TroyGould
ATTORNEYS

Appellate Court Upholds $1.6 Million Sanction Award Against Employer That Filed Trade Secrets Claim in Bad Faith

Russell I. Glazer
June 2009

The California Court of Appeal has upheld an attorney fee award of more than $1.6 million against a company that unsuccessfully sued two of its former executives for misappropriation of trade secrets. The case, *Flir Systems, Inc. v. William Parrish et al.*, involved a high-tech company that manufactured components for infrared cameras and similar products. The company sued the executives after they left to start a new company in a similar field. The court found that the company brought the lawsuit in bad faith, in violation of California's ‘strong public policy that permits ex-employees to start new entrepreneurial endeavors.’

California's Trade Secrets Act allows a plaintiff to obtain an injunction against ‘actual or threatened misappropriation’ of their trade secrets. However, the Act also allows an award of attorneys' fees against the plaintiff, ‘if a claim of misappropriation is made in bad faith.’ As the court explained in *Flir Systems*, bad faith exists within the meaning of the Act if (1) the claim is ‘objectively specious’ and (2) the plaintiff acted with ‘subjective bad faith in bringing or maintaining the action.’ Thus, even if the plaintiff had a good faith reason to file a trade secret claim, sanctions may still be awarded if the plaintiff persists in maintaining the claim after learning that the defendant has done nothing wrong.

In *Flir Systems*, three key facts supported the court's conclusion that the company had acted in bad faith:

- First, the company's chief executive officer testified that the company had filed the lawsuit because ‘we can't tolerate a competitive threat’ by the defendants. As a result, the court concluded that the company had ‘filed a specious action as a preemptive strike and for an anticompetitive purpose.’
- Second, the court concluded that the company had no information showing that the executives had actually misappropriated its trade secrets. Instead, the company filed suit based on mere ‘speculation that a departing employee may misappropriate and use a trade secret in a startup business.’
- Finally, the court held that the company had ‘maintained the action in bad faith by imposing unnecessary settlement conditions.’ Specifically, the company had demanded that the executives provide monetary compensation, a non-competition agreement, an agreement not to hire the company's employees, and a promise not to challenge the company's patent applications. The court found that these demands ‘were inflammatory, violated public policy, and were made in bad faith.’

Conclusion
As the *Flir Systems* decision illustrates, California law highly favors employee mobility, and contains strict sanctions against employers who would use the Trade Secrets Act to prevent competition. Companies should make sure that they have solid evidence of wrongdoing before filing trade secrets actions against former employees.