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## Statute of Limitations and Trade Secret Claims: Some Answers and Some Questions

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At a time when many significant technological advances are driven by the ingenuity of a relatively small group of highly skilled (and highly mobile) employees, the prospect that a technology company will find itself on one or the other side of a claim of trade secret misappropriation has become a settled feature in the strategic landscape. Any time such an employee leaves one employer to join another working on competing product lines, there is some risk that the first employer's trade secrets will "migrate" with the employee and be put to improper use, with or without the second employer's active encouragement or even knowledge. The result is a kind of foreboding: The holder of a trade secret must take adequate measures to protect its property, but it generally cannot afford to let loose the cannons of litigation without some concrete evidence that its trade secrets have actually been misappropriated. Similar uncertainties hang over the heads of the new employer for, with every strategic hire, it knows there is a risk that a claim of trade secret misappropriation may eventually follow, possibly at a time chosen by the competitor based solely on tactical, business considerations. Faced with these uncertainties, both sides often adopt an uneasy policy of wait and see.

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Understanding how the courts will apply the statute of limitations for claims of trade secret misappropriation is, thus, critically important for potential plaintiffs and defendants alike. Plaintiffs must know how long they can safely wait before they must choose to undertake costly and disruptive litigation or permanently relinquish significant rights. For purposes of their own business planning, potential defendants need some sense of how long they must continue to look over their shoulders and when they are free to focus on the future rather than the past.

This article reviews the statute of limitations provision in § 6 of the Uniform Trade Secrets Act (UTSA) and discusses how that provision has been applied in the courts of California, most notably, in the California Supreme Court's 2002 decision in *Cadence Design Sys., Inc. v. Avant! Corp.*<sup>1</sup> and most recently in the California court of appeal's May 30, 2008, ruling in *Cypress Semiconductor Corp. v. Superior Court*.<sup>2</sup> These opinions provide some guidance on how the UTSA's statute of limitations will be applied in various settings, principally by showing how the courts have applied the single claim principle and the discovery rule, both of which are set forth in § 6. Nevertheless, these cases still leave many important questions unanswered. For the holders of trade secrets the pragmatic advice, perhaps now more than ever, is to be extremely diligent in investigating any suspected instances of misappropriation and, when misappropriation appears to have occurred, in taking appropriate action to enforce their rights. Failure to do so may result in the permanent loss of the right to prevent acts of continuing misappropriation.

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## The Single Claim Principle and the Discovery Rule

Before the adoption of the UTSA in California and elsewhere, much of the uncertainty over when the clock begins to run on a claim of trade secret misappropriation turned on divided opinion as to how the statute of limitations applied when a defendant continued to use a trade secret. One view held that each instance in which a defendant misused a given secret gave rise to a new cause of action. Another view was that each such instance was subsumed with a “single claim” that began to run, once and for all, when the secret was first misappropriated. Common law supported both of these divergent views, thus creating uncertainty on the question of when the clock on a plaintiff’s claim begins to run. In *Monolith Portland Midwest Co. v. Kaiser Aluminum & Chem. Corp.*,<sup>3</sup> the Court of Appeals for the Ninth Circuit ruled that California’s statute of limitations<sup>4</sup> began to run when the defendant first misused or improperly disclosed plaintiff’s trade secret. The court therefore barred plaintiff’s claim for trade secret misappropriation despite plaintiff’s contention that the tort was continuing.<sup>5</sup> The court of appeals explained, “California does not treat trade secrets as if they were property. It is the confidential relationship between the parties at the time the secret is disclosed that is protected. . . . The fabric of the relationship once rent is not torn anew with each added use or disclosure.”<sup>6</sup>

In so ruling, the Ninth Circuit rejected the position of the Court of Appeals for the District of Columbia Circuit, which had previously ruled in *Underwater Storage, Inc. v. U.S. Rubber Company* that a plaintiff could recover for continued misuse of a trade secret that occurred within the statutory period even though the initial misappropriation occurred more than three years before plaintiff filed a complaint.<sup>7</sup> According to the court in *Underwater Storage*, misappropriation of a trade secret is a continuing tort, and the period set by the statute of limitations starts over with each new misuse or disclosure.<sup>8</sup>

The drafters of the UTSA, who sought to harmonize the definition of trade secret misappropriation and provide a single statute of limitations for the various common law theories of recovery, recognized the split in authority presented by *Monolith* and *Underwater Storage Devices*.<sup>9</sup> The UTSA follows *Monolith* by providing that a continuing misappropriation constitutes a single claim,<sup>10</sup> but it rejects the common law rule set forth in *Monolith* that the limitations period begins to run when the misappropriation first occurs.<sup>11</sup> Instead, the UTSA adopts the “discovery rule.” The statute of limitations set forth at § 6 of the UTSA reads:

An action for misappropriation must be brought within three years after the misappropriation is discovered or by the exercise of reasonable diligence should have been discovered. For the purposes of this section, a continuing misappropriation constitutes a single claim.<sup>12</sup>

Perhaps the best indication of the policy rationale behind this provision (and the best indicator of what the drafters meant when they referred to claims that “should have been discovered by the exercise of reasonable diligence”) comes from a statement in the official comment to § 6:

This Act rejects a continuing wrong approach to the statute of limitations but delays the commencement of the limitation period until an aggrieved person discovers or reasonably should have discovered the existence of misappropriation. If objectively reasonable notice of misappropriation exists, three years is sufficient time to indicate one’s legal rights.<sup>13</sup>

On its face, the comment confirms that a principal goal of § 6 was to overrule the continuing misappropriation doctrine (with the foreseeable practical consequence of foreclosing many claims that might otherwise have been pursued). At the same time, the drafters included actual or constructive *discovery* of misappropriation as the triggering event for the statute of limitations in order to mitigate the harsh result that a claim could become time barred before the would-be plaintiff had any reasonable way to know that a misappropriation had occurred.<sup>14</sup> The thrust of this new formulation was consistent with the basic purpose of statutes of limitations generally: “to prevent the assertion of stale claims by plaintiffs who have failed to file their action until evidence is no longer fresh and witnesses are no longer available.”<sup>15</sup> In effect, the drafters required that, once objectively reasonable evidence of misappropriation became available, from witnesses or otherwise, the plaintiff would be required to bring suit within three years; the plaintiff could not extend the limitations period for a claim based on a single act of theft merely by pointing to the defendant’s subsequent and continuing misuse of the secret. This core rationale and how it should apply in the run-of-the-mill case are easy to understand. How the single claim principle and the discovery rule should be applied in less typical settings is less clear. Recently, some degree of clarification has come from the California courts.

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### ***Cadence Design Sys., Inc. v. Avant! Corp.: The California Supreme Court Applies the Single Claim Principle***

California adopted the UTSA, including the exact language of the statute of limitations, in 1984.<sup>16</sup> The California Supreme Court first interpreted § 6 of the UTSA in 2002, in *Cadence Design Sys., Inc. v. Avant! Corp.*, on request for certification from the Ninth Circuit. Although the court's decision turned on statutory interpretation of § 6, *Cadence* was not really a statute of limitations case.<sup>17</sup> In *Cadence*, the parties disputed whether a 1994 release agreement between the parties, which released all claims that they may have had against each other at the time, including "claims which the parties do not know or suspect to exist," barred Cadence's claims for misappropriation of trade secrets based on Avant!'s alleged copying of Cadence's source code in 1991.<sup>18</sup> Cadence alleged that it had discovered the copying in 1995 and that misuse of the source code had continued after the date of the 1994 release agreement and, therefore, that the claim on which Cadence was suing had not yet existed in 1994 and was not affected by the release agreement.

Avant! naturally disagreed, arguing that the 1994 release barred claims for any subsequent continuing use or disclosure of trade secrets allegedly misappropriated before the release was entered.<sup>19</sup> Avant! argued that the UTSA codified the California common law rule set forth in *Monolith*, that a claim for misappropriation of trade secrets arises only once, when the initial misappropriation occurs.<sup>20</sup> Pointing to the UTSA statute of limitations, which defines continuing misappropriation as a single claim,<sup>21</sup> Avant! asserted that both California common law and the UTSA rejected the notion of a trade secret as a kind of property that is newly damaged by each misuse.<sup>22</sup>

In response, Cadence contended that the UTSA had changed the common law view set forth in *Monolith* and treated trade secrets as property by, for example, defining misappropriation of a trade secret to include knowing, unauthorized use of a trade secret even when the defendant breached no confidential relationship with the owner.<sup>23</sup> Cadence further argued that the single claim rule set forth in § 6 applied solely to the statute of limitations and could not be generalized into a rule about whether future wrongdoing could be covered by an earlier release.<sup>24</sup>

Relying heavily on the language of § 6, the court agreed with Avant! that the single claim rule could not be restricted to questions about the statute of limitations. The court adopted a broad application of the single claim principle for all purposes related to litigation.<sup>25</sup> Significantly, however, the court did not accept Avant!'s

argument that California had rejected the treatment of trade secrets as a form of property.<sup>26</sup> Citing California Penal Code § 499c, which states that trade secrets constitute goods, chattels, materials, and property, the court wrote that trade secrets are "indisputab[ly]" a form of property.<sup>27</sup> Without explaining the significance of that point, the court simply noted that the nature of the property interest and the means for vindicating the interest are subject to state law, including the definitions set forth in the UTSA.<sup>28</sup>

The court also considered how its ruling squared with *PMC, Inc. v. Kadisha*, an earlier court of appeal decision holding that an act of continuing misappropriation might constitute more than one claim when multiple defendants were involved.<sup>29</sup> Although the Supreme Court stopped short of expressly approving the holding in *Kadisha*, it stressed that *Kadisha* was not inconsistent with the *Cadence* ruling:

[*Kadisha*] holds only that there may be separate claims of continuing misappropriation among different defendants, with differing dates of accrual and types of tortious conduct—some defendants liable for initial misappropriation of the trade secret, others only for later continuing use. This holding does not conflict with our conclusion that there is only a single UTSA claim against a single defendant appropriating a single plaintiff's trade secret.<sup>30</sup>

These two points—that trade secrets constitute property that can be protected beyond any particular confidential relationship and that multiple wrongdoers might be subject to multiple claims, even if the same trade secret were involved—have significant implications for how the courts should apply the single claim rule and the statute of limitations in future cases. They also raise important questions for how potential plaintiffs and defendants should evaluate possible trade secret claims.

### ***Cypress Semiconductor Corp. v. Superior Court: The California Court of Appeal Clarifies the Single Claim Principle and the Discovery Rule***

The most recent significant decision to apply the reasoning in *Cadence* came in *Cypress Semiconductor Corp. v. Superior Court*, decided on May 30, 2008.<sup>31</sup> Unlike *Cadence*, *Cypress* was a straightforward statute of limitations case, and unlike *Cadence*, it directly addressed the question how the single claim principle should apply to circumstances involving multiple potential defendants.<sup>32</sup> In answering that question, the *Cypress*

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court also provided an important formulation of how the discovery rule should be applied.<sup>33</sup>

The facts in *Cypress* are as follows. In 2000, Silvaco sued Circuit Systems, Inc. (CSI) for misappropriating Silvaco's trade secrets and incorporating them into CSI's electronic design automation (EDA) program, DynaSpice. Then, in a stipulated judgment in 2003, CSI admitted that its DynaSpice program incorporated Silvaco's trade secrets.<sup>34</sup> Before the stipulated judgment, CSI had sold its DynaSpice technology to Cypress. In its 2004 complaint against Cypress, Silvaco alleged that Cypress had refused to stop using DynaSpice after being notified in 2003 that the program contained Silvaco's trade secrets.<sup>35</sup>

Cypress asserted a statute-of-limitations defense.<sup>36</sup> Cypress argued that its use of DynaSpice was a continuation of CSI's initial misappropriation; therefore, under the single claim rule of § 6, the statute of limitations on Silvaco's claim against Cypress was triggered when Silvaco discovered, or reasonably could have discovered, CSI's misappropriation.<sup>37</sup> Cypress pointed to *Monolith* for the position that, under California law, trade secret protection is based on obligations associated with confidential relationships rather than protection of a property interest.<sup>38</sup> Following that line of reasoning, according to Cypress, Silvaco's discovery in 2000 of CSI's breach of the confidential relationship triggered the statute of limitations on all misappropriations flowing from that breach, including the subsequent continuing use of the trade secret by Cypress.<sup>39</sup>

Silvaco asked the trial court to overrule Cypress's statute-of-limitations defense as a matter of law.<sup>40</sup> Silvaco argued that its claim against Cypress did not accrue until 2003, which (as was conceded) was the first time that Cypress actually learned that DynaSpice contained Silvaco's trade secrets. To establish a claim for misappropriation of a trade secret, a plaintiff must show that the defendant actually "knows or has reason to know" that the trade secret was acquired by improper means or by a person with a duty to maintain its secrecy.<sup>41</sup> Hence, Silvaco reasoned, the claim against Cypress could not have accrued, and the statute of limitations could not have begun to run, until 2003.<sup>42</sup> The trial court granted Silvaco's request to exclude evidence relating to the statute-of-limitations defense, holding that the statute could not have begun to run until all the elements of the claim were present.<sup>43</sup>

The court of appeal found flaws in both sides' positions. First, the court rejected Cypress' argument that the statute of limitations is triggered as to claims against all potential defendants upon discovery of the initial misappropriation by an original wrongdoer.<sup>44</sup> The

court held that such a rule would allow "malevolent" third parties to "lie low" until the limitations period expires and then to use another's trade secrets with impunity.<sup>45</sup> In addition, the court, echoing *Cadence*, pointed out that UTSA *did not* reject the view that trade secrets are property interests.<sup>46</sup> If it had, plaintiffs could never assert claims against third parties who had no confidential relationship with the plaintiff but who knew that the trade secret was acquired by improper means or by accident or mistake.<sup>47</sup> Finally, the court cited the explicit statement in *Cadence* that "an act of continuing misappropriation may be said to constitute more than one claim . . . when multiple defendants are involved."<sup>48</sup>

Based on these considerations, the court held:

Cypress's acquisition and use of the trade secrets was a consequence of CSI's misappropriation and, to that extent, it was a continuation of the injury caused by CSI's initial misappropriation. But Silvaco does not allege that Cypress was involved in CSI's misappropriation and Silvaco seeks damages arising only from Cypress's use of the software after it learned of the original misappropriation. Under these circumstances, if Silvaco has a claim for misappropriation against Cypress, it is a separate claim with its own limitations period. Any other interpretation of the law would lead to the absurd consequence of allowing a third-party defendant like Cypress to engage in its own misappropriation without risk of suit so long as it waited for the three years to run on the original misdeed.<sup>49</sup>

After concluding that subsequent acts of misappropriation by a separate defendant can give rise to a separate claim with its own limitations period, the court next considered when that period began to run on Silvaco's claim against Cypress.<sup>50</sup> Here, the court rejected Silvaco's argument (and the trial court's conclusion) that the cause of action did not accrue (and thus that the statute of limitations did not begin to run) until Cypress had the requisite knowledge that the software it was using contained misappropriated trade secrets.<sup>51</sup> Although recognizing that Silvaco's analysis seemed "logical enough," the court concluded that it was based on a false premise, namely, that a statute of limitations begins running "only when a plaintiff can unassailably establish a legal claim for trade secret misappropriation."<sup>52</sup> Quoting a 1993 US district court opinion, *Intermedics, Inc. v. Ventritex, Inc.*, the court stated that "[a]ccrual does not wait until a plaintiff is in a position to present evidence which will (regardless of

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what evidence the defense musters) establish facts that make liability a legal certainty.”<sup>53</sup> From this starting point, the court went on to formulate its own gloss on the discovery rule of § 6.

The court began by observing that, “since a cause of action for misappropriation incorporates an element of knowledge on the part of the defendant, the trial court was correct in deciding that Cypress’s knowledge was one of the elements necessary to the cause of action.”<sup>54</sup> Then the court went on to say that:

Where the trial court went astray was in its focus upon Cypress’s actual innocent mental state prior to August 2003. That focus was, in effect, an assessment of the merits of Silvaco’s claim against Cypress, not a determination of when Silvaco should have suspected that it had been injured by a type of wrongdoing.

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The proper focus, for purposes of the running of the statute of limitations, is not upon the defendant’s actual state of mind but upon the plaintiff’s suspicions. Indeed, a defendant’s bad faith is often something a plaintiff cannot prove directly. In many cases a plaintiff must allege the defendant’s tortious state of mind on information and belief. Certainly that plaintiff should not be expected to wait until he or she has direct proof of the defendant’s mental state before filing the lawsuit. The plaintiff’s subsequent inability to prove the requisite mental state means that the plaintiff cannot prevail on the merits of the claim but it does not retroactively affect the running of the statute of limitations.

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In this case, therefore, the statute began to run when Silvaco had any reason to suspect that the CSI customers knew or should have known that they had acquired Silvaco’s trade secrets.

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Section 3426.6 states that “An action for misappropriation must be brought within three years after *the misappropriation.*” (Italics added.) As we have explained above, the misappropriation that triggers the running of the statute is that which the plaintiff suspects, not that which may or may not actually exist.<sup>55</sup>

Read literally, some of these statements are puzzling. Among other things, the court seems to suggest that the statute of limitations on a claim for trade secret misappropriation can begin to run even before the would-be defendant has actually engaged in the misconduct that gives rise to liability, that is, using the plaintiff’s trade secret with the requisite culpable state of mind. Pushed to the limit, such a rule would clearly lead to absurd results. One can imagine a situation in which a would-be plaintiff has some reason to “suspect” that a potential defendant is knowingly misusing the plaintiff’s trade secrets, even though the potential defendant actually has not done so and will not do so for several years. Under the formulation used in *Cypress*, the statute could elapse before the tort was ever committed.<sup>56</sup>

Yet, whatever its questionable logic, the harsh consequences of this formulation are probably more theoretical than real. In practice, when the holder of a trade secret learns facts that lead it to believe that its trade secret has been consciously misappropriated, it has a strong motivation to pursue its remedies or, at a minimum, express its concerns promptly with instructions to cease and desist. Even if the would-be defendant had earlier lacked the actual mental state to support liability, it will have the requisite mental state after such notice and could successfully be pursued for any subsequent misuse. By starting the clock on the plaintiff’s claim as soon as the plaintiff has reason to suspect that such a claim exists, *Cypress* aggressively promotes the underlying purpose of any statute of limitations: to motivate plaintiffs to bring their claims before evidence becomes stale and memories fade.<sup>57</sup>

A second feature of the *Cypress* court’s formulation may have more practical significance. The court suggests that the statute of limitations begins to run as soon as the prospective plaintiff has “any reason to suspect” that its trade secret has been misappropriated.<sup>58</sup> How the court actually dealt with the facts in *Cypress* indicates how this any-reason-to-suspect standard should be interpreted.

In *Cypress*, the record already reflected that, as early as 2003, there had been reports in the trade press and on the Internet publicizing Silvaco’s claims against CSI. Silvaco knew CSI had customers that may have purchased the DynaSpice technology, and Silvaco obviously had some reason to suspect that, through the public reports, those customers had learned that DynaSpice might contain Silvaco’s trade secrets.<sup>59</sup> Despite those facts, the court did not conclude that its any-reason-to-suspect standard had been satisfied.<sup>60</sup> Instead, the court simply concluded that, like most reasonableness assessments, whether or not Silvaco had sufficient reasons to suspect Cypress’s knowing misappropriation was a

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question for the jury.<sup>61</sup> Ultimately, for the statute to be triggered, the evidence must be such that the plaintiff's "suspicions" are, in the words of the official comment to § 6, "objectively reasonable."<sup>62</sup>

### **Questions Left Open After *Cadence* and *Cypress***

The recent decision in *Cypress* expands on the jurisprudence already developed in *Cadence*. First, applying the single claim principle, *Cypress* firmly held what *Cadence* merely suggested: After an initial act of misappropriation by an original wrongdoer, a new statutory limitations period begins to run for any subsequent tortfeasor who had not been involved in the initial misappropriation but who thereafter knowingly misuses the earlier misappropriated trade secret.<sup>63</sup> Second, applying the discovery rule, *Cypress* suggests that, for any given act of misappropriation, the statute of limitations begins to run as soon as the would-be plaintiff has a reasonable basis to "suspect" that its trade secret has been misappropriated. In other words, as soon as it has a reasonable basis to suspect that the would-be defendant has used the trade secret with a culpable mental state.<sup>64</sup>

Yet, these conclusions leave many important practical questions unanswered. First and most obviously, *Cypress* says little about the quality or quantity of evidence that will give rise to a reasonable suspicion of misappropriation or the proactive steps that a plaintiff must take to uncover such wrongdoing. Nor does *Cypress* give clear answers on how the single claim and discovery rules will be applied to other commonly occurring fact patterns, such as when a single tortfeasor misappropriates multiple different trade secrets from the same plaintiff or when a second and subsequent tortfeasor begins to take part in the misappropriation earlier perpetrated by a related entity. Still, the rationales articulated in both *Cypress* and *Cadence* provide some hints as to how the courts may handle these questions.

### **Assessing Whether a Plaintiff Has Reason to Suspect Misappropriation**

The *Cypress* court found that the record before it was insufficient to determine, as a matter of law, when the statutory period began to run.<sup>65</sup> *Cypress* formulated the question for the jury as whether the plaintiff had "any reason to suspect" that a misappropriation had occurred.<sup>66</sup> But what facts will be deemed sufficient to give a plaintiff reason to suspect that a misappropriation has taken place?

To those who need to answer this important question, *Cypress* offers little guidance other than confirming that a finder of fact may properly consider publicly available information in determining whether a trade

secret owner had a reason to suspect misappropriation, and this appears to be so, whether or not the owner of the trade secret ever actually read such information. In this respect, *Cypress* is consistent with other decisions holding that a plaintiff may be charged with knowing facts that would have been learned through a reasonably diligent investigation.<sup>67</sup> Under *Cypress*, if such facts (garnered from publicly available sources or elsewhere) would have created a reasonable suspicion of misappropriation, the discovery test has been satisfied.<sup>68</sup> Whether such information would give rise to reasonable suspicion is typically a question for the jury.

*Cypress's* treatment of the discovery rule is not unlike that of the District of Columbia Court of Appeals in its January 2008 decision in *New Media Strategies, Inc. v. Pulpfree, Inc.*<sup>69</sup> There, the court of appeals reversed the lower court's grant of summary judgment that the USTA statute of limitations barred New Media's claim for misappropriation of trade secrets.<sup>70</sup> New Media had provided its business plan, which apparently included New Media's trade secrets, to Pulpfree in connection with a possible acquisition by New Media of Pulpfree's software.<sup>71</sup> The lower court ruled that New Media could have discovered the alleged misappropriation by reasonable diligence after Pulpfree indicated in email correspondence to New Media and on its Web site that it was shifting its business to a new model that New Media should have recognized as similar to its own business.<sup>72</sup> The court of appeals reversed, explaining that Pulpfree's characterizations of its business were too vague to say, as a matter of law, that New Media should have recognized that Pulpfree had begun to compete with New Media.<sup>73</sup> In addition, testimony by New Media's director that he did not know of Pulpfree's new Web site until three years after it was published created a genuine issue of material fact as to New Media's knowledge of Pulpfree's alleged misappropriation.<sup>74</sup> In short, a plaintiff's knowledge that a defendant possessed its trade secret and the availability on the Internet of information suggesting that the defendant was seeking to compete with the plaintiff were insufficient to hold, as a matter of law, that the statute of limitations was triggered. The question was for the jury.

In contrast, given *Cypress's* emphasis on triggering the statute of limitations as soon as the plaintiff has "any reason to suspect" misappropriation, courts following *Cypress* could react differently when there is evidence that a would-be plaintiff had actual suspicion but nevertheless delayed bringing suit. Under those circumstances, other courts have held, as a matter of law, that the statute of limitations begins to run when the would-be plaintiff expresses actual suspicions, either in internal discussions or in communications with

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the potential defendant.<sup>75</sup> The reasoning here appears straightforward; if the evidence in hand actually raised suspicions of misappropriation, it is hard to imagine that any reasonable jury could conclude the plaintiff lacked a “reason to suspect” the wrongdoing.

However straightforward it may seem, the practical upshot of this approach is significant. Many trade secret holders, particularly in the technology sector, harbor generalized concerns about ongoing misappropriation of their trade secrets. When those generalized concerns become reasonably articulable, for example, when company insiders voice concerns about specific trade secrets possibly having been misappropriated by an identified tortfeasor, there is a risk that a court could conclude, as a matter of law, that at that point the plaintiff had sufficient “reason to suspect” the misappropriation to trigger the statute of limitations. Prudence, therefore, dictates that, once a trade secret holder actually begins to suspect misappropriation, it must act quickly to investigate. Such investigation would allow a trade secret holder to document the information suggesting that misappropriation may have occurred and, if necessary, assert its claims. A prolonged policy of wait and see could prove fatal.

### **Applying the Single Claim Rule of *Cadence* to Misappropriations Involving Separate but Closely Connected Defendants**

In *Cypress*, the defendant had purchased a license to the product containing the misappropriated trade secret (apparently in good faith) and then continued to use it even after being instructed to cease and desist.<sup>76</sup> By its terms, *Cypress* addressed application of the UTSA statute of limitations when the defendant is “a third party who was uninvolved in the original misappropriation.”<sup>77</sup> The *Cypress* ruling therefore leaves open the question of whether the result would have been different if there had been a closer relationship between the first tortfeasor and the second. For example, rather than purchasing a license from the party that initially misappropriated the trade secret and then using that secret in the second tortfeasor’s own independent business, the second tortfeasor may instead simply be a new officer or director of the original tortfeasor, and the second tortfeasor’s only misconduct may consist in continuing the misappropriation already begun. Under those circumstances, does the arrival of a new officer or director at the original tortfeasor revive the plaintiff’s otherwise untimely claims?

This is a significant practical question in light of *PMC, Inc. v. Kadisha*, a decision that preceded *Cadence* but which *Cypress* cited with approval on other grounds.<sup>78</sup> There, the California court of appeal held that officers, directors, and shareholders of a corporation could be

personally liable for allowing the continued misuse of a trade secret misappropriated by the corporation before their involvement with the corporation began.<sup>79</sup> Specifically, the court held that the newly arrived officers and director could be independently liable under UTSA if they used, “through the corporation,” trade secrets that they knew or should have known to have been misappropriated.<sup>80</sup> The court rejected the defendants’ contention that they could not have participated in the trade secret misappropriation because the alleged misappropriation had occurred before they joined the company, explaining that continuing use of improperly acquired trade secrets is also misappropriation.<sup>81</sup> That court was not faced with the question whether the defendants’ independent liability constituted a separate claim for purposes of UTSA’s statute of limitations.<sup>82</sup>

Following *Cypress*, and in view of *PMC*’s rule that officers, directors, and shareholders may be independently liable for allowing misappropriation to continue, there is a possibility that subsequent courts will conclude that misappropriation claims against officers, directors, or shareholders accrue separately from the claim against their companies and, therefore, potentially have a separate limitations period. Such a conclusion, though understandable at a formalistic level, may not be consistent with the underlying policies of § 6.

The *Cypress* court’s ruling that continuing misappropriations by separate defendants give rise to separate claims with separate limitations periods was made in a context in which the new defendant had acquired the trade secret through an arm’s length relationship with the original tortfeasor and thereafter used the secrets in its own business, for its own profits, and in ways that may have threatened the plaintiff far differently from the original misuse.<sup>83</sup> Under those circumstances, the evidence upon which the plaintiff would rely to fix liability on the new tortfeasor (and the considerations motivating the plaintiff to pursue the new claims) might be considerably different and far more recent than those relating to the original tortfeasor. Thus, it made perfect sense for *Cypress* to permit a second three-year period in which to bring those new claims.

The rationale, however, becomes less forceful when the new defendant is more closely associated with the company that originally misappropriated the trade secret and when the new defendant’s misconduct consists in maintaining the *status quo* regarding an act of continuing misappropriation. In that situation, it makes little sense for a personnel change at the company improperly using the trade secret to revive a previously time-barred claim. After all, the new officer or director is likely to be indemnified by the company and will thus pass the economic consequences of the litigation

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(and any liability determination) on to the very same company that had previously become immune. What is more, in making its case, the plaintiff will have to rely overwhelmingly on the same stale evidence that it failed to use against the company when the misappropriation was initially discovered. On such facts, permitting a second bite at the apple would defeat the underlying purposes of § 6.

Whatever the merits or disadvantages of such a rule, if courts ultimately conclude that *Cypress* requires a separate statute of limitations for claims against officers, directors, or owners who join a company that is already engaging in continuing use of a misappropriated trade secret, such a rule could provide a way for plaintiffs to mitigate some of the harm from failing to timely assert a claim against the company itself. Nevertheless, obtaining satisfactory remedies may be difficult, since effective injunctive relief may be unavailable without the company itself as a defendant. What is more, as noted in the *Cypress* opinion, a failure of a trade secret owner to take prompt action to stop misappropriation may lead to the complete loss of the trade secret's protected status.<sup>84</sup>

### **Applying the Single Claim Rule of *Cadence* to Misappropriation of Multiple Trade Secrets by a Single Defendant**

Another question left open by both *Cadence* and *Cypress* concerns whether, under the single claim rule, the theft of multiple trade secrets by a single defendant constitutes a single claim or multiple distinct claims. Is the limitations period triggered for all trade secrets misappropriated by a single defendant when the plaintiff discovers or should have discovered the defendant's theft or misuse of a single trade secret?

Under pre-*Cadence* case law, the answer to that question might have been yes, as seen in *Intermedics, Inc. v. Ventritex, Inc.*, a US district court opinion decided without the benefit of the California Supreme Court's formulation of the single claim rule.<sup>85</sup> In *Intermedics*, plaintiff sued former employees and the company that employed them, Ventritex, for misappropriation of trade secrets related to an implantable defibrillator.<sup>86</sup> Intermedics had previously filed a complaint against the same defendants more than four years earlier for misappropriations arising out of the same defibrillator project.<sup>87</sup> Following the trial in the second action, the jury found that, in the earlier litigation, Intermedics either had discovered or should have discovered many of the misappropriations for which it was now suing.<sup>88</sup> Claims based on those secrets were clearly time barred.

The court then addressed whether the statute of limitations had also begun to run four years earlier with respect to other trade secrets whose misappropriation

the jury had not charged the plaintiff with having previously uncovered.<sup>89</sup> Starting from the then-prevalent view that California did not treat trade secrets as a form of property and focusing instead on the relationship between the trade secret owner and the defendant, the court found that, "absent some unusual and compelling considerations," California courts are unlikely to find that a new claim arises every time a single defendant, who has only one relationship with the trade secret owner, improperly acquires or uses information from the owner that could be characterized as a separate trade secret, as long as the trade secrets concern "related matter."<sup>90</sup>

After *Cadence* and *Cypress*, such reliance on the relationship theory of trade secret protection could be misplaced. Both courts recognized that trade secrets are a form of property that can be protected outside any particular confidential relationship. A trade secret holder has rights as against the world, and those rights are not delimited based on individualized relationships with specified third parties.<sup>91</sup> Without the relationship theory as the exclusive theoretical basis for defining trade secret misappropriation, the logical underpinnings of the *Intermedics* ruling gives way.

A potential plaintiff can possess myriad (though possibly related) trade secrets. The fact that the plaintiff knows that a defendant has stolen one of them would not, by itself, automatically give grounds to suspect that the defendant had also stolen others, even if the secrets somehow concern "related matter." Following *Cypress*, the question should be one for the jury, to be decided in light of all the relevant facts, such as the specific relationship between the different secrets and (more importantly) the extent to which the defendant's access to one secret also suggests access to the other. If, under all the relevant circumstances, a jury concludes that the plaintiff should have suspected the misappropriation of both secrets based on what it knew regarding one, then a single limitations period is appropriate. But to impose a single limitations period as a matter of law would be inconsistent with *Cadence* and *Cypress*.

In addition, the bright line rule proposed by the *Intermedics* court creates a potential for precisely the kind of injustice that *Cypress* rejected, namely, that a plaintiff's claim could become time barred even before the plaintiff had reason to suspect the relevant misappropriation. Such an outcome runs counter to the drafters' purpose in adopting the discovery rule—giving plaintiffs sufficient time to vindicate their legal rights.

In short, it would be more in keeping with *Cypress* to determine on a secret-by-secret basis (as *Cypress* did on a defendant-by-defendant basis) whether a plaintiff has the required suspicion that a potential defendant improperly obtained or used that trade secret.<sup>92</sup> This

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approach would also be consistent with the statutory scheme, which authorizes a cause of action for misappropriation of a trade secret, not trade secrets generally, and not for breach of a confidential relationship.<sup>93</sup> Although the development of case law is never entirely predictable, it seems likely that California courts after *Cypress* will conclude that the statute of limitations should be assessed separately for claims of misappropriation of separate trade secrets.

### Conclusion

By establishing both the single claim principle and the discovery rule, § 6 of the UTSA attempts to strike a balance between meaningful and effective limitations periods and the legitimate need of trade secret holders for adequate time in which to investigate and assert meritorious claims. *Cadence* and *Cypress* have specified how the two facets of § 6 apply in important factual settings. Although many questions remain unsettled, several points are now reasonably clear.

First, trade secrets constitute a form of property and, therefore, may be protected as against all third parties. There need be no confidential relationship between the plaintiff and the defendant. Anyone who knows or has reason to know that he has obtained another's trade secrets from an unauthorized source can be liable.

Second, the statute of limitations on a claim of trade secret misappropriation begins to run faster than many rights holders may have suspected, namely, as soon as the owner of the trade secret has a reasonable basis to suspect the misappropriation. As a result, prospective plaintiffs must be particularly vigilant in investigating potential instances of misappropriation and in asserting their claims. A prolonged delay before investigating or filing suit can permanently undermine the plaintiff's ability to seek redress from the wrongdoer, even when the wrongdoer's misuse of the plaintiff's secret continues long into the future.

Third, there is a possibility that in a least some circumstances courts will permit what would otherwise be time barred claims to be asserted against subsequent participants in an older, continuing misappropriation. In most cases, however, that possibility will not outweigh the prejudice caused by letting the claim against the original tortfeasor lapse.

Fourth, consistent with the express language of the UTSA and the reasoning in *Cadence* and *Cypress*, the statute of limitations on a claim for trade secret misappropriation should be assessed on an individualized basis, secret-by-secret, even when the potential defendant is a single individual or entity. That a plaintiff reasonably suspects the misappropriation of one trade secret should not automatically cause the clock to run

on claims regarding other secrets. As to each individual trade secret, the finder of fact must answer the same question: Should the plaintiff have reasonably suspected the misappropriation?

### Notes

1. See *Cadence Design Sys., Inc. v. Avant! Corp.*, 29 Cal. 4th 215. Darin Snyder and O'Melveny & Myers LLP represented defendant and appellant Avant! Corporation in this case.
2. *Cypress Semiconductor Corp. v. Superior Court*, 2008 Cal. App. LEXIS 812, H032114 (Cal. Ct. App. May 30, 2008).
3. *Monolith Portland Midwest Co. v. Kaiser Aluminum & Chem. Corp.*, 407 F.2d 288 (9th Cir. 1969).
4. See Cal. Civ. Proc. Code § 339.
5. *Monolith*, 407 F.2d at 292.
6. *Id.* at 293.
7. *Underwater Storage, Inc. v. U.S. Rubber Co.*, 371 F.2d 950, 954 (D.C. Cir. 1966).
8. See *id.*
9. See UTSA at Comment to § 6.
10. See *id.* at § 6.
11. See *id.*
12. Cal. Civ. Code § 3426.6.
13. Uniform Trade Secrets Act, Official Comment to § 6.
14. See *id.*
15. *Addison v. California*, 21 Cal. 3d 313, 317 (1978).
16. See 1984 Cal. Stat. § 1724.
17. *Cadence Design Sys.*, 29 Cal. 4th 215.
18. *Id.* at 219.
19. *Id.*
20. *Id.*
21. Cal. Civ. Code § 3426.6.
22. *Cadence*, 29 Cal. 4th at 220-221.
23. See *Cadence's Opening Brief*, 2001 WL 34152369 at \*16.
24. *Cadence*, 29 Cal. 4th at 223-224.
25. *Id.* at 224.
26. *Id.* at 225.
27. *Id.*
28. *Id.*
29. See *PMC, Inc. v. Kadisha*, 78 Cal. App. 4th 1368 (2000).
30. *Cadence*, 29 Cal. 4th at 225.
31. *Cypress*, 2008 Cal. App. LEXIS 812.
32. See *id.*
33. See *id.* at \*16-23.
34. *Id.* at \*3.
35. *Id.* at \*4.
36. See *id.* at \*4.
37. *Id.* at \*6-7.
38. *Id.* \*8-9.
39. *Id.*
40. *Id.* at \*4.
41. Cal. Civ. Code § 3426.1.
42. *Cypress*, 2008 Cal. App. LEXIS 812 at \*4-5.
43. *Id.*

44. *Id.* at \*10.
45. *Id.* at \*10-11.
46. *Id.* at \*12.
47. *Id.*
48. *Id.* (citing *Cadence*, 29 Cal. 4th at 224).
49. *Id.* at \*14.
50. *See id.* at \*15.
51. *See id.*
52. *See id.* at \*15-16.
53. *Id.* at \*16 (quoting *Intermedics*, 822 F. Supp. 634, 641 (N.D. Cal. 1993)).
54. *Cypress*, 2008 Cal. App. LEXIS 812 at \*18.
55. *Id.* at \*18-21.
56. *See id.*
57. *See* 21 Cal. 3d at 317.
58. *See Cypress*, 2008 Cal. App. LEXIS 812 at \*23.
59. *See id.* at \*3.
60. *See id.* at \*23.
61. *See id.*
62. *See* UTSA, Official Comment to § 6.
63. *See* 2008 Cal. App. LEXIS 812.
64. *See id.*
65. *See id.* at \*23.
66. *Cypress*, 2008 Cal. App. LEXIS 812 at \*18.
67. *See Adcor Indus., Inc. v. Bevcorp, LLC*, 411 F. Supp. 2d 778, 785 (N.D. Ohio 2005) (“In determining whether a party should have discovered wrongful conduct, the relevant inquiry is whether the facts known would lead a fair and prudent man, using ordinary care and thoughtfulness, to make further inquiry.”); *Read & Lundy, Inc. v. Wash. Trust Co.*, 2002 R.I. Super. LEXIS 181, No. PC99-2859 (R.I. Super. Dec. 13, 2002) (“If a person becomes aware of facts which would make a reasonably prudent person suspicious, he or she has a duty to investigate further and is charged with knowledge of matters which would have been revealed by such an investigation.”); *Alamar Biosciences, Inc. v. Difco Labs., Inc.*, 1995 U.S. Dist. LEXIS 21342, Civ-S-941856 (E.D. Cal. 1995) (“When there is reason to suspect that a trade secret has been misappropriated, and a reasonable investigation would produce facts sufficient to confirm this suspicion (and justify bringing suit), the limitations period begins.”).
68. *Cypress*, 2008 Cal. App. LEXIS 812 at \*18.
69. *New Media Strategies, Inc. v. Pulpfree, Inc.*, 941 A.2d 420 (D.C. Ct. App. 2008).
70. *Id.*
71. *Id.* at 421.
72. *Id.* at 423.
73. *Id.* at 425-426.
74. *Id.* at 426.
75. *Ashton-Tate Corp. v. Ross*, 916 F. 2d 516 (9th Cir. 1990) (statutory period triggered by letter from trade secret owner to employee of defendant expressing concern that defendant was using his proprietary evidence); *Adcor*, 411 F. Supp. 2d at 787-788 (claim was time barred where there was evidence that plaintiff’s employees discussed their suspicions that defendants had acquired and were using plaintiff’s proprietary information more than four years before plaintiff filed suit); *Stutz Motor Car v. Reebok Int’l, Ltd.*, 909 F. Supp. 1353 (C.D. Cal. 1995) (claim time barred where plaintiff’s employees had discussed possible claims against defendant more than three years before and product accused of incorporating trade secrets was widely advertised more than three years before); *Alamar Bioscience.*, 40 U.S. P.Q.2d (BNA) 1437 (plaintiff’s management considered possibility of bringing suit more than three years before but refrained because of uncertainty that defendant’s work incorporated plaintiff’s trade secret; plaintiff was charged with knowledge in defendant’s publicly available patent applications that would have confirmed defendant’s use of the secret).
76. *Cypress*, 2008 Cal. App. LEXIS 812 at \*4.
77. *Id.* at \*5.
78. *Kadisha*, 78 Cal. App. 4th 1368 (2002).
79. *Id.*
80. *Id.* at 1383.
81. *Id.* at 1385.
82. *Id.*
83. *Cypress*, 2008 Cal. App. LEXIS 812 at \*3-5.
84. *See id.* at \*22.
85. *See Intermedics*, 822 F. Supp. 634.
86. *See id.* at 637.
87. *Id.*
88. *Id.* at 641.
89. *Id.* at 650.
90. *Id.* at 652.
91. *See Cadence*, 29 Cal. 4th at 225 (“Avant!’s arguments notwithstanding, it appears indisputable that trade secrets are a form of property.”); *Cypress*, 2008 Cal. App. LEXIS 812 at \*12 (“[T]he CUTSA incorporates a property approach in that it makes third parties liable even if they had no prior relationship to the owner of the trade secrets.”).
92. *See Cypress*, 2008 Cal. App. LEXIS 812 at \*23.
93. *See* Cal. Civ. Code §§ 3426.1, *et. seq.*

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