

CADENCE V. AVANT!: THE UTSA AND CALIFORNIA TRADE SECRET LAW

By Jeff Danley

Trade secret law performs an important and useful function in the protection of intellectual property. For instance, it offers a limited amount of protection for information that may lack the requisite novelty or nonobviousness requirements needed to obtain patent protection.¹ As a result, a large company that identifies efficiencies within its structure or develops new technologies can protect them as trade secrets even if these discoveries lack the requisites necessary to become patented.² Furthermore, protecting information as a trade secret may cost less money than protecting it through the patent process—an important fact especially to small business ventures.³ Yet, despite their value, trade secrets, unlike patents or copyrights, have never enjoyed the protection of federal law. Because of the vagaries of state law, the trade secret regime lacks the unifying rationale present in these other systems.

Despite the lack of a unifying rationale in trade secret law, the California Supreme Court, in *Cadence Design Systems, Inc. v. Avant! Corp.*,⁴ resolved any uncertainty as to the basis of California's trade secret regime by holding that the Uniform Trade Secrets Act ("UTSA") provides this underlying foundation in California. The court resolved this uncertainty in two ways. First, the court adhered solely to the definitions of the UTSA and the comments in the original uniform act in rendering its decision.⁵ Second, the court clarified the underlying rationale for California trade secret law by expressly rejecting the alternative arguments advanced by both parties.⁶ The court refused to apply the former common law rationale, which focuses upon the actions of the defendant when determining liabil-

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1. See generally ROBERT MERGES ET AL., *INTELLECTUAL PROPERTY IN THE NEW TECHNOLOGICAL AGE* 31-33 (2d ed. 2000).

2. Steven Wilf, Commentary, *Trade Secrets, Property, and Social Relations*, 34 CONN. L. REV. 787, 792 (2002).

3. MERGES ET AL., *supra* note 1, at 29; see also Wilf, *supra* note 2, at 792 (discussing the importance of trade secret law to start ups and bio-tech companies).

4. 29 Cal. 4th 215 (2002).

5. See *id.* at 221-23 ("In order to answer the certified question, we must examine the pertinent language of the UTSA."):

6. See *id.* at 220-21 (describing the arguments of Cadence and Avant! and stating that "[a]s will be discussed, neither Cadence's nor Avant!'s position is entirely correct").

ity.⁷ It pointed out that the California legislature rejected this common law approach when it adopted the UTSA in 1984.⁸ Furthermore, even though the court acknowledged that trade secrets have property-like elements, it refused to base California trade secret law solely upon this property rationale.⁹ Instead, the court stated that the UTSA, as enacted in California, provided the underlying basis for trade secrets in California.¹⁰

This Note considers the implications of the *Cadence* decision. In doing so, the Note first compares and contrasts three different regimes that courts have advanced in attempts to provide a unifying basis for trade secret decisions. Second, this Note discusses the holding in *Cadence v. Avant!*. The third part concludes that the California Supreme Court's decision promotes economic efficiency in the trade secret regime in two ways: first, it increases the value of trade secrets by allowing trade secret holders to more easily protect their proprietary information; second, the decision provides guidance to both parties as to the scope of trade secret laws, thus encouraging parties to enter into settlement agreements as opposed to resolving their disputes through litigation.

I. UNDERLYING THEORIES OF TRADE SECRETS AND ATTEMPTS AT UNIFICATION

Courts and commentators have proposed at least three different systems to attempt to unify trade secret law. First, in the "property system," each new misuse of the trade secret by the defendant gives rise to a new claim, since each is a violation of the property right in the trade secret.¹¹ Each new claim, then, has its own statutory period during which the plaintiff may bring suit. The trade secret laws of New York operate as an example of this property view of trade secret law.¹² Second, in the "tort system," the harm to the trade secret holder's interest occurs when the defendant breaches a duty of trust that has developed between the plaintiff and

7. *See id.*

8. *See id.* at 221.

9. *See id.* at 222.

10. *See id.* at 226.

11. *See Underwater Storage Inc. v. U.S. Rubber Co.*, 371 F.2d 950, 955 (D.C. Cir. 1966) (holding that "where the secret has been misappropriated the wrongdoer and his privies are amenable to suit for any use of the secret").

12. Robert T. Neufeld, Note, *Mission Impossible: New York Cannot Face the Future Without a Trade Secret Act*, 7 *FORDHAM INTELL. PROP. MEDIA & ENT. L.J.* 883, 912-16 (1997) (describing the state of New York's trade secret law).

defendant.¹³ Thus, only one claim arises—at the initial act of improper disclosure or use. The drafters of the RESTATEMENT (FIRST) OF TORTS (1939) (Restatement) sought to unify state trade secret law around this system. Finally, in the UTSA,¹⁴ applied by the California Supreme Court in *Cadence*, a claim arises upon the improper acquisition of the trade secret;¹⁵ this regime, although similar to the tort system in certain respects, tempers some of the harsh results that may occur under the Restatement approach.

A. Differing Definitions of Trade Secret, Misappropriation, and Claim

1. “Trade Secret”

Though the property-based jurisdictions use the same definition for what constitutes a trade secret as that used in the Restatement,¹⁶ the Restatement provides a narrower definition of a trade secret than the UTSA. The Restatement defines a trade secret to mean a process or device “for continuous use” in the course of business.¹⁷ As a result, it excludes mere “ephemeral events” from its definition of a trade secret.¹⁸ In doing so, the Restatement focuses upon business processes and practices actually used by a company instead of any information that could bring economic benefit to a company. The UTSA, however, provides a more expansive definition of a trade secret by including all information from which a person obtains economic value.¹⁹ The drafters of the UTSA reasoned that trade secret law should protect people who have not “had an opportunity or acquired the means to put a trade secret to use.”²⁰ The drafters also wanted

13. See *Monolith Portland Midwest Co. v. Kaiser Aluminum & Chem. Corp.*, 407 F.2d 288, 292-93 (9th Cir. 1969) (rejecting the rationale applied by the court in *Underwater Storage* because California, at the time, based its trade secret laws upon the relationship of the parties, not the property-like qualities of the secret).

14. California adopted the UTSA with little comment or change in 1984. See Historical and Statutory Notes, CAL CIV. CODE § 3426 (West 1997) (recognizing the similarity between each provision in this section and the corresponding section in the UTSA); see also *Cadence*, 29 Cal. 4th at 220.

15. UNIF. TRADE SECRETS ACT § 1 (amended 1985), 14 U.L.A. 437 (1990).

16. See, e.g., *Integrated Cash Mgmt. Servs., Inc. v. Digital Transactions, Inc.*, 920 F.2d 171, 173 (2d Cir. 1990) (applying New York trade secret law); *Ashland Mgmt. Inc. v. Janien*, 82 N.Y.2d 395, 407 (1993) (stating that while no “generally accepted” definition of a trade secret exists, the definition provided in § 757 comment b of the Restatement (First) of Torts “has been cited with approval from this and other courts”).

17. RESTATEMENT (FIRST) OF TORTS § 757 cmt. b (1939).

18. *Id.*

19. UNIF. TRADE SECRETS ACT § 1, 14 U.L.A. 437.

20. *Id.* § 1, cmt.

trade secret protection to extend to "negative information" that showed that a particular practice or device does not work.²¹ Thus, a trade secret includes any proprietary information that gives a company an economic advantage.

2. "Misappropriation"

Although some property-based systems, such as that of New York, also use the Restatement definition for misappropriation,²² the two systems rely upon different underlying rationales for punishing misappropriation. While both systems focus upon the improper use or disclosure of a trade secret, the Restatement imposes a duty to protect the information that parties share in a confidential relationship.²³ This duty focuses upon the relationship between the parties and may arise through either contract or tort. Thus, under the Restatement, a party breaches this duty and commits misappropriation only when it *first* discloses or uses the information in an unauthorized manner.²⁴

The property system, however, recognizes a property interest that the trade secret holder possesses in the trade secret.²⁵ This system, seeks to protect this property interest instead of any relationship.²⁶ Accordingly, *each* unauthorized use or disclosure of the trade secret causes a separate injury to the property itself and gives rise to an act of misappropriation.²⁷

The UTSA expands the definition of misappropriation to include the improper acquisition of the trade secret. Consequently, under the UTSA, a trade secret holder may seek an injunction against another party that has improperly acquired its trade secret even before that other party has used or disclosed it.²⁸ Although nothing appears in the comments to explain this change, one commentator reasons that, under this definition, the plaintiff

21. *Id.*

22. *Integrated Cash Mgmt. Servs., Inc. v. Digital Transactions, Inc.*, 920 F.2d 171, 173 (2d Cir. 1990) (citing the Restatement when determining the definition of trade secret misappropriation in New York).

23. *See* RESTATEMENT (FIRST) OF TORTS § 757.

24. *Monolith Portland Midwest Co. v. Kaiser Aluminum & Chem. Corp.*, 407 F.2d 288, 292 (9th Cir. 1969). Courts also may base the duty upon reasonable standards of commercial morality. *See E.D. duPont deNemours & Co. v. Christopher*, 431 F.2d 1012, 1015-16 (5th Cir. 1970) (stating that Texas law forbids as improper the taking of trade secret information from another when the holder takes reasonable precautions to protect the information).

25. *See* JAMES POOLEY, *TRADE SECRETS* § 1.02[1] (1997).

26. *See id.*

27. *Underwater Storage Inc. v. U.S. Rubber Co.*, 371 F.2d 950, 953 (D.C. Cir. 1966).

28. UNIF. TRADE SECRETS ACT § 2 (amended 1985), 14 U.L.A. 437 (1990).

can more easily detect the improper acquisition of a trade secret because the defendant usually must obtain the secret by taking it from the plaintiff.²⁹ The defendant, however, may go to great lengths to conceal its use and disclosure of the trade secret.³⁰ As a practical matter, the improper acquisition of a trade secret violates either a confidential relationship between the parties or general commercial ethics as much as the improper use and disclosure.

3. "Claim"

While the Restatement and property systems define the same acts as misappropriation, claims for trade secret misappropriation arise similarly under the Restatement and UTSA. Under the UTSA and the Restatement, a claim arises once: at the time of the initial misappropriation of the trade secret.³¹ As a result, while continuing misuse and improper disclosure of the trade secret by the defendant may augment the damages recovered by the plaintiff, the court considers only one claim for misappropriation.³² Under the property view, each new misuse gives rise to a new claim for misappropriation.³³ Consequently, the plaintiff must state a claim for a particular act of misappropriation before the court will compensate the plaintiff for that misappropriation.

Thus, before the court will compensate the plaintiff for all injuries incurred by the defendant's actions, the plaintiff must state a claim for each act of misappropriation.

B. Differing Statutes of Limitations

Although each system uniquely implements its statute of limitations provision, the systems sometimes share certain elements.

1. *Number of Statutory Periods for a Continuing Misappropriation*

A continuing misappropriation gives rise to only a single claim under both the UTSA and Restatement, while each act of misappropriation by the defendant under the property system gives rise to its own statutory pe-

29. Milton E. Babirak, Jr., *The Virginia Uniform Trade Secrets Act: A Critical Summary of the Act and Case Law*, 5 VA. J.L. & TECH. 15, 16 (2000).

30. *Id.*

31. *See Cadence Design Sys., Inc. v. Avant! Corp.*, 29 Cal. 4th 215, 226 (2002); *see also Monolith Portland Midwest Co. v. Kaiser Aluminum & Chem. Corp.*, 407 F.2d 288, 293 (9th Cir. 1969) (holding that claim arose once upon initial misappropriation).

32. *See Cadence*, 29 Cal. 4th at 226.

33. *See Underwater Storage Inc. v. U.S. Rubber Co.*, 371 F.2d 950, 955 (D.C. Cir. 1966).

riod. Both the Restatement and UTSA focus upon the relationship between the parties.³⁴ Because the defendant cannot abuse this relationship further after the initial misappropriation, only one claim for trade secret misappropriation accrues.³⁵ Thus, the plaintiff need only look at the date of the initial misappropriation under the Restatement and the date of discovery under the UTSA to determine when the statute of limitations began to run on the claim for misappropriation. The property view, however, focuses upon the property right that the plaintiff possesses in the trade secret. Thus, each act of misappropriation gives rise to a new claim³⁶ because each act causes damage to this property right. Each claim, then, has its own statutory period.³⁷ Hence, a plaintiff will have to investigate the date of each misappropriation to determine if the statute of limitations will bar that claim.

2. *The Discovery Provision in the UTSA*

Because the Restatement provided no independent statute of limitation provision for trade secret claims, states have applied their own statute of limitation provisions. Before the enactment of the UTSA, California courts used the general statute of limitations for actions upon a contract.³⁸ Since this statute of limitations provided no discovery provision, the statutory period started as soon as the initial misappropriation occurred.³⁹ Similarly, the statute of limitation provisions in property-oriented systems do not provide for a discovery provision.⁴⁰ The UTSA, however, does contain a specific provision tolling the statutory period until the plaintiff knows or reasonably should have known of the misappropriation by the defendant.⁴¹ Chart 1 summarizes the different implementations of the statute of limitations and the discovery provisions in the UTSA, tort, and property systems.

34. See *Monolith*, 407 F.2d at 293; see also *Cadence*, 29 Cal. 4th at 226.

35. See *Monolith*, 407 F.2d at 293; see also *Cadence*, 29 Cal. 4th at 226.

36. See *Underwater Storage*, 371 F.2d at 955.

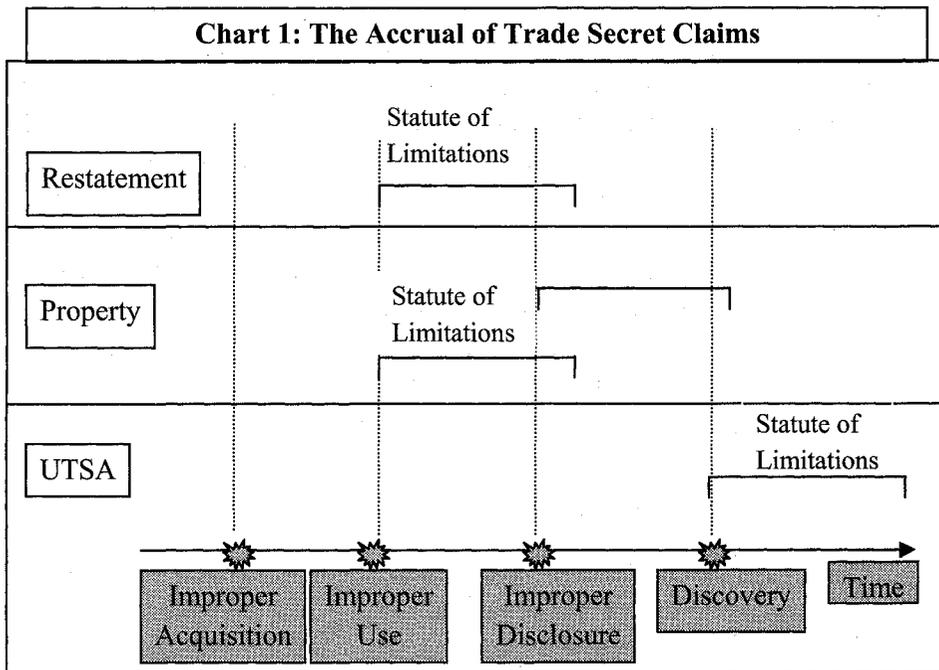
37. *Id.*

38. See *Monolith*, 407 F.2d at 293 (imposing the statute of limitations for an unwritten contract).

39. *Id.*

40. See N.Y. C.P.L.R. § 214(4) (McKinney 1962) (providing the statute of limitations for an action based upon an "injury to property"); see also *id.* § 213(2) (providing the statute of limitations for an action based upon a "contractual obligation").

41. See UNIF. TRADE SECRETS ACT § 6 (amended 1985), 14 U.L.A. 437 (1990).



II. THE *CADENCE* DECISION

In *Cadence v. Avant!*, the parties and the court discussed the applicability of all three of these trade secret systems. Cadence argued that the court should use the property-based system, which not coincidentally would allow Cadence to press any claims for misappropriation arising after a release agreement went into effect. Avant!,⁴² conversely, argued that the court should look to earlier, pre-UTSA California cases that relied upon the Restatement. Under such a view, the release agreement would cover all of Avant!'s actions, even those occurring after the signing of the release agreement. In resolving a certified question from the Ninth Circuit, the California Supreme Court applied the UTSA to hold that a claim for trade secret misappropriation arises only once, which is at the time of the initial misappropriation. In the process, the court rejected the alternative Restatement and property-oriented rationales advanced by the parties.

A. Facts

This case began, like most every other trade secret case, when four former Cadence employees left to form Avant! in 1991.⁴³ Both companies

42. Pronounced as "uh-vahn-tee."

43. Peter Burrows, *Does Crime Pay?*, BUS. WK., Sept. 3, 2001, ¶ 11, available at 2001 WL 26534462.

produce “place and route” software that automates integrated circuit design.⁴⁴ At this time, one of the four Avant! founders brought with him, without authorization, 30,000 lines of Cadence database code that Avant! incorporated into its first commercial product.⁴⁵ By combining this database code with its own technology, Avant! quickly began attracting business from some large corporations, such as Intel and Motorola.⁴⁶

Despite this initial theft, the lawsuit might never have developed if not for the events surrounding the departure several years later of a Cadence vice president, Gerald Hsu, to become Avant!’s CEO. Concerned that Hsu might use trade secret information at Avant!, Cadence drafted a claim for trade secret misappropriation and named Hsu and Avant! as defendants.⁴⁷ After lengthy negotiations, the three parties—Hsu, Avant!, and Cadence—signed a general release agreement in which Cadence waived any claim for trade secret misappropriation that it may have against either Hsu or Avant!.⁴⁸ Most importantly, this waiver applied regardless of whether Cadence knew that any claim existed, even if such knowledge would have “materially affected” the decision to sign.⁴⁹ As a result, this waiver effectively precluded Cadence from bringing a suit based upon any actions by Hsu or Avant! that occurred before June 1994—the time at which the parties signed the release.⁵⁰

At this same time, Avant!, under Hsu’s leadership as CEO, began taking actions to improve the competitiveness of Avant!’s products. These actions, however, led to the discovery by Cadence of the 1991 theft. Soon after taking over as CEO, Hsu learned that Avant!’s competitors had developed technology that they had incorporated into an improved product.⁵¹

44. Cadence Design Sys., Inc. v. Avant! Corp., 29 Cal. 4th 215, 217 (2002).

45. Burrows, *supra* note 43, ¶ 11.

46. *Id.*

47. *Cadence*, 29 Cal. 4th at 218.

48. *Id.* The release agreement stated:

Cadence, [Avant!], and Hsu . . . hereby forever release and discharge each other . . . of and from any and all manner of action, claim or cause of action . . . which they may have against each other at the time of the execution of this Agreement, known or unknown, including . . . any claims arising out of, or in connection with, . . . any anticompetitive activity or unfair competition or trade secret misappropriation.

Id. at 218-19.

49. The “waiver” language read as follows: “THESE RELEASES EXTEND TO CLAIMS WHICH THE PARTIES DO NOT KNOW OR SUSPECT TO EXIST IN THEIR FAVOR, WHICH IF KNOWN BY THEM WOULD HAVE MATERIALLY AFFECTED THEIR DECISION TO ENTER INTO THIS RELEASE.” *Id.* at 219.

50. *Id.*

51. Burrows, *supra* note 43, ¶ 13.

After a failed attempt at buying a start-up that possessed this improved technology, Avant! stole two batches of Cadence software through two former Cadence employees.⁵² Cadence remained unaware of either the original theft in 1991 by the Avant! founder or the theft later under Hsu until a former Cadence programmer noticed a slight flaw in Avant!'s products—a flaw that the programmer had inadvertently created while working for Cadence.⁵³ The programmer informed Cadence management, which then contacted the Santa Clara District Attorney's office regarding the possible theft by Avant! of its trade secrets.⁵⁴ In December, 1995, the district attorney's office raided Avant!'s corporate headquarters, where it discovered a log that detailed the 1991 copying of Cadence code.⁵⁵

B. The Decision by the California Supreme Court

The California Supreme Court held that Cadence's claim for trade secret misappropriation arose only once, when Avant! initially misappropriated the trade secret.⁵⁶ The court stated that each subsequent misuse or unauthorized disclosure by Avant! augmented Cadence's initial claim for trade secret misappropriation but did not give rise to a new claim.⁵⁷ The court rejected arguments from Cadence that the agreement should not cover misuse that occurred *after* the parties signed the release. The court stated that "a *claim* for misappropriation of a trade secret arises for a given plaintiff against a given defendant only once, at the time of the initial misappropriation, subject to the discovery rule provided in California Civil Code § 3426.6."⁵⁸ Because this claim existed at the time the parties signed the release agreement, and the release agreement covered all claims then existing, the court's opinion likely precludes any further litigation based upon the 1991 acquisition of this trade secret.⁵⁹

In reaching its decision, the court relied almost exclusively upon the wording of California's implementation of the UTSA and the Commissioners' comments in the original Uniform Act.⁶⁰ The court initially cited

52. *Id.* ¶ 14.

53. *Id.* ¶ 15.

54. *Id.*

55. *Cadence*, 29 Cal. 4th at 218.

56. *Id.* at 227.

57. *Id.*

58. *Id.* at 222 (emphasis original).

59. *Id.* at 225. The California Supreme Court issued an answer to a certified question by the Ninth Circuit. The Ninth Circuit never applied this ruling to the case because the parties settled before the court could do so.

60. *Cf. Glue-Fold, Inc. v. Slautterback Corp.*, 82 Cal. App. 4th 1018, 1024-26 (2000) (citing the *Monolith Portland Midwest Co. v. Kaiser Aluminum & Chem. Corp.*,

the definitions in the California statute for “misappropriation” and “improper means.”⁶¹ The statute includes in its definition of misappropriation the “[d]isclosure or use of a trade secret of another without express or implied consent by a person who . . . [u]sed improper means to acquire knowledge of the trade secret.”⁶² The statute defines improper means as including “theft, bribery, misrepresentation, breach or inducement of a breach of a duty to maintain secrecy, or espionage through electronic or other means.”⁶³ Furthermore, the statute defines other activities, such as reverse engineering or independent derivation, as defenses against a claim for trade secret misappropriation.⁶⁴ Consequently, the court noted that the scope of protection differs fundamentally from that in patent law, in which the patent holder receives a short-term monopoly to exclude all others from using the patented invention.⁶⁵

The court then looked to the Commissioners’ comments to the UTSA to aid its interpretation of § 3426.6,⁶⁶ which sets forth the statute of limitations for trade secret claims. In affording the Commissioners’ comments substantial weight when interpreting this section, the court noted that the legislature derived it almost verbatim from the UTSA with little debate.⁶⁷ In the comments to the analogous section of the UTSA, the Commissioners explicitly rejected the property view that a separate statute of limitations period arises each time the defendant misuses a trade secret.⁶⁸ They instead adopted the view that a continuing misappropriation gives rise to a single statute of limitations period for a claim of trade secret misappropriation.

407 F.2d 288 (9th Cir. 1969), decision and federal court decisions in support of its decision instead of using the UTSA). The National Conference of Commissioners on Uniform State Laws recommended the UTSA for enactment by all states in 1979. 1 ROGER M. MILGRIM, *MILGRIM ON TRADE SECRETS* § 1.01[2] (2003). The American Bar Association approved the draft of the UTSA in 1980. *Id.* California adopted the provisions of the UTSA with little comment. *See* Historical and Statutory Notes, CAL. CIV. CODE § 3426 (West 1997) (recognizing the similarity between each provision in this section and the corresponding section in the UTSA).

61. *Cadence*, 29 Cal. 4th at 221.

62. CAL. CIV. CODE § 3426.1(b)(2)(A).

63. *Id.* § 3426.1(a).

64. *Id.* § 3426.1(a).

65. *Cadence*, 29 Cal. 4th at 221.

66. CAL. CIV. CODE § 3426.6 (stating that “[a]n 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”).

67. *Cadence*, 29 Cal. 4th at 221.

68. *Id.* at 222.

priation.⁶⁹ The court then noted that defining a continuing misappropriation as possessing a single statute of limitations period implies defining a continuing misappropriation as giving rise to a single claim for litigation in general.⁷⁰ Finally, without contrary indications from the legislature, the court applied the same meaning to the term “claim” in cases of both litigation and contractual releases.⁷¹ Under the UTSA, then, this claim accrues upon discovery of the misappropriation by the plaintiff.⁷²

The court also used the wording of the statute to distinguish between the terms “misappropriation” and “claim.” A party may *misappropriate* a trade secret under the UTSA definition multiple times, not only with the initial improper acquisition of the trade secret but also with each subsequent misuse and improper disclosure of the trade secret.⁷³ A *claim* for trade secret misappropriation under the UTSA, however, arises only once—at the time of the initial misappropriation. Each additional misuse or improper disclosure augments the damages that the plaintiff may recover for this one claim of continuing misappropriation.⁷⁴ To hold that a continuing misappropriation gives rise to multiple claims for trade secret misuse would contradict the comments in the original Uniform Act, in which the Commissioners expressly rejected the property view that a continuing misappropriation gives rise to multiple claims.⁷⁵

Throughout its opinion, the court reaffirmed the role of the UTSA as a guide to interpretation of California’s trade secret law. For instance, it rarely relied upon California precedent in the part of the opinion that explains the rationale for its holding. In fact, when reaching its conclusion on the definition of a continuing misappropriation, the court referred to only one case, on two separate occasions—once when according significant weight to the Commissioners’ comments⁷⁶ and again when asserting that the California statute views a continuing misappropriation as a single claim for statute of limitations purposes.⁷⁷ As a result, the court indicated the significance of the UTSA in California trade secret law.

69. *Id.*

70. *Id.*

71. *Id.*

72. *Id.*

73. *Id.*

74. *Id.*

75. *Id.*

76. *Id.* at 221-22 (citing to *Glue-Fold, Inc. v. Slautterback Corp.*, 82 Cal. App. 4th 1018 (2000)).

77. *Id.* at 222-23.

In another portion of its opinion the court explicitly acknowledged the role of the UTSA. Although acknowledging the fact that “trade secrets are a form of property,” the court reminded the parties that the State defines the scope of the property interest and the methods by which a property holder can vindicate this interest.⁷⁸ In this case, the State allows a trade secret holder to have only one claim for a continuing misappropriation—based upon the Commissioners’ comments in the UTSA.⁷⁹ Thus, presumably, the UTSA helps define this area of the California trade secret law.

III. DISCUSSION

This decision by the California Supreme Court demonstrates that the UTSA, as implemented in California, improves both the rights of trade secret holders and the clarity of the application of trade secret laws when compared to both the Restatement and the property systems. This improvement in the rights of trade secret holders will encourage the creation of trade secret information. In addition, this increased clarity will encourage settlement and simplify litigation. This Part explores both of these salutary changes by examining hypothetical situations similar to the events leading to the *Cadence* litigation.

A. California Trade Secret Statutes Improve the Rights of Trade Secret Holders

Notwithstanding the decision in this case, trade secret holders will benefit from the California statutes when compared to the Restatement and property systems. First, the California statutes expand the scope of the terms “trade secret” and “misappropriation.” Second, the statutes implement a discovery provision when bringing a trade secret claim which permits a trade secret owner to more reliably bring suit against misappropriators. Finally, the statutes better protect trade secret information by forbidding innocent parties from using trade secret information that they have obtained—provided they have not materially relied upon this information. Consequently, these benefits to trade secret holders should encourage investment in the research and development of new products and business

78. *Id.* at 224. Interestingly, in this same section, the California Supreme Court also acknowledged the property-like features of a trade secret claim. The court stated: “[I]t appears indisputable that trade secrets are a form of property. But the nature of the property interest and the means by which the interest can be vindicated are matters of state law. The UTSA defines an act of continuing misappropriation for litigation purposes as a single claim.” *Id.*

79. *Id.*

practices, as misappropriation of such information will be more likely redressable.

1. *Expanding the Scope of "Trade Secret" and "Misappropriation"*

When compared to the Restatement, the California statutes reduce the burden of protecting trade secrets for software companies, such as Cadence, by expanding the definition of misappropriation to include the improper acquisition of a trade secret.⁸⁰ As a result, Cadence could have proven a trade secret misappropriation claim if it had discovered that one of the Avant! founders had taken Cadence trade secret information with him when he left Cadence without having to wait for Avant! to improperly use the computer code.⁸¹ This distinction becomes important upon realizing that Avant! concealed the theft of the code by releasing its product in object code, which no one, including Cadence, could decipher.⁸²

The California statutes also employ a more expansive definition of a trade secret. This definition allows entities to protect a broader range of information than that protected by the Restatement. While the Restatement requires that the information be in continuous use before acquiring protection as a trade secret,⁸³ the UTSA protects any information that derives independent economic value from not being publicly known.⁸⁴ Thus, California extends its protection to information that a party has acquired but not put to use.⁸⁵ Although not at issue in this case, the expanded definition

80. See RESTATEMENT (FIRST) OF TORTS § 757 (1939) (stating that "one who discloses or uses another's trade secret, without privilege to do so, is liable to the other").

81. *Cadence*, 29 Cal. 4th at 218.

82. *Id.* at 217 n.3.

83. RESTATEMENT (FIRST) OF TORTS § 757 cmt. b (stating that "a trade secret may consist of any formula, pattern, device, or compilation which is used in one's business" and that a trade secret "differs from other secret information in business in that it is not simply information as to single or ephemeral events in the conduct of business").

84. California defines 'trade secret' as:

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.

CAL. CIV. CODE § 3426.1(d) (West 1997).

85. See Laurence H. Reece III, *Trade Secret Misappropriation: A Review and Analysis of Massachusetts Law*, 71 MASS. L. REV. 171 (1986); see also *Continental Car-Na-Var Corp. v. Moseley*, 24 Cal. 2d 104, 109 (1944) (refusing to protect a list of former customers as a trade secret absent a showing that the plaintiff made regular sales to the

would have provided protection for Cadence's information while Cadence was developing it but before it became incorporated into any product. If the Avant! founder took the computer code in this sensitive stage, the Restatement would have provided no protection while California statutes would have allowed Cadence to bring suit.

With this change, California statutes provide an incentive for companies to create trade secrets by assuring them that the law will provide protection. Under the old approach, companies like Cadence would fear investing in the development of new technologies, for fear that, before the information was used in an actual product, their new ideas could be stolen without any legal means of redress. Moreover, by including the improper acquisition of a trade secret under the definition of "misappropriation," the USTA lowers the risk of maintaining and protecting trade secrets. This increases the value of the secrets, and thus encourages their development.

2. *The Discovery Provision of the California Trade Secret Statutes*

The California statutes also favor the plaintiff by implementing a discovery provision. The discovery provision tolls the statutory period until the innocent party learns or should have learned of the misappropriation.⁸⁶ Because the Restatement does not contain its own statute of limitations provision for trade secret cases, states apply their own statutory period. In the pre-UTSA California, this period accrued at the time of the misappropriation.⁸⁷ If the misappropriator could conceal his actions until the statutory period ran, then the statute of limitations would bar a trade secret holder from bringing a claim.⁸⁸ Compared to the Restatement, the discovery provision in the California trade secret statutes relieves the trade secret holder of the burden of detecting all improper uses and disclosures of its

customers on the list); *Cal Francisco Inv. Corp. v. Vronis*, 14 Cal. App. 3d 318, 322 (Cal. App. 1971) (citing the Restatement in stating that a business must continuously use information for it to qualify as a trade secret).

86. CAL. CIV. CODE § 3426.6 (stating that "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").

87. *Monolith Portland Midwest Co. v. Kaiser Aluminum & Chem. Corp.*, 407 F.2d 288, 292 (9th Cir. 1969).

88. *See id.* (stating that § 339 of the California Code of Civil Procedure sets forth a two-year statute of limitation for actions based "upon a contract, obligation, or liability not founded upon an instrument of writing" and that this statutory period begins as soon as the misappropriation occurs regardless of when the innocent party learns of the misappropriation).

trade secrets. Instead, companies such as Cadence need only take reasonable measures to ensure that they will receive legal protection.⁸⁹

By including the discovery provision, the law reduces the burden on the trade secret holder in protecting its information. This, in turn, encourages entities to create more trade secrets, since the risk of losing the value of the investment (by having a lawsuit precluded by the statute of limitations) is lower.

3. *Protecting Information From Use by Innocent Parties*

Finally, California favors trade secret holders by forbidding innocent parties from using misappropriated information unless they have materially relied upon it. This type of situation would have arisen if Avant! had sold or given the information stolen from Cadence to an innocent third party. Under the Restatement, if an innocent party paid for the trade secret in good faith, then no cause of action would exist, even if the trade secret owner only sought an injunction.⁹⁰ The Restatement arrived at this conclusion because the innocent party did not subvert any confidential relationship.⁹¹ In California under the UTSA, however, if an innocent party learns that it possesses a misappropriated trade secret, even in good faith, the court may issue an injunction against the innocent party (provided it has not materially relied upon the trade secret).⁹² In weighing the interests of the trade secret holder in protecting the trade secret and the innocent party in using the information for which it has paid, California favors the trade secret holder.

Such a result may seem at odds with the focus on confidential relationships and commercial ethics in the California statutes and the UTSA since the innocent party has broken neither.⁹³ Only after recognizing the property rights that accrue in trade secret information does the right to enjoin an innocent party make sense. Although the innocent party neither subverts a confidential relationship nor breaches acceptable commercial ethics by using the trade secret information acquired in good faith, this use does damage the value of the property right that the trade secret holder possesses in keeping this information a secret. Because of this damage to the property right of the trade secret holder, the UTSA allows the court to en-

89. CAL. CIV. CODE § 3426.6 (stating that “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”).

90. See RESTATEMENT (FIRST) OF TORTS § 757 (1939).

91. See *id.*

92. CAL. CIV. CODE § 3426.1(b)(2)(C).

93. *Id.* § 3426.1(b).

join the use of the information by the innocent party. Because the California Supreme Court has recognized this property element in trade secrets in its *Cadence* decision, California courts in the future should use these property-like elements to favor the rights of trade secret holders over innocent parties.

Favoring the trade secret holder also increases the value of trade secret information, which encourages companies to invest in research leading to the creation of new trade secrets. Much like the provisions discussed above, the increased legal protection available to trade secret information makes investment in creation of such information less risky and thus the secrets more valuable. The net effect of these changes is likely to be a substantial increase in the creation of new, innovative business practices and products.

B. Clarifying the Rules Governing Trade Secret Misappropriation

In addition to favoring plaintiffs, the California statutes also will allow parties to settle disputes more efficiently by clarifying the rules that govern trade secret misappropriation. In *Cadence*, for instance, the parties could have settled much more quickly had they known how the courts would apply the California UTSA. First, these statutes provide greater clarity for issuing injunctions when compared to the Restatement and property systems, neither of which provide guidance to courts in deciding whether to issue an injunction in a trade secret dispute. California further provides direction to the court in deciding the duration of an injunction: guidance that the Restatement and property systems lack. The ability to combine multiple misappropriations into a single claim also leads to greater clarity in California trade secret law when compared to the property system, since the parties will realize that the defendant may be liable for all of the damages resulting from misappropriation. At the same time, this knowledge will allow parties to draft tighter release agreements in the future, such that parties situated similarly to *Cadence* may better protect their trade secret information in settlement negotiations.

1. Greater Clarity in the Issuing and Duration of Injunctions

California provides for greater clarity and efficiency by guiding the court in its decision both in issuing an injunction and in deciding the length of the injunction in the case of an actual or threatened misappropriation.⁹⁴ The Restatement did not provide for the application of an injunction in the particular instance of trade secret misappropriation. Instead, it contained a general provision for issuing an injunction applicable

94. *Id.* § 3426.2(a).

to all torts.⁹⁵ California, by comparison, contains an explicit provision to govern the length of the injunction, thereby guiding the court in its decision making process.⁹⁶ By doing so, the California UTSA helps assure that both parties will realize the possible remedies that the court may issue: a fact that increases the possibility that the two sides may settle before a trial. In addition to encouraging settlement, it will further improve the efficiency of the court system by reducing the number of possible issues about which the two sides may argue.

Had Cadence not signed the release agreement, this provision would have become important because it would have guided the court in deciding whether to issue an injunction as well as deciding the length of the injunction. In this hypothetical case, the court probably would have issued an injunction because of the actual and threatened continued misappropriation by Avant!. Furthermore, because the information remained a trade secret even after Avant! acquired it, the statute would have directed the court to issue an open-ended injunction against further use by Avant! until such time as the information lost its trade secret status. As a result, the statutes provide both parties with an opportunity to realistically assess their position and negotiate a settlement before going through with costly litigation.

2. *Combining Multiple Misappropriations into a Single Claim*

California also provides for greater clarity and efficiency, when compared to property based systems such as the one used by New York, by combining instances of continuing misappropriation into a single claim.

95. RESTATEMENT (FIRST) OF TORTS §§ 933-43. In this vacuum, three different approaches arose. In one approach, the court enjoined the defendant from ever using the trade secret. *Shellmar Prods. Co. v. Allen-Qualley Co.*, 87 F.2d 104, 107-108 (7th Cir. 1936). Another court held that once trade secrets have been disclosed to the public, the court will no longer enforce the injunction. *Conmar Prods. Co. v. Universal Slide Fastener Co.*, 172 F.2d 150, 156 (2d Cir. 1949). In a compromise holding, a third court enjoined the defendant from using the trade secret for the length of time the court determined the defendant would have taken to legally discover the trade secret. *Winston Research Corp. v. Minn. Mining & Mfg. Co.*, 350 F.2d 134, 142 (9th Cir. 1965).

96. CAL. CIV. CODE § 3426.2(a). The California statute states:

Actual or threatened misappropriation may be enjoined. Upon application to the court, an injunction shall be terminated when the trade secret has ceased to exist, but the injunction may be continued for an additional period of time in order to eliminate commercial advantage that otherwise would be derived from the misappropriation.

Id. § 3426.2(a).

Each improper use or disclosure in New York gives rise to a new claim.⁹⁷ Each claim in a property system possesses a different date on which the statute of limitation will run.⁹⁸ Under the California statutes, by contrast, one claim would arise for all acts of trade secret misappropriation in instances of a continuing misappropriation.⁹⁹ This claim accrues upon the initial act of misappropriation, but the discovery provision tolls the statute of limitations. The tolling provision, then, prevents the parties from litigating over the date of the initial misappropriation and allows the innocent party to recover on all misappropriations; in New York, the statute of limitations may bar certain claims and allow others. This situation in New York may encourage parties to litigate the dates of different misappropriations, especially those falling close to the cut off date of the statute of limitations, a situation that discourages settling. Thus by giving both parties better information regarding the defendant's potential liability, the California statutes will allow some parties to settle out of court when they otherwise would not under New York's trade secret laws.

California also provides for greater clarity when compared to New York's property-based system by providing a single statute of limitations period applicable to all trade secret claims. In New York, differing statutes of limitations exist depending upon whether the underlying cause of action for the misappropriation claim arises under property law or contract.¹⁰⁰ A party in New York must commence a claim for an injury to property within three years,¹⁰¹ while a party must commence a claim based upon a contractual obligation within six years.¹⁰² Furthermore, neither the label used in the cause of action nor manner in which the plaintiff pleads its claim restricts the type of statutory period the New York court may apply.¹⁰³ In California, however, a three-year statute of limitations, subject to the discovery provision, applies to all claims for trade secret misappropriation.¹⁰⁴ By providing a single statutory period applicable to all trade secret

97. Michael Hutter, *The Case for Adoption of a Uniform Trade Secrets Act in New York*, 10 ALB. L.J. SCI. & TECH. 1, 48 (1999).

98. *Gen. Precision v. Ametek, Inc.*, 20 N.Y.2d 898, 899 (1967) (stating that a cause of action arises each time the defendant used the plaintiff's secret).

99. *Cadence Design Sys., Inc. v. Avant! Corp.*, 29 Cal. 4th 215, 226 (2002).

100. Hutter, *supra* note 97, at 7.

101. N.Y. C.P.L.R. § 214(4) (McKinney 1962).

102. *Id.* § 213(2).

103. *See Petnel v. Am. Tel. & Tel. Co.*, 280 A.D. 706, 709 (N.Y. App. Div. 1952) (dismissing certain claims that the plaintiff had brought as fraud, which tolls the statute of limitation until discovery, because the improper use of the plaintiff's trade secret represented the gravamen of the cause of action).

104. CAL. CIV. CODE § 3426.6 (West 1997).

claims, the California statutes remove one further issue that the parties must litigate in New York. This greater clarity again provides both parties with better information regarding the potential liability of the accused, which will also encourage the parties to settle before litigation begins.

Some may criticize the situation in California as creating a rush to the courthouse in that the statutory period begins as soon as the trade secret holder discovers the misappropriation. Consequently, the trade secret owner must file suit before the statutory period runs regardless of whether the particular misappropriation resulted in harm sufficient enough to persuade the trade secret holder to file claim absent the statute of limitations. In essence, the trade secret holder must file suit soon after learning of the misappropriation to protect his future interest in the trade secret information or risk forever being barred by the statute of limitations of doing so.

This argument, however, misses the point that the state protects this information precisely because it is a *secret*; if a competitor gains access to this information, then the trade secret holder has a duty to vindicate the secrecy of this information by obtaining an injunction from the court forbidding the other company from using this information. By waiting until some sufficient misappropriation occurs to vindicate its rights, the trade secret holder may lull the misappropriator into a false sense of security that the trade secret owner does not plan to press a claim. Furthermore, this issue provides the parties with a further issue to litigate—even more so if the court decides to implement a policy similar to the doctrines of laches and estoppel in which the court would prohibit a claim precisely because the trade secret holder failed to vindicate its rights in a reasonable period of time. Finally, as the *Cadence* court noted, the state defines the trade secret owner's interest in the trade secret and the method by which he may vindicate his rights in this interest.¹⁰⁵ If the state requires the trade secret holder to maintain the secrecy of its information, then trade secret holder should not complain when he fails to do so.

IV. CONCLUSION

The California Supreme Court in *Cadence v. Avant!* demonstrated that the UTSA, as implemented in California, both provides an improvement in the rights of trade secret holders and creates greater clarity in the application of trade secret laws when compared to both the Restatement and the property system. Although *Cadence* probably would have lost its claim against *Avant!* had the parties not settled, trade secret holders gain with

105. *Cadence Design Sys., Inc. v. Avant! Corp.*, 29 Cal. 4th 215, 224 (2002).

the enactment of the UTSA in California. This gain comes from the expanded definition of “trade secret” and “misappropriation” as well as from the ability of trade secret holders to enjoin innocent third parties that have obtained the trade secret holder’s proprietary information. As a result, the increased rights of trade secret holders will encourage the creation of trade secret information. Finally, the California statutes will allow parties to settle disputes more efficiently by clarifying the rules that govern trade secret misappropriation. This efficiency will allow parties in trade secret disputes to better negotiate a resolution—with reduced involvement by the court system—by drafting more robust settlements that better protect trade secret information.