

Defending Trade Secret Misappropriation Claims

The Identification of Trade Secrets

by Sid Leach
Snell & Wilmer L.L.P.

A complaint filed in court alleging misappropriation of trade secrets normally does not plead specifics concerning the particular trade secrets at issue. This is understandable; otherwise, the complaint would have to be filed under seal, and notice pleading does not require such specifics. A defendant typically obtains information identifying the trade secrets that were allegedly misappropriated through discovery. Unlike a patent case, where the metes and bounds of the claimed invention are set forth in the patent document, rarely do you find existing documentation that delineates the trade secrets with particularity.

I. The Importance of Identifying Trade Secrets

A leading treatise on trade secrets discusses the difficulty that a defendant may face in formulating defenses prior to being apprised of the details of the trade secrets at issue. (1) Once the trade secrets are identified, the defendant can undertake an investigation of whether the claimed trade secrets are generally known, whether the plaintiff has taken reasonable measures to protect the identified trade secrets, whether any of the defendant's employees had access to the trade secrets, and whether any of the trade secrets have been used by the defendant.

The importance of identifying the trade secrets cannot be overstated. Trade secret misappropriation cases can be won or lost over the identification of the trade secrets.

A. The Identification of Trade Secrets Usually Is Crucial to the Outcome of a Case

A party seeking to protect trade secrets must "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." (2) A number of cases have been decided in favor of the defendant because the plaintiff failed to specifically identify or describe the trade secrets that were allegedly misappropriated.

A recent decision by the U.S. District Court in Arizona illustrates this point. In the case of *Lexcel Solutions, Inc. v. MasterCard International Inc.* (3), the plaintiff alleged that, after several years of developing specialized simulation software for the defendants pursuant to a series of licensing agreements, the defendants terminated their contractual relationship with the plaintiff, and through reverse engineering, modified and ultimately designed replacement software, thereby exploiting the plaintiff's trade secrets. (4) The court granted summary judgment in favor of the defendants on the trade secret misappropriation claim, in part, because the plaintiff "failed to specify what information

qualifies as a trade secret." (5) A conclusory statement in an affidavit that the plaintiff's software "contains" trade secrets was found to be insufficient to avoid summary judgment. (6) In the *Lexcel* case, the trade secret claim was governed by the Uniform Trade Secrets Act, which has been enacted in at least thirty-nine states, including Arizona. (7)

The failure to identify the trade secrets has had an impact on the outcome of other cases. In the case of *Imax Corp. v. Cinema Technologies, Inc.* (8), the Ninth Circuit affirmed summary judgment on a trade secret misappropriation claim based upon the plaintiff's failure to specifically identify the alleged trade secrets. In the case of *MAI Systems Corp. v. Peak Computer, Inc.* (9), the Ninth Circuit found an affidavit insufficient because it merely stated that the plaintiff's software "contain[s] valuable trade secrets." In that case, the court reversed a summary judgment in favor of the plaintiff because the trade secrets in the software were not specifically identified. Without a specific identification of the trade secrets, the court of appeals was unable to determine whether the defendant had misappropriated them.

B. A Trade Secret Plaintiff Must Set Forth Specific Facts in Order to Avoid Summary Judgment

In a growing number of jurisdictions, the substantive law requires a plaintiff to specifically identify the alleged trade secrets. (10) Nevertheless, cases granting summary judgment against a plaintiff for failing to specifically identify the plaintiff's trade secrets are also justified by the requirement under Rule 56(e) of the Federal Rules of Civil Procedure that the party opposing a motion for summary judgment "must set forth specific facts" to show there is an issue for trial.

Conclusory assertions without substantial factual evidence are inadequate to raise a genuine issue of fact in order to avoid summary judgment. (11) In case of *Lujan v. National Wildlife Federation*, (12) the plaintiff's affidavit filed in opposition to a motion for summary judgment was ambiguous regarding whether the adversely affected lands were the ones that the plaintiff actually used. In ruling that the affidavit was insufficient, the Supreme Court said:

Rule 56(e) provides that judgment "shall be entered" against the nonmoving party unless affidavits or other evidence "set forth specific facts showing that there is a genuine issue for trial." The object of this provision is not to replace conclusory allegations of the complaint or answer with conclusory allegations of an affidavit. (13).

If a plaintiff fails to set forth such "specific facts" identifying the trade secrets that were allegedly misappropriated, the defendant should be entitled to summary judgment in its favor (assuming the plaintiff has had an opportunity for discovery).

II. Obtaining an Identification of Trade Secrets

Until the defendant knows what the alleged trade secrets are, the defendant is to some extent shooting in the dark. A party defending against a trade secret

misappropriation claim should serve an interrogatory requesting the plaintiff to describe in full and complete detail all of plaintiff's trade secrets that defendant allegedly misappropriated, or to which defendant has had access, or that are the subject of the allegations of the complaint. In most cases, an interrogatory is the best way to obtain an identification of the trade secrets at issue.

In some cases, courts have entered protective orders against discovery from the defendant until the plaintiff identified the trade secrets that were allegedly misappropriated. (14) The identification of trade secrets may be an iterative process. As the plaintiff takes more discovery, the plaintiff may be better able to identify the trade secrets that have allegedly been used. At some point in the litigation, however, there needs to be a final identification of trade secrets that does not change and upon which the parties will go to trial.

III. Conclusion

At least one writer has recommended that a business periodically document its trade secrets, even in the absence of any litigation. (15) Such an exercise is not practical for most businesses. However, should litigation ever become necessary, the precise formulation of the trade secrets at issue in a case takes on great importance, because it typically shapes the determinative issues for the remainder of the litigation. Because of the importance of this exercise, it is often helpful to involve counsel in drafting the identification of trade secrets who also has a technical background.

Footnotes:

1. Roger M. Milgrim, MILGRIM ON TRADE SECRETS § 16.01[5] (vol. 4 2004).
2. *Whyte v. Schlage Lock Co.*, 101 Cal. App.4th 1443, 1453, 125 Cal. Rptr. 2d 277, 286 (2002), *quoting from Diodes, Inc. v. Franzen*, 260 Cal. App.2d 244, 253, 67 Cal. Rptr. 19 (1968).
3. *Lexcel Solutions, Inc. v. MasterCard International Inc., et al.*, No. CV-03-1454-PHX-JAT (D. Ariz. Sept. 9, 2005).
4. *Id.*, slip op. at 1-2.
5. *Id.*, slip op. at 11.
6. *Id.*, slip op. at 12.
7. The court applied Missouri law. Mo. Rev. Stat. § 417.453(4) (2004). Arizona has also enacted the Uniform Trade Secrets Act, and the relevant provisions of the Arizona statute are identical to the Missouri statute. A.R.S. § 44-401(4) (2004). Some states, like California, have enacted a slightly modified version of the statute. *Compare* Cal. Civ. Code, § 3426.1 (d) (2002).

8. *Imax Corp. v. Cinema Technologies, Inc.*, 152 F.3d 1161, 1164-68 (9th Cir. 1998).
9. *MAI Systems Corp. v. Peak Computer, Inc.*, 991 F.2d 511, 522 (9th Cir. 1993), *cert. dismissed*, 510 U.S. 1033 (1994).
10. *E.g., Universal Analytics Inc. v. MacNeal-Schwendler Corp.*, 707 F. Supp. 1170, 1177 (C.D. Cal. 1989)(plaintiff failed to inform defendant or the court "precisely which trade secret it alleges was misappropriated"), *aff'd*, 914 F.2d 1256 (9th Cir. 1990); *Khazai v. Watlow Electric Manufacturing Co.*, 201 F. Supp.2d 967, 974 (E.D. Mo. 2001) ("the subject matter of the information to be protected must be specifically described"); *Litton Systems Inc. v. Sundstrand Corp.*, 750 F.2d 952, 957-59 (Fed. Cir. 1984) (affirmed denial of preliminary injunction where trade secrets insufficiently identified).
11. *Collins v. Longview Fibre Co.*, 63 F.3d 828, 834 (9th Cir. 1995), *cert. denied*, 516 U.S. 1048 (1996); *Drake v. Minnesota Mining & Manufacturing Co.*, 134 F.3d 878, 887 (7th Cir. 1998) ("Rule 56 demands something more specific than the bald assertion of the general truth of a particular matter[;] rather it requires affidavits that cite specific concrete facts establishing the existence of the truth of the matter asserted.").
12. *Lujan v. National Wildlife Federation*, 497 U.S. 871 (1990).
13. 497 U.S. at 888-89 (citations omitted).
14. *E.g., Automed Techs. v. Eller*, 160 F. Supp.2d 915, 925-26 (N.D. Ill. 2001).
15. James H.A. Pooley, TRADE SECRETS 7-8 (1989).