

# Recent Developments in the Law

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## LETTER

*June 2005, Special Edition Special Issue  
Copyright Awards*

In order to keep you abreast of recent developments in the law, Saunders & Schmieler's *S&S Recent Developments in the Law* reports on the significance of current decisions of major import in the jurisdictions of Maryland, the District of Columbia, Virginia, and the federal Fourth Circuit.

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The Law Firm of Saunders & Schmieler, P.C. is pleased to announce that, in a continuing effort to provide high quality and cost-effective representation to its clientele, the firm is participating with the University of Baltimore School of Law in its Student EXPLOR (Experience in Legal Organizations) program. Under this program, a student from the University of Baltimore School of Law will be volunteering his time at Saunders & Schmieler's Silver Spring, MD offices.

Acting under the supervision of Saunders & Schmieler's attorneys, the EXPLOR student will provide valuable assistance in areas ranging from conducting legal research using the firm's extensive WestLaw National Gold research database, to drafting pleadings, motions, and memoranda. Perhaps most important to our clients, the firm does not bill for time the EXPLOR student spends working on a client's file.

It is our sincere belief that the use of this valuable program will help minimize the cost of legal services we provide while maximizing the effectiveness of our ongoing efforts to advance our clientele's

interests.

**UNITED STATES COURT  
OF APPEALS FOR THE  
FOURTH CIRCUIT**

***Major Victory for Federal Insurance Company - Misappropriation of a Trade Secret and the Misuse of that Trade Secret to Develop, Advertise, and Market a Subsequently Developed Product is not Covered by the "Advertising Liability" Coverage of Perdue Farms' Insurance Policy; Insurer Bears no Duty to Indemnify Perdue Farms for its Violation of Confidentiality Agreement***

**Title:** *Perdue Farms, Inc. v. Nat'l Union Fire Ins. Co.*, No. 04-1176 (4th. Cir. June 2, 2005).

Unpublished opinion available at <http://pacer.ca4.uscourts.gov/opinion.pdf/041176.U.pdf>

**Case Summary:** Philosophical clichés aside, this litigation required the U.S. District Court for the District of Maryland and the U.S. Court of Appeals for the Fourth Circuit to decide which came first: the chicken or the advertising. Significantly for the insurers, the court determined that the chicken came first, and thus the advertising liability provisions of the relevant insurance policies did not require the insurers to indemnify Perdue for its appropriation of a Florida man's proprietary chicken preparation method.

In its *per curiam* opinion, the Fourth Circuit stated at the outset that "[t]he District Court concluded that no reasonable jury could find Perdue's damages covered by the advertising liability provision," and that the Court would affirm that decision.

Dennis Hook approached Pizza Hut in 1991 with a unique process for cooking chicken, a process that would allow fast-service restaurants to prepare and serve a chicken product with the appearance of rotisserie chicken in less than 10 minutes. Pre-seasoned chicken was placed in vacuum sealed bags, cooked, then refrigerated or frozen; thereafter, it could be re-heated and finished by using a microwave and conventional or pizza oven. Pizza Hut and Hook entered a development agreement in 1992 with the potential for up to \$20 million in royalty payments to Hook. Then, in 1993, Pizza Hut contracted with Perdue as a source of chicken for the product; Pizza Hut and Perdue signed a confidentiality agreement under which Pizza Hut disclosed information to Perdue "for the purpose of development, improvement, and/or possible manufacturing," and Perdue agreed not to use the secret information for its own account or purposes. Pizza Hut decided not to pursue the product, and, unknown to Hook, about six months after he visited the Perdue plant to discuss the process, Perdue began developing a product called "TenderReady" using Hook's preparation techniques.

Hook eventually learned of TenderReady at a trade show in Paris; Hook saw sales brochures there describing the "essential, previously confidential nature of his process." Hook demanded that Pizza Hut enforce the confidentiality agreement and, when Pizza Hut declined to take action, brought suit against Perdue in Florida to enforce the confidentiality agreement and collect damages for the misappropriation of his trade secret. Hook's complaint alleged that Perdue misappropriated his trade secret in violation of Florida's Uniform Trade Secrets Act (FUTSA); Hook alleged that as a result of the misappropriation, Perdue gained a commercial advantage and caused "the actual loss of the independent economic value of the Process." Hook also alleged independently that Perdue breached the confidentiality agreements. At trial, the jury found that Hook's process a trade secret and that Perdue had misappropriated it. The jury awarded Hook \$25 million in actual damages and \$2 million in damages for unjust enrichment; the court further awarded \$6.75 million in punitive damages, and almost \$15 million in pre-judgment interest. The damage awards were reduced by the Florida appellate court, but prior to its final judgment, Hook and Perdue entered a "high-low" settlement agreement according to which Perdue would pay a

guaranteed minimum of \$10 million, but no more than \$30 million. Perdue ended up paying Hook the full \$30 million, and it is this \$30 million payment for which Perdue sought indemnification in separate proceedings commenced in the U.S. District Court for the District of Maryland.

Perdue claimed that it should be covered by the advertising liability provisions of its insurance policies; those provisions, though, are limited by a disclaimer for coverage under advertising liability for claims made against Perdue due to its "failure of performance of contract." The insurers disclaimed coverage, arguing that the offense against Hook did not occur because of Perdue's advertisement of the process, but rather because of Perdue's misappropriation of the process itself. The insurers also stressed that Perdue's failure to perform its contractual obligations under the confidentiality agreement triggered the "failure to perform" exception, releasing the insurers from any duty to indemnify Perdue.

The District Court agreed with the insurers, finding, in reviewing the Florida proceedings, that "the jury found that Perdue misappropriated the Hook process by developing and marketing the TenderReady line of chicken." (citing *Perdue Farms, Inc. v. Nat'l. Union Fire Ins. Co.*, 197 F. Supp. 2d 370, 375 (D.Md. 2002)). By extension, Hook had pursued damages based on the argument that Perdue's action of appropriating his process had preempted him from licensing it to others, not that Perdue's advertisement of the process had caused his injury.

On appeal, Perdue focused on perceived inconsistencies between the District Court's opinion on National's duty to defend and the court's opinion on the duty to indemnify. Perdue advanced the argument on appeal that, because of these inconsistencies, the appellate court should err on the side of finding coverage. The Court of Appeals noted, on this argument, that Maryland law clearly states "the duty to defend is broader than the duty to indemnify," and thus, Perdue's focus was misplaced.

One of the hotly contested issues in the appellate briefing was the appropriate standard of appellate review; Perdue argued that the appeals court should conduct a de novo review, but the insurers argued that the appeals court should accept the factual findings of the District Court so long as there was not "clear error." The Court of Appeals stated that the question before the District Court was a legal question of whether there was insurance coverage, and that such a legal question is subject to de novo review.

The Court of Appeals found that "the exclusion for 'failure of performance of contract' bars coverage under the breach of contract claims." This was because, in the court's view, "[n]o matter how artfully Perdue attempts to construe its actions, Perdue failed to perform its obligations under the confidentiality agreements."

The question of how Perdue had misappropriated Hook's trade secret required more of the Court's attention. The Court had to determine whether the Florida jury based its damages award on the disclosure of Hook's process, or on Perdue's use of Hook's process. If the damages were based on Perdue's use, the advertising liability sections of Perdue's insurance policy would not trigger a duty to indemnify. The Court started by looking at the jury's award itself; because the jury made an unjust enrichment award and found that Hook's injury occurred in 1993, when Perdue began developing the TenderReady product, the Court inferred that the jury focused on Perdue's use of the process to create a product, not on Perdue's disclosure of the process in the brochures Hook saw in 1996. Thus, because Hook's injuries consisted of losing the ability independently to develop and license the chicken preparation process, and not in losing the ability to advertise or market the process, the Court held that the advertising liability sections of Perdue's policies would not apply.

**Commentary:** The Fourth Circuit made the correct decision in holding that Perdue's liability arose out of its use of Hook's process, and that the advertising liability portions of Perdue's insurance policies did not

apply when Perdue failed to perform under its confidentiality agreement. En route to this holding, the Court picked up on several significant aspects of the insurers' brief.

First, the Court rightly accepted the argument in the brief that "Perdue's liability in the underlying suit was predicated upon its failure to perform under its contracts and the exclusion is clearly applicable to bar any Advertising Liability coverage." This argument had been advanced and accepted before the District Court, but it is clear that the Court of Appeals found it especially compelling, noting that even if Hook's injuries had been caused by Perdue's advertising, the "failure of performance of contract" exclusion would clearly have barred indemnification.

Second, the Court highlighted the importance of Perdue's development of a product based on Hook's process, rather than the content of the advertising Perdue used to market its product. Although the District Court had acknowledged this distinction, the Court of Appeals concluded that Perdue's liability was based on "its use and development of Hook's process," not because it "co-opted Hook's advertising idea."

Where the Court went wrong, fortunately not in a way that resulted in an incorrect outcome, was where it insisted on reviewing the entire matter *de novo*. Axiomatically, a trial court's factual determinations should not be overturned on appeal unless those determinations are clearly erroneous; where the parties agree to the facts, there can be no legal error. It is only legal conclusions that should be reviewed *de novo* after a motion for summary judgment; while the grant of a motion of summary judgment is a legal conclusion, when the legal conclusion is based on undisputed facts, a reviewing court should not arrogate unto itself the power to review - and potentially overturn - those facts. The question for the appellate court should be a simple one, and the Fourth Circuit cited the relevant Maryland law when it said it was left "to determine whether the trial court correctly interpreted and applied the relevant law to the uncontested facts."

In sum, the Court of Appeals made the right decision and for the right reasons. It is curious that the Court decided to leave its opinion unpublished, which means that the opinion will not serve as binding precedent within the circuit. This opinion should be published and should become precedential; it contains a lucid determination of what is advertising and what is not for purposes of an advertising liability provision in an insurance policy, and the court's guidance could benefit future litigants, insurers, and insureds.