously serviced for the plaintiff. As a result of their competition, plaintiff suffered a substantial decline in its sales in those areas serviced by defendants. Further pertinent facts are set forth in the opinion.

****280** On 10 March 1971, plaintiff brought these actions seeking to enforce the covenants not to compete contained in defendants' contracts. Pursuant to appropriate notice, plaintiff moved for temporary injunctions against defendants. Following a hearing the superior court made appropriate findings of fact and entered an interlocutory order restraining defendants from further competition with plaintiff.

From this order defendants appealed.

Grier, Parker, Poe, Thompson, Bernstein, Gage & Preston, by Mark R. Bernstein, Sydnor Thompson and W. Samuel Woodard, Charlotte, for plaintiff appellee.

McElwee & Hall, by John E. Hall, and W. G. Mitchell, North Wilkesboro, for defendant appellants.

***74** BRITT, Judge.

Did the trial court err in entering the temporary injunction appealed from? We hold that it did.

[1] By seeking to have defendants enjoined from certain acts, plaintiff asks the court to exercise its equitable jurisdiction. While under our present system the same court grants legal as well as equitable relief, this does not allow a party the option to demand either at his will; equitable relief will be granted only when legal relief is inadequate, and the party must bring himself within the rule by alleging and establishing facts which will warrant the equitable remedy. McIntosh, N.C. Practice and Procedure, 2d Ed., Sec. 2191.

Although the Supreme Court of North Carolina and this court have considered numerous cases involving anticompetitive covenants, our search fails to reveal any case in which either court addressed itself to a determination of whether the contract before it was, in fact, a naked contract not to compete or an ancillary contract in restraint of trade and whether a restrictive covenant not ancillary to a principal contract of employment, sale, or lease is enforceable.

In 54 Am.Jur.2d, Monopolies, Sec. 514, p. 961, it is said:

'As a general rule, an anticompetitive covenant is unenforceable unless it is ancillary or incidental to a lawful contract, even though it is supported by a consideration. A restrictive provision which might be upheld if it were incidental to some principal contract cannot be enforced if it appears to be the main purpose of the contract, and not subordinate thereto.'

In Purchasing Associates, Inc. v. Weitz, 13 N.Y.2d 267, 246 N.Y.S.2d 600, 196 N.E.2d 245 (1963) the New York Court of Appeals said:

'At one time, a covenant not to compete, basically an agreement in restraint of trade, was regarded with high disfavor by the courts and denounced as being 'against the benefit of the commonwealth'. (Citations) It later became evident, however, that there were situations in which it was not only desirable but essential that such covenants not to compete be enforced.

'Where, for instance, there is a sale of a business, involving as it does the transfer of its goodwill as a going ***75** concern, the courts will enforce an incidental covenant by the seller not to compete with the buyer after the sale. (Citations) * * * The sole limitation on the enforcibility (sic) of such a restrictive covenant is that the restraint imposed be 'reasonable,' that is, not more extensive, in terms of time and space, than is reasonably necessary to the buyer for the protection of his legitimate interest in the enjoyment of the asset bought. (Citations)

'Also enforcible (sic) is a covenant given by an employee that he will not compete with his employer when he quits his employ, and the general limitation of 'reasonableness', to which we have just ****281** referred, applies equally to such a covenant. (Citations) However, since in the case of such a covenant the element of good will, or its transfer, is not involved and since there are powerful considerations of public policy which militate against sanctioning the loss of a man's livelihood, the courts have generally displayed a much stricter attitude with respect to covenants of this type. (Citations)'

In Little Rock Towel & Linen Supply Co. v. Independent Linen Serv. Co., 237 Ark. 877, 377 S.W.2d 34 (1964) we find:

'A naked contract not to compete with another is against public policy. Shapard pard v. Lesser, 127 Ark. 590, 193 S.W. 262, 3 A.L.R. 247. Such an agreement is permissible, however, either in connection with the sale of a going business or, as here, in connection with a contract of employment. Yet even in those instances the restraint is unreasonable and void if it is greater than is required for the protection of the promisee or if it imposes an undue hardship upon the person who is restricted. Rest., Contracts, s 515, which we quoted with approval in Marshall v. Irby, 203 Ark. 795, 158 S.W.2d 693. Owing to the possibility that a person may be deprived of his livelihood the courts are less disposed to uphold restraints in contracts of employment than to uphold them in contracts of sale. Williston, Contracts (Rev.Ed.), s 1643; Banks, Covenants Not to Compete, 7 Ark.L.Rev. 35.'

In Super Maid Cook-Ware Corporation v.Hamil, 50 F.2d 830 (1931), the 5th Circuit Court of Appeals said:

***76** 'Appellant by its prayer for injunctive relief prima facie puts itself in the position of seeking, by contract, to deprive appellees of the right to earn their livelihood. Equity places upon it the burden of showing that the contract was fair, the restrictive covenants reasonable, and that they have a real relation to, and are really necessary for, the protection of appellant in the business to which the covenants are an incident. For, fundamentally, in and of themselves these covenants are in restraint of trade, and unenforceable. It is a settled principle of law that no man may, per se, contract with another that that other will not follow a calling by which he may make his livelihood. It is only when they are incidental to some contract which is reasonable in its purpose and its terms, and it is necessary to the protection of the rights of the employer under such contract, that the validity of restrictive covenants will be recognized and enforced, and then only when they are themselves reasonable, no public interests are involved, and the restriction is limited to the very point of the necessity of protecting contract rights, to which the covenant is incidental. In short, it is never the covenant itself, but the covenant in relation to the facts of the situation or contract to which it is incidental, which may be valid.

'Further, it is well settled that, while a court of equity will in proper cases issue its writ of injunction to enforce covenants of this kind, it will not do so unless the whole matter appears equitable; that is, unless it rests upon a contract which is fair in its terms, involves no imposition nor injustice, and the private interests of the employer in the subject-matter of the contract to which the restrictive covenant is incidental, requires in good faith for its protection the enforcement of the covenant. Hepworth Mfg. Co. v. Ryott (1920) 1 Ch. 1, 9 A.L.R. 1484; Samuel Stores v. Abrams, 9 A.L.R. 1450, note; Taylor Iron & Steel Co. v. Nichols, 73 N.J.Eq. 684, 69 A. 186, 24 L.R.A., N.S., 933, 133 Am.St.Rep. 753; Kinney v. Scarbrough Co., 138 Ga. 77, 74 S.E. 772, 40 L.R.A.,N.S., 473; Herbert Morris, Ltd. v. Saxelby, 1 App.Cas. 688; Clark Paper & Mfg. Co. v. Stenacher, 236 N.Y. 312, 140 N.E. 708, 29 A.L.R. 1325; Club Aluminum Co. v. Young, 263 Mass. 223, 160 N.E. 804; ****282** Mentor Co. v. Brock, 147 Minn. 407, 180 N.W. 553, 20 A.L.R. 857; Southern Properties v. Carpenter (Tex.Civ.App.) 21 S.W.2d 372, 373.'

***77** The case of Orkin Exterminating Co. v. Jones, et al., 258 N.C. 179, 128 S.E.2d 139 (1962), involved covenants not to compete set forth in original contracts of employment. Our Supreme Court held that courts of equity will enforce such a covenant not to compete if it is: (1) in writing, (2) entered into at the time and as part of the employment contract, (3) based on valuable consideration, (4) reasonable as to time and territory, (5) fair to the parties and (6) not against public policy.

Contracts in restraint of trade or commerce are condemned by statutes in North Carolina. G.S. 75-1 provides in pertinent part as follows: 'Every contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade or comerce in the State of North Carolina is hereby declared to be illegal. . . .' G.S. 75-2 provides: 'Any act, contract, combination in the form of trust, or conspiracy in restraint of trade or commerce which violates the principles of the common law is hereby declared to be in violation of s 75-1.' G.S. 75-4 provides: 'No contract or agreement hereafter made, limiting the rights of any person to do business anywhere in the State of North Carolina shall be enforceable unless such agreement is in writing duly signed by the party who agrees not to enter into any such business within such territory: Provided, nothing herein shall be construed to legalize any contract or agreement not to enter into business in the State of North Carolina, or at any point in the State of North Carolina, which contract is now illegal, or which contract is made illegal by any other section of this chapter.' These statutes were enacted by the 1913 General Assembly.

[2] In the case before us the covenants not to compete were included in contracts of employment entered into by the defendants after defendant Liles had been in plaintiff's employment for six years and defendant Polk for six months. When the employment preexists the execution of the contracts, there must be some additional consideration to the employee to support his covenant not to compete. Greene Co. v. Kelley,

261 N.C. 166, 134 S.E.2d 166 (1964).

The principles stated above must be applied as we turn to an examination of the facts in this case. As mentioned before, the contracts before us were not entered into at the time defendants were employed by plaintiff. Each contract provided for the initiation of a profit sharing plan allegedly for the benefit***78** of defendants (and other employees) and for the reimbursement of one-half of defendants' gasoline bills for any quarter in which their gross sales exceeded $9,000. In return defendants executed the covenants not to compete with plaintiff. The terms and conditions of defendants' existing employment were not altered in any other manner. Plaintiff's promise to reimburse defendants for their gasoline bills could be terminated at plaintiff's option and it is not contended that such a promise would be valid consideration to support defendants' covenants. The profit sharing plan instituted pursuant to defendants' contracts provided that plaintiff could, at any time, amend the plan so long as such amendment did not divert the corpus of the trust to a purpose other than for the benefit of members of the plan. Under this provision plaintiff did in fact alter the plan to reduce its contributions to the trust fund. These reductions had the effect of eliminating, for a period of two years, any contributions by plaintiff. Under the plan if an employee under written contract with plaintiff terminated his employment, he would not be entitled to his vested interest until three years from the date of termination. It was further provided that if the former employee competed with plaintiff during this period, he would forfeit his vested interest and it would revert to the accounts of all other participants in the plan in proportion to ****283** their share of allocable contributions for that year. It is noted that the forfeiture provision extends two years beyond the period covered by defendants' covenants not to compete. Contribution to an employee's account was based on the ratio of the employee's compensation to the total compensation of all participants in the plan. Other relevant circumstances include the fact that Mr. Jules Buxbaum is the president and sole shareholder of plaintiff corporation. As such he was paid the highest salary of any employee and therefore he was the greatest beneficiary of the profit sharing plan.

An analysis of the profit sharing plan leaves little doubt as to whether it was a consideration for defendants' covenants. The plan was drawn up by plaintiff; it was subject to amendment by plaintiff; it was amended by plaintiff to reduce, and for a period of two years eliminate, contributions to the plan; it imposed a three-year limitation on competition by former employees and the greatest benefit of the plan accrued to plaintiff's president and owner, Jules Buxbaum. We find this consideration to be illusory as to defendants. 'A consideration ***79** cannot be constituted out of something that is given and taken in the same breath-. . . .' Kadis v. Britt, 224 N.C. 154, 163, 29 S.E.2d 543, 548 (1944).

Somewhat analogous to the facts in this case is the following statement by the court in Super Maid Cook-Ware Corporation v. Hamil, Supra: 'Without guaranteeing to the defendants one day's regular work, without the obligation of the appellant to employ them or pay them anything, upon a seductive promise of the disclosure of the information upon which they may hope to build a profitable line of sales, the appellees are induced to sign a paper which, while it has the general appearance of a contract, but keeps the promise to the ear while it breaks it to the hope. Such a contract, wanting in mutuality, presenting no equitable considerations, a court of equity will not enforce. (Citations)'

[3] To be enforceable, a covenant not to compete must protect some substantial interest of the employer. We are not convinced from the evidence in this case that defendants had access to any trade secrets. Defendants were already employees of plaintiff at the time the contracts were executed. They had acquired a knowledge of plaintiff's business methods, customer list and territories prior to the execution of the contracts. The plaintiff had failed to protect his interest at the time the defendants came into his employment. By the contracts plaintiff was merely attempting to close the barn door after the horse was out.

[4] The inescapable conclusion then is that in actuality the restrictive covenant not to compete here sought to be enforced is not an ancillary contract at all. It is the main purpose of the contract and not a subordinate feature. It becomes and is, therefore, a naked contract not to compete not protected as to enforceability by the exceptions afforded ancillary contracts in restraint of trade permissible in connection with the sale of a going business, a contract of employment, or a lease.

For the reasons stated the order appealed from is

Reversed.

MORRIS and PARKER, JJ., concur.
N.C.App. 1971.
Wilmar, Inc. v. Liles
13 N.C.App. 71, 185 S.E.2d 278, 51 A.L.R.3d 816,
1972 Trade Cases P 73,870

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