Trade Secrets and Noncompete Blog

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A Mere Good Faith "Suspicion" That Defendants Misappropriated Trade Secrets Is Insufficient To Establish Plaintiff Did Not Engage In Objective Bad Faith

The commencement and continued prosecution of a misappropriation of trade secrets action without objective evidence of actual misappropriation can result in the imposition of attorneys' fees against the plaintiff if it does not prevail on that cause of action. On April 17, 2012, we blogged about this issue in connection with a malicious prosecution action that was filed against Latham & Watkins after the unsuccessful prosecution of a trade secrets action on behalf of a client.

On July 11, 2012, in *SASCO v. Rosendin Electric, Inc.*, 2012 WL 2826955 (Cal.App. 4 Dist.), the California Court of Appeal, Fourth Appellate District, provided more clarity on this issue and affirmed the trial court's order awarding defendants almost $485,000 in attorneys' fees and costs pursuant to California Civil Code § 3426.4 (the Uniform Trade Secrets Act). SASCO sued Rosendin Electric, Inc, another licensed electrical contractor and three individual defendants for misappropriation of trade secrets, among other things. SASCO identified a proprietary computer program to be one of its trade secrets. SASCO also alleged that the individual defendants contacted a third-party that had put out a competitive bid and encouraged it to ignore SASCO's bid and to award the job to Rosendin. After the parties engaged in what the court described as "fierce discovery battles," defendants filed a motion for summary judgment and after obtaining a continuance of the hearing to conduct additional discovery, SASCO voluntarily dismissed the action without opposing the motion for summary judgment. Defendants moved for attorneys' fees.

The trial court accepted for the sake of argument that SASCO's computer program was a trade secret. The court concluded, however, there was no evidence of misappropriation and that SASCO had sued defendants based on the suspicion that they must have misappropriated trade secrets because the individual defendants went to work for a competitor, which subsequently secured a contract for which both companies were competing. The trial court concluded that plaintiff engaged in bad faith pursuant to Civil Code § 3426.4, which consisted of both objective speciousness and subjective bad faith.

The appellate court affirmed and agreed that the claim was objectively specious because there was no evidence to support the claim. The plaintiff argued it should not be required to show actual evidence of misappropriation because the case was dismissed before trial and defendants allegedly withheld discovery. The plaintiff argued that the trial court should have looked to Code of Civil Procedure section 128.7 (which is comparable to Fed. R. Civ. P. Rule 11) which would preclude a finding of objective speciousness if the factual contentions were "likely to have evidentiary support, or …are likely to have evidentiary support after a reasonable opportunity for further investigation or discovery." The appellate court refused to apply a standard that applied to a general pleading statute.

The appellate court also agreed with the trial court that continuing to prosecute the action without evidence of actual misappropriation constituted subjective bad faith.

Based on this decision, an employer has to be very careful before it commences a misappropriation of trade secrets action -- even if the departing employee was entrusted with trade secrets and that employee went to work for a competitor. If the employer is presented with evidence that no misappropriation occurred and continues to prosecute the case and loses or dismisses the case, the defendant's application for attorney's fees may be granted.

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