



JAMS (JUDICIAL ARBITRATION AND MEDIATION SERVICES)

JAMS Case No.1110009296

POLIMASTER LTD. AND NA&SE TRADING CO. LIMITED V. RAE SYSTEMS INC.

INTERIM AWARD

05 July 2007

Tribunal:

[Read Ambler](#) (Sole arbitrator)

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Interim Award

THE UNDERSIGNED ARBITRATOR, having been duly appointed by JAMS pursuant the parties' stipulation to arbitrate the above matter under the JAMS Comprehensive Arbitration Rules and Procedures, having examined the submissions, proof and allegations of the parties, finds, concludes and issues this Interim Award as follows:

I. Introduction and Procedural Statement

- [1]. This arbitration was preceded by litigation in the United States District Court for the Northern District of California: POLIMASTER LTD., NA&SE TRADING CO. vs. RAE SYSTEMS, INC., Case No. C05 01887 HRL. Judge Jeremy Fogel has reportedly retained jurisdiction of the matter pending this arbitration.
- [2]. The Arbitration Agreement ("Agreement") is set forth in ¶ 9.2 of the Nonexclusive License for Proprietary Information Usage executed by the parties on January 14, 2003. Although the recital at the beginning of the Nonexclusive License for Proprietary Information Usage states that it is an agreement between Na&Se as "Licensor" and RAE as "Licensee" all three parties signed, with Polimaster signing as "Manufacturer." On May 5, 2006, claimant Polimaster filed a "Commencement Letter" with JAMS outlining the agreement of Polimaster (but not expressly Na&Se) and RAE to arbitrate pursuant to the JAMS Comprehensive Arbitration Rules and Procedures. Thereafter JAMS formally commenced this arbitration.
- [3]. On July 7, 2006, pursuant to Rule 9(b) of the JAMS Comprehensive Arbitration Rules and Procedures, Claimants Polimaster and Na&Se (hereinafter "Polimaster") filed a letter Demand for Arbitration.¹ RAE thereafter timely filed its Answer to Demand for Arbitration, and also filed counterclaims, to which Polimaster responded. Polimaster disputed in a motion to dismiss whether any counterclaims could be brought herein and also whether certain affirmative defenses lie. Polimaster's concerns were addressed in a motion heard on October 20, 2006. The motion to dismiss was denied in an order dated November 13, 2006. Various other pre-hearing disputes were also resolved in pre-hearing written orders.
- [4]. The matter came on regularly for arbitration hearing on March 5, 2007. The hearing was concluded on March 16, 2007, at which time the evidence was closed. Counsel briefed the matter pursuant to a stipulated schedule, with the last simultaneous briefs due on May 22, 2007. On June 1, 2007, RAE submitted an additional letter brief responding to new arguments made by Polimaster in its May 22, 2007 reply brief. Polimaster objected; the arbitrator overruled the objection by an email order dated June 7, 2007, on which date the matter was deemed to have been submitted for decision.²

¹ Polimaster's suggestion that it was not a party to the License Agreement is contrived. Polimaster signed the License Agreement, and admitted that it entered into the License Agreement in its federal complaint and in its demand for arbitration. Polimaster also asserted claims against RAE under the License Agreement in its federal complaint and in this proceeding. While negotiating the License Agreement, Polimaster told RAE that there was "only one" reason to make NA&SE a party to the contract, "taxes."

II. Facts

- [5]. The following is a statement of those facts found by the Arbitrator to be true and necessary to the award. To the extent that this recitation differs from any party's position, that is the result of the Arbitrator's determinations as to credibility and relevance, burden of proof considerations, and the weighing of the evidence, both oral and written.

Background

- [6]. This case involves the manufacturing and sale of handheld radiation detection devices. Polimaster began developing radiation detectors in 1995 at its headquarters in Minsk, Belarus. Prior to 2003, RAE, a San Jose, California company, produced chemical gas detection products. After the terrorism events and tragedies on 9/11, RAE concluded in 2002 that the radiation detection market could be a profitable area for RAE. In April of 2002, Dr. Peter Hsi, the Chief Technical Officer at RAE, conducted research into the radiation detector market at the request of Robert Chen, RAE's Chief Executive Officer. The research was intended to provide RAE with an overview of the technology and products available in the marketplace. In addition, in June of 2002, RAE had retained nuclear engineers in Shanghai to assist RAE in its efforts related to radiation detection technology. Dr. Hsi kept Mr. Chen updated as to his progress in this effort throughout 2002.
- [7]. Because of the lengthy amount of time it would take for RAE to develop its own marketable radiation detector, RAE developed the strategy of seeking out a partner which had an established ability to develop and manufacture radiation detection products. RAE's strategy was to use a "dual approach" to entering the radiation detector market: while developing its own detector, RAE explored the possibility of immediate entry into the market as a manufacturer of others' detectors. By integrating another company's detector into its existing product line, Mr. Chen and Dr. Hsi reasoned, RAE could begin building goodwill and a sales and marketing foundation in the radiation detection field right away, so RAE would be an established vendor by the time its own detector was ready for sale.
- [8]. Pursuant to this effort to locate a company that manufactured radiation detection products, RAE focused on Polimaster and its personal radiation detectors, which used cesium iodide (CsI) crystals. Based on its prior research into the market, RAE had already focused on radiation detectors which used CsI crystals before it contacted Polimaster. RAE also believed that Polimaster's personal radiation detectors were the best in their category.
- [9]. RAE sought out Polimaster and sent it an email in July 2002. RAE informed Polimaster that RAE was interested in selling Polimaster's radiation detectors in the United States. Polimaster informed RAE that it already had an exclusive representative in the United States, TSA Systems Ltd., and that RAE would need TSA's agreement in order to be involved in any efforts related to the sale of Polimaster's radiation detectors in the United States.
- [10]. Mr. Chen visited with Polimaster in September of 2002. During this visit, the parties discussed entering into an agreement that authorized RAE to manufacture Polimaster's radiation detectors.

² See, CMO No. 4 dated June 28, 2007.

The parties also discussed the possibility of developing a product which combined Polimaster's radiation detection technology and RAE's chemical detection technology in one product.

- [11]. Pursuant to this visit with Polimaster and at Polimaster's direction, RAE then engaged in its own discussions with TSA concerning how RAE and TSA could agree to work together related to the sale of Polimaster's radiation detectors in the United States. TSA informed RAE that TSA had a license with Polimaster to manufacture and sell Polimaster's products, and that TSA was interested in entering into a sublicense with RAE. RAE and TSA then signed a Memorandum of Understanding which explicitly acknowledged that RAE would be "sub-licensing" rights related to Polimaster's products from TSA.
- [12]. In January 2003, representatives of Polimaster, Na&Se, RAE and TSA met in California in January 2003 to execute final agreements between the parties. As a result of the meetings in California, Na&Se, which held the rights to Polimaster's proprietary information, entered into an agreement with RAE entitled the Nonexclusive License for Proprietary Information Usage ("License Agreement") on January 14, 2003. The License Agreement granted RAE, among other things, the exclusive right to manufacture four Polimaster licensed products in the United States and China.
- [13]. On the same date, and in conjunction with the License Agreement, RAE entered into an agreement with Polimaster entitled "Product and Component Buy/Sell Agreement" ("Buy/Sell Agreement"). In the Buy/Sell Agreement, RAE agreed that it would ramp up its Licensed Product manufacturing gradually. Initially, RAE would purchase "100% kits" from Polimaster, *i.e.*, Polimaster would sell RAE all of the parts needed to manufacture the Licensed Products, and RAE would assemble and sell them. RAE would then phase out 100% kit manufacturing. Over a period of three to six months, RAE would start sourcing parts from third-party suppliers, and eventually would begin building its own parts, and even selling some to Polimaster. Finally, RAE and TSA entered into an agreement delineating a commitment by TSA to purchase Polimaster's products from RAE on favorable price terms.³
- [14]. On February 27, 2003, RAE's Robert Chen received a package of documents from Polimaster. The documents did not include any specific details regarding the PM 1703M's internal sensor block - where the crystal and photodiode reside - Or any Polimaster products or components. In fact, although the contracts between RAE and Plaintiffs were signed on January 15, 2003, RAE did not receive any Polimaster units under those contracts until May 30, 2003, when RAE received 150 fully-assembled pagers from Polimaster, labeled with RAE's "GammaRAE" mark. RAE did not receive its first order of 100% kits from Polimaster until July 9, 2003. RAE assembled the kits and sold the finished products in the summer of 2003.
- [15]. On May 24, 2003, Dr. Sun and two RAE engineers from Shanghai traveled to Minsk, Belarus to learn more about the manufacturing process. The engineers were taught how to assemble component parts, how to operate the PM 1703M user interface, how to test and calibrate the entire detector unit using Polimaster's calibration software, and how to set parameters for the PM 1703M. Dr. Sun reviewed the manufacturing documentation Polimaster provided to RAE, which generally describes the PM 1703M's component parts and contains only a few outline drawings of the sensor block.

³ As discussed *infra*, within months of granting an exclusive license to manufacture its products in the United States market, Polimaster breached the parties' License Agreement by usurping for itself one of the largest manufacturing orders for the products ever received in the United States - the Coast Guard order. In fact, Polimaster had been continuing to source licensed products directly to TSA for sale in the United States, in violation of RAE's exclusive manufacturing license, since the contracts were entered.

These few pages do not contain information, whether read alone or in conjunction with the remaining pages of technical documentation, that would enable an engineer to reconstruct the PM 1703M's internal sensor block.

The GammaRAE II

- [16]. Meanwhile, RAE's independent research and development efforts continued to progress. RAE refined its portable radiation detection prototype for the purpose of integrating it into its existing portable chemical detector product, the AreaRAE. Dr. Hsi and his team initially referred to the portable radiation detection module that they developed for use in the AreaRAE as the RadRAE module ("RadRAE"). The RadRAE was incorporated in, and sold as part of, RAE's AreaRAE-gamma product, which was announced in October 2003 and available for shipment in March 2004.
- [17]. On January 25, 2005, RAE issued a press release announcing that RAE was taking orders for the GammaRAE II, its new portable radiation detection product. RAE also announced that orders would be available for shipment in April 2005. RAE received its first order for the GammaRAE II on February 23, 2005. RAE shipped the first order of the GammaRAE II, as announced, on April 13, 2005.

Polimaster Files Federal Suit

- [18]. Polimaster filed suit in federal court on May 9, 2005 and sought a preliminary injunction based on RAE's alleged misappropriation of Polimaster's trade secrets in connection with the GammaRAE II. After extensive briefing and a hearing, the District Court denied Polimaster's motion, concluding that Polimaster was unlikely to succeed on the merits. As the order denying Polimaster's motion stated, "[M]any of the product specifications disclosed to RAE, such as the type of crystal detector, the alarm algorithm, the time of calibration and the general components of the detector block, are contained in the Operating Manual for the Gamma Pager PM 1703M." Although Polimaster claimed that RAE misappropriated Polimaster's manufacturing "know-how," it did not "adequately identif[y] specific manufacturing procedures employed by RAE that fall within this category." According to the District Court, "the similarities in the parties' finished products" were insufficient to demonstrate that RAE had relied on any of Polimaster's proprietary information.
- [19]. More than a year later, Polimaster filed and served its demand for arbitration herein.

III. Analysis

A. Polimaster Has Failed to Prove the Misappropriation of Any Trade Secret

[20]. In order to prove the misappropriation of a trade secret, Polimaster must first prove that it had a trade secret capable of misappropriation.

Polimaster Failed To Prove the Existence of Any Trade Secret

[21]. Polimaster failed to prove the existence of any trade secret in connection with its allegedly proprietary radiation detection technology.

[22]. The California Uniform Trade Secrets Act defines a trade secret as:
[I]nformation... that: (1) [d]erives 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) [i]s the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

Cal. Civ. Code § 3426.1(d). Polimaster failed to establish either element.

[23]. The radiation detection technology at issue in this arbitration - the combination of a cesium iodide crystal and a photodiode - has been in the public domain for decades. It is axiomatic that information in the public domain is not a trade secret. *Sinclair v. Aquarius Electronics, Inc.*, 42 Cal. App. 3d 216 (Cal. Ct. App. 1974) ("[B]y definition, a trade secret is something which has not been placed in the public domain.").

[24]. Polimaster also voluntarily disclosed detailed information with respect to its product specifications and calibration methodologies. As the District Court found, in denying Polimaster's motion for a preliminary injunction, "many of the product specifications disclosed to RAE, such as the type of crystal detector, the alarm algorithm, the time of calibration and the general components of the detector block, are contained in the Operating Manual for Gamma Pager PM1703M," which "is made available to the public on the Polimaster website without restriction." Polimaster admitted as much in the evidence it submitted in the District Court. It is axiomatic that making information available on the internet deprives it of trade secret protection. *See, e.g., Religious Tech. Ctr. v. Netcom On-line Comm.*, 923 F. Supp. 1231, 1256 (N.D. Cal. 1995); *Hirel Connectors, Inc. v. United States of America*, CV01-11069 DSF (VBKJx) 2005, 2005 U.S. Dist. LEXIS 44170 at *14 (Jan. 5, 2005) (holding that information posted on the internet lost any trade secret protection despite over twenty years of prior efforts to maintain secrecy).

[25]. Furthermore, Polimaster sent RAE its "Technical Requirements," operating manuals and software and graphics files for the instruments for translation during the parties' negotiations in 2002, before any agreements were entered. In the District Court, Polimaster admitted that the "Technical Requirements" it voluntarily disclosed to RAE was "a basic formal document specifying ALL instrument parameters and characteristics (physical, electrical, environmental, etc.) as well as Methods of its verification (e.g. method of calibration for gamma radiation)." This broad, voluntary disclosure precludes Polimaster from demonstrating that this information has been kept confidential, a prerequisite for trade secret protection. *See Religious Tech. Ctr.*, 923 F. Supp. at 1250-51. Polimaster also provided RAE samples of its pager products and permitted RAE to tour its manufacturing facilities months before any agreements were entered.

- [26]. Polimaster's own expert witness, H. Dale Snowder, admitted on cross-examination that Polimaster's allegedly proprietary technology - the use of a cesium iodide crystal in combination with a photodiode - is well-known technology with respect to radiation detection, and has been since about 1975. Mr. Snowder also admitted that the size of the crystal and photodiode used by Polimaster are not secrets. Rather, Mr. Snowder admitted that any inventor in the world could determine the size of the cesium iodide crystal and photodiode used by Polimaster simply by opening its device. These admissions are fatal to Polimaster's trade secret claims. "If a physical feature of a product can readily be observed, if it may be easily ascertained or duplicated, it is not a trade secret." See *TGC Corp. v. HTM Sports*, 896 F. Supp. 751, 759 (E.D. Tenn. 1995) (applying the Uniform Trade Secrets Act).
- [27]. Polimaster also failed to identify any trade secret regarding the manufacturing procedures used to assemble its products. "[A] plaintiff who seeks relief for misappropriation of trade secrets must identify the trade secrets and carry the burden of showing that they exist." *Diodes, Inc. v. Franzen*, 260 Cal. App. 2d 244, 250-51 (Cal. Ct. App. 1968); see also *Universal Analytics Inc. v. MacNeal-Schwendler Corp.*, 707 F. Supp. 1170, 1177 (C.D. Cal. 1989) (plaintiff failed to identify "precisely which trade secret it alleges was misappropriated"), *aff'd*, 914 F.2d 1256 (9th Cir. 1990); *Twin Vision Corp. v. Bellsouth Communication Systems, Inc.*, No. 97-55231, 1998 U.S. App. LEXIS 13607 at *6 (9th Cir. June 22, 1998) (holding that plaintiff's conclusory assertions "that its engineering change orders ("ECOs"), schematics, and software constitute trade secrets" were insufficient).
- [28]. In denying Polimaster's motion for a preliminary injunction, the District Court ruled that Polimaster had not adequately identified specific manufacturing procedures employed by RAE that constituted Polimaster's trade secrets. During his deposition as Polimaster's corporate representative in this arbitration, Mr. Gordeev was still unable to identify what alleged manufacturing secrets Polimaster provided to RAE. At the hearing, Polimaster failed to describe what, if any, of its manufacturing processes constitute trade secrets. That failure is dispositive. The vague assertion that RAE received training with respect to the assembly, calibration and testing of the Polimaster products is insufficient to sustain Polimaster's burden of proof.

Polimaster Failed To Prove That RAE Acquired or Used Its Alleged Trade Secrets by Improper Means.

- [29]. Given that Polimaster has failed to prove the existence of any trade secrets in connection with its allegedly proprietary radiation detection technology, Polimaster cannot prevail on this claim. But the arbitrator also finds that Polimaster has also failed to prove that RAE acquired or used its alleged trade secrets by improper means.
- [30]. Polimaster has the burden of proof on its misappropriation claim, including the burden of proof as to the element of acquisition by or use of "improper means" by RAE. Under California law, "[i]t is the plaintiff's burden to show improper use as a part of its prima facie case. Proof that defendant's use resulted from independent derivation or reverse engineering is evidence that there was no improper use on its part. The defendant does not have a 'burden of proof' to make that showing." *Sargent Fletcher, Inc. v. Able Corp.*, 110 Cal. App. 4th 1658, 1669 (Cal. Ct. App. 2003). Thus, "if the evidence is evenly balanced, the party that bears the burden of persuasion must lose." *Id.* at 1666-67.

- [31]. But the evidence is far from evenly balanced. The uncontroverted evidence demonstrates that Dr. Hsi and his team began researching and developing a radiation detection prototype in early 2002 based upon independent research and publicly available information. Uncontroverted documentary evidence establishes that Dr. Hsi selected and began to source RAE's crystal and photodiode selections long before its contracts with Polimaster. Dr. Hsi also attended seminars offered by Berkeley Nucleonics Corporation and Hamamatsu in the fall of 2002 that detailed publicly available information about making dosimeters, ratemeters, and isotope identifiers; how to calibrate radiation detection devices; and the use of materials such as cesium iodide, lithium iodide, and photodiodes applied to radiation detection. RAE finished the prototype that ultimately led to the GammaRAE II by the end of 2002.
- [32]. The algorithms contained in the source codes of the respective devices, which Polimaster's expert described as the heartbeat of the devices, the feature that determines their relative precision, efficiency and performance, and the feature that is the fingerprint of their respective developers, are entirely different. The electronic circuitry and wiring boards of the respective devices are entirely different.
- [33]. The similarities that Polimaster purports to rely on pertain to elements that have been in the public domain for years and have been publicly disclosed by Polimaster. Furthermore, none of these supposed similarities is contained in any of the technical or engineering documentation Polimaster provided RAE pursuant to the License Agreement. On the contrary, the few pages of technical documentation pertaining to Polimaster's detector block provided to RAE do not identify its component parts. Polimaster failed to meet its burden of proof.

B. Polimaster Failed to Prove a Breach of the License Agreement Based on the Use of Any Allegedly Proprietary Information.

- [34]. Polimaster failed to prove that RAE used any of its allegedly "Proprietary Information" to develop or manufacture GammaRAE II in breach of the License Agreement. Under the License Agreement, Polimaster supplied RAE with completed radiation detector blocks (sometimes referred to as "Unique Components"), which RAE was to use in manufacturing the licensed products. As a result the parties agreed, and the License Agreement expressly provides, that Polimaster would not disclose what it claimed were its manufacturing secrets with respect to the radiation detector blocks; but the fact that Polimaster was to supply RAE with completed detector blocks made it unnecessary to do so. This was also consistent with both sides' wish to make the proprietary information definition "as narrow as possible."
- [35]. Accordingly, the definition of Proprietary Information in the License Agreement is limited to "a set of Engineering and Technical documentation as well as manufacture [sic] secrets that in the aggregate with the unique components is [sic] necessary and sufficient for manufacture of the 'License Products.'" This set of information is listed in Appendix 2: List of Proprietary Information, and expressly excludes "Constructor Documentation" for the detector blocks. Indeed, none of the engineering or technical documentation listed in Appendix 2 of the License Agreement contains information identifying the components or design specifications of Polimaster's detector blocks.

- [36]. The evidence demonstrates that the parties acted in the manner contemplated by the License Agreement – Polimaster did not provide RAE with any significant design or manufacturing information pertaining to its radiation detector blocks. Like the License Agreement, the design documentation provided to RAE when its engineers were trained in Minsk expressly excludes design documentation "for the specific parts manufactured and supplied by Polimaster," i.e., the detector blocks.
- [37]. None of the alleged detector block similarities upon which Polimaster purports to rely in this arbitration is even contained in the technical documentation Polimaster provided RAE, defined as "Proprietary Information" under the License Agreement. On the contrary, each of these purported similarities involves information that has been in the public domain for many years, and that was both publicly disclosed by Polimaster and readily ascertainable from an examination of its products in the marketplace. As the District Court found, "in light of the fact that much of the information was publicly available, [Polimaster]'s discussion of the many similarities between the Gamma Pager PM 1703M and the GammaRAE II is insufficient to establish that RAE relied upon [Polimaster]'s technical documentation."
- [38]. As the District Court also ruled, it would be unreasonable to construe the term "Proprietary Information" to include information that was made publicly available by Polimaster, given controlling law and the parties' mutual intent to define the term in the License Agreement as narrowly as possible and industry standards. Polimaster's own expert, Mr. Snowden, conceded that he understands the term proprietary information to mean information that is not publicly available.
- [39]. Furthermore, Polimaster's attempt to broaden the term "Proprietary Information" to include information that has been in the public domain for years, and that was both publicly disclosed by Polimaster and readily ascertainable from an examination of its products in the marketplace, would violate California Business and Professions Code § 16600. Section 16600 provides that "every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void." Cal. Bus. & Prof. Code § 16600. Misappropriation of trade secret information constitutes a judicially-created exception to section 16600. *Scott v. Snelling and Snelling, Inc.*, 732 F. Supp. 1034, 1043 (N.D. Cal. 1990). But that exception does not extend to information in the public domain, or information voluntarily disclosed or readily ascertainable through reverse-engineering or other methods, none of which qualifies for trade secret protection. Even if Polimaster's unreasonable construction of the term "Proprietary Information" had been intended by the parties, and there is convincing evidence that it was not, such an agreement would prevent RAE from competing with Polimaster under circumstance in which no trade secrets are implicated, in violation of California law. Such an agreement would be void under Section 16600 and unenforceable here.
- [40]. Polimaster's only remaining basis for its misappropriation claim is algorithms. Polimaster submitted Mr. Snowden's expert report, which states that algorithms are the heartbeat of a radiation detection instrument, the feature that determines its relative precision, efficiency and performance, and the feature that is the fingerprint of its developer. It was on this basis that Polimaster successfully moved to compel the disclosure of RAE's confidential software codes containing its algorithms, despite the fact that, at that time, it had not contended that RAE had been provided its source code or algorithms, and had not even produced its own source code or algorithms for

comparison in this arbitration. At that time, however, Polimaster accused RAE of reverse engineering the binary code containing its algorithms that had been provided under the License Agreement.

- [41]. The results did not bear out Polimaster's assertions. There is no dispute that the algorithm "fingerprints" simply do not match. Polimaster's own expert has conceded that there is no evidence of any significant parallels between the parties' respective source codes, and nothing to suggest that there are significant parallels to be found. He has also admitted that there is nothing to support a reasoned opinion that RAE reverse-engineered Polimaster's binary code to determine Polimaster's algorithms. RAE's expert Barbara Frederiksen was able to read the respective sets of source code. She concluded that although the respective sets of algorithms "might be accomplishing the same end purpose," since they are both designed for a hand-held radiation detector, but "they did so in a completely different way."
- [42]. RAE uses a different circuit, different 1C device, different passive components, different PCB artwork with different trace layout, different component placement, different PCB size, different connectors, and a different mounting mechanism than Polimaster. RAE's wiring boards are far more complex, with a greater number of active and passive components. Polimaster's expert, Mr. Snowden, admits that he did not perform any analysis comparing the electronic circuitry or wiring boards of the respective devices. He did not compare the main microprocessor circuit boards, the preamplifier circuit boards or the PCB layouts.
- [43]. The overwhelming evidence demonstrates that RAE developed its technology-- GammaRAE II-- independently. Polimaster has failed to meet its burden of proof

C. Polimaster Failed to Prove Its Claim for Breach of RAE's Alleged Obligation to Purchase 100 Units Per Month Pursuant to the Parties' Buy/Sell Agreement.

- [44]. Within months of granting an exclusive license to manufacture its products in the United States market, Polimaster breached the parties' License Agreement by usurping for itself one of the largest manufacturing orders for the products ever received in the United States - the Coast Guard order. In fact, Polimaster had been continuing to source licensed products directly to TSA for sale in the United States, in violation of RAE's exclusive manufacturing license, since the contracts were entered.
- [45]. RAE's exclusive license to manufacture Polimaster's pager devices sold in the United States market was the entire basis upon which the parties entered the Buy/Sell Agreement. Without the exclusive license to manufacture the licensed products, RAE had no reason to buy any components from Polimaster and no legal right to do anything with them. Polimaster has conceded that the License Agreement and Buy/Sell Agreement were interrelated; that the Buy/Sell Agreement was entered in conjunction with the License Agreement; and that the purpose of the License Agreement to Polimaster was to facilitate the sale of completed radiation detector blocks by Polimaster to RAE. Polimaster's breach of RAE's exclusive license to manufacture its products relieved RAE of any

obligation to purchase detector blocks from Polimaster under the Buy/Sell Agreement. *See Cutler Lab Inc. v. Twining*, 221 Cal. App. 2d 302, 314-16 (Cal. Ct. App. 1963) ("Where performance is possible but the fundamental reason for both parties entering into the contract has been frustrated by an unanticipated supervening circumstance which destroys the value of performance by the party standing on the contract, performance is excused.").

- [46]. Polimaster also suspended the License Agreement and Buy/Sell Agreement on April 7, 2004, informing RAE that it would stop delivery of the detector blocks to produce the licensed products at RAE's manufacturing facility in China. Polimaster never withdrew this unilateral "suspension" of the agreements, and ultimately terminated them. Pursuant to paragraph 9.3(b), Polimaster's suspension and ultimate termination of the Buy/Sell Agreement terminated all of RAE's obligations under the contract: "If Polimaster terminates, both RAE's rights and obligations under this Agreement will automatically terminate in its [sic] entirety." Polimaster's failure to perform its obligations under the agreements also gave rise to the same result by operation of California law.
- [47]. A party claiming breach of contract must have either performed its obligations under the contract or have an excuse for non-performance. *Otworth v. Southern Pac. Transportation Co.*, 166 Cal. App. 3d 452, 459 (Cal. Ct. App. 1985) (citing *Lortz v. Connell*, 273 Cal. App. 2d 286, 290 (1960)). Polimaster's breach of RAE's exclusive manufacturing rights and unilateral "suspension" of the agreements on April 7, 2004 excused RAE from any obligation to purchase a minimum number of detector blocks from Polimaster. *See Torrey v. Shea*, 29 Cal. App. 313, 319-20 (Cal. Ct. App. 1916) ("the willful and inexcusable failure of one party to perform a material part of a contract on his part to be performed is tantamount to an abandonment of the entire contract; and clearly, if plaintiffs in the present case so failed, they should not be permitted to recover damages for the refrisai of the defendants to further comply with the contract."). "It is well settled that the breach of an important condition may excuse the other party from performance... 'A party complaining of the breach of a contract is not entitled to recover therefore unless he has fulfilled his obligations.'" *Wiz Technology Inc. v. Coopers & Lybrand LLP*, 106 Cal. App. 4th 1, 12 (Cal. Ct. App. 2003) (quoting *Pry Corp. of America v. Leach*, 177 Cal. App. 2d 632, 639 (Cal. Ct. App. 1960)).

D. Polimaster Failed to Prove Its Claim for Unfair Competition.

- [48]. Polimaster claims that 'RAE's unfair and deceitful conduct in concealing its intent and efforts to develop a product in competition with Polimaster's products violates the California Unfair Trade Practices Act,' California Unfair Trade Practices Act, Cal. Bus. & Prof. Code § 17200 *el seq.* But Polimaster's claim for unfair competition, based on RAE's alleged misappropriation of trade secrets and breach of the License Agreement, fails for the reasons discussed above.
- [49]. Polimaster's suggestion that RAE engaged in unfair competition by misrepresenting its intentions to compete with Polimaster is entirely unfounded. In fact, the evidence presented at the hearing makes clear that no such misrepresentation was ever made. During the negotiations, RAE expressly declined Polimaster's request that it agree not to compete with Polimaster, an agreement that appears nowhere in any of the written contracts, and that would have violated California law in any event. Furthermore, RAE expressly refused to treat publicly available information as Polimaster's "proprietary information," and as negotiations continued, the parties mutual intent was to define the term in the License Agreement "as narrowly as possible."

- [50]. Although RAE had no obligation to disclose its business strategy to Polimaster, throughout the parties' relationship RAE never concealed its intent to develop its own technology and repeatedly advised Polimaster of its plans.
- [51]. For example, in August 2003, RAE informed Polimaster of its ongoing plan to integrate radiation detection into its chemical sensing product and advised Polimaster that although it would be RAE's first choice as a supplier, RAE reserved the right to seek other suppliers or to develop its own product. In August of 2004, RAE informed Polimaster that its inquiry with respect to crystal suppliers was in connection with its ongoing development program, and days later, made clear that it did not consider the combination of a scintillating crystal and photodiode, which had been in the public domain for many years, to be Polimaster's proprietary technology.
- [52]. In contrast to RAE's candid communications, Polimaster simply disregarded RAE's exclusive right to manufacture its products and usurped the Coast Guard order for itself. In the course of doing so, Polimaster brazenly told RAE that it was trying to convince TSA to abide by the License Agreement and promised to inform RAE as soon as it received any information -while failing to disclose that months earlier, it had purported to grant GNP (another corporation formed by TSA's owner) the same rights it had conveyed to RAE under the License Agreement. Four days after this communication, Polimaster entered a contract with GNP to manufacture the licensed products for the Coast Guard order. Nearly three weeks after entering this contract, and despite its promise to inform RAE as soon as it received any information, Polimaster wrote to RAE apologizing for the long silence, and again, failed to disclose that TSA had formed GNP, that Polimaster had purported to make GNP its exclusive distributor in the United States, or that Polimaster had entered a sales contract with GNP to fill the Coast Guard order. Polimaster ultimately informed RAE that in light of its prior relationship with TSA, it would continue to disregard RAE's contractual rights, and that in order for the parties to continue to do business, RAE's license would need to be substantially modified (for the benefit of Polimaster and TSA and at RAE's expense) and RAE would need to agree not to compete with Polimaster.
- [53]. Polimaster's attempt to recover damages on its claim for unfair competition fails. It is axiomatic that damages are not recoverable on a section 17200 claim, and Polimaster has not given RAE any money or property that is subject to restitution under the statute. *Korea Supply Co. v. Lockheed Martin Corp.*, 29 Cal. 4th 1134, 1144-45, 1149 (Cal. 2003).
- [54]. Polimaster has failed to prove this claim.

E. Polimaster's Alleged Damages for Breach of the Buy/Sell Agreement Are Unfounded and Unrecoverable.

- [55]. In discovery, Polimaster failed to identify an expert witness regarding its alleged damages and failed to produce any documents to support them. At the hearing, Polimaster presented the testimony of its own accountant, setting forth a hypothetical damages model that bore virtually no relationship to the terms of the Buy/Sell Agreement or the parties' conduct with respect to it. Among the many flaws in this unfounded damages model were the following:

- Polimaster assumes that RAE was required to buy three times more than the minimum number of units the contract requires.
- Polimaster assumes that RAE was required to buy more costly components than the contract requires, units that RAE *never* actually purchased but that involve alleged profit margins for Polimaster substantially higher than the units that RAE actually purchased. Polimaster also manipulated its assumptions regarding RAE's hypothetical purchases in order to use the highest price per unit permitted in the agreement, and assumed that RAE was obligated to purchase more expensive kits, rather than detector blocks, during a 17-month period in which RAE actually purchased detector blocks only. By adopting this assumption, not based on the facts, Polimaster was able to nearly double its alleged profit per unit.
- Polimaster initially failed to credit RAE for any of the substantial number of units it did purchase. When it purported to remedy this flaw, it did so by subtracting the lower profit per unit figure for RAE's purchases from its inflated hypothetical profit per unit numbers, resulting in an insupportable comparison. In reality, RAE's purchases satisfied any obligation it may have had, and thus give rise to no damages at all.
- Despite the plain language of the Buy/Sell Agreement, ¶9.3(b), Polimaster assumes that RAE remains obligated to purchase the minimum number of units. This assumption is incorrect since Polimaster suspended the agreement and informed RAE that it was going to stop delivery of the units. Indeed Polimaster's so-called damages model assumes that RAE is still obligated to purchase more units than the contract requires, despite the fact that for years, Polimaster has refused to deliver units and taken the position that RAE has no legal right to do anything with them. Polimaster also ignored the liquidated damages provision of the Buy/Sell Agreement.
- Polimaster fails to account for its obligation to purchase units from RAE.

[56]. Polimaster's purported damages model is unfounded, was not subjected to discovery pursuant to the rules applicable to this arbitration and is entitled to no weight in this analysis. Polimaster has failed to meet its burden of proof with respect to damages.

F. Polimaster Is Not Entitled to a Permanent Injunction.

[57]. Polimaster's request for a permanent injunction precluding RAE from selling any radiation detector that uses a scintillating crystal and photodiode, including GammaRAE II, NeutronRAE II and AreaRAE is insupportable. Polimaster has failed to cite any authority authorizing a permanent injunction prohibiting RAE from making use of technology that has been in the public domain for decades and that has been disclosed by Polimaster on the internet and elsewhere. None of this information is a trade secret and any contract to treat publicly available information as Polimaster's proprietary information would violate California law prohibiting the enforcement of contracts not to compete. Cal. Bus. & Prof. Code § 16600. Polimaster has also failed to demonstrate the inadequacy of a damages remedy. Cal. Civ. Code § 3422; *see also* Cal. Civ. Code § 3274 (providing that compensation is the general remedy afforded by California law and limiting the availability of specific and preventive relief). In addition, Polimaster's request to enjoin the sale of RAE's AreaRAE product is beyond the scope of its arbitration demand.

G. Polimaster's Breach of RAE's Exclusive License to Manufacture Polimaster's Pager Products Is Uncontroverted.

- [58]. Section 2.3 of the License Agreement grants RAE an exclusive license to manufacture Polimaster's pager products to be sold "into the economic turnover in the territory of the USA, with agreeing conditions with company TSA Systems, Ltd., CO, USA." TSA's consent is reflected in the agreement between TSA and RAE, executed in Sunnyvale at the same time Polimaster and RAE entered the License Agreement and Buy/Sell Agreement: "Whereas, RAE and Polimaster has [sic] entered into an agreement to license and manufacture Polimaster products for distribution in certain territories worldwide with TSA consent."
- [59]. Polimaster's argument that RAE's exclusive license was conditioned on TSA's agreement, and that agreement was never obtained, simply ignores the contracts at issue, and the controlling admissions of its own corporate designee. Under California law, the meaning of a contract is determined by the mutual intent of the parties. *Pacific Gas & Elec. Co. v. G. W. Thomas Drayage & Rigging Co.*, 69 Cal. 2d 33, 38 (Cal. 1968). TSA, through its CEO and President Alan Frymire, admitted that it consented to RAE's exclusive license to manufacture Polimaster's pager products at the conclusion of the Sunnyvale meetings in which the three contracts were executed by Polimaster, TSA and RAE. Mr. Gordeev, Polimaster's corporate designee, admitted the same in his deposition. Polimaster understood that the condition with respect to TSA's consent had been satisfied by the conclusion of the negotiations and execution of the agreements in Sunnyvale. As the testimony of all parties demonstrates, and as the License Agreement expressly provides, RAE was granted an exclusive license to manufacture Polimaster's pager products sold in the United States market.
- [60]. Furthermore, Polimaster admits that at the time of the dispute with respect to the Coast Guard order, it wanted to proceed in the manner to which the parties had agreed previously - that RAE would manufacture, TSA would sell and Polimaster would sell unit components to RAE. Finally, Polimaster admits that TSA or GNP (an alter-ego company Frymire formed to take over selling Polimaster's units in the United States) ultimately talked Polimaster into manufacturing the units used to fill the Coast Guard order itself.
- [61]. Finally, Polimaster claims that it was not a party to the License Agreement, which it Polimaster signed, but that is contradicted by Polimaster's own judicial admissions in the Complaint it filed in the District Court and in its Demand for Arbitration. The hearing testimony demonstrated that Polimaster was a party to the License Agreement.
- [62]. Polimaster failed to prove any violation of the federal Procurement Integrity Act (the "Act"), 41 U.S.C. § 423, and its accusations of criminal misconduct on the part of the responsible Coast Guard officer and RAE are unsupported. As discussed in detail in RAE's pre-hearing brief, the Act prohibits a participant in the contracting process from knowingly obtaining "*contractor bid or proposal information or source selection information* before the award of a Federal agency procurement contract to which the information relates." 41 U.S.C. § 423(b) (emphasis added). "Contractor bid or proposal information" and "source selection information" are very specific and formal documents in the government procurement process, methodically prepared and usually signed by a government official.⁴

⁴ There is no evidence that anyone from the Coast Guard ever sent, or that RAE ever knowingly received, "contractor bid or proposal

- [63]. Furthermore, Polimaster's accusations of misconduct in connection with RAE's unsuccessful efforts to obtain the Coast Guard order are irrelevant. In this arbitration, RAE is not contending that it should have been awarded the Coast Guard order, or would have been awarded the order but for TSA's and Polimaster's misconduct. Rather, it seeks to recover damages for breach of its exclusive right to manufacture the products used to fill that order once it had been obtained by TSA, manufacturing rights that Polimaster usurped for itself in breach of the License Agreement.
- [64]. The argument that RAE's action against TSA for breach of the contract between RAE and TSA, fraud and other torts, precludes RAE from recovering its damages for Polimaster's breach of the License Agreement (a separate and distinct contract) is simply wrong. These two disputes concern different contracts, between different parties. Polimaster cites no authority to support its position that RAE's settlement of its case against TSA is an accord and satisfaction of its claim against Polimaster.⁵
- [65]. There is no evidence that Polimaster breached RAE's exclusive manufacturing license because RAE was unable to perform. RAE's exclusive manufacturing license was not conditioned on whether it was using kits supplied by Polimaster or had begun to manufacture the products using only Polimaster's detector blocks. Furthermore, the evidence demonstrates that RAE was always able to perform under the License Agreement. At about the same time that Polimaster was usurping RAE's exclusive license to manufacture the units used to fill the Coast Guard order, RAE manufactured a large order for the United States Marine Corps. Polimaster's records also reflect that by the time the Coast Guard order was placed, RAE was no longer purchasing kits from Polimaster and had transitioned into the next manufacturing phase in which it obtained only detector blocks from Polimaster.
- [66]. Polimaster's argues that RAE has not proven damages in connection with two contracts Polimaster entered to manufacture units for TSA on March 26, 2004, on the basis of Polimaster's assertion that "no such sales actually took place on that date." But Polimaster did not present any evidence that these sales were not made, and the TSA contracts relied on by RAE's expert were the best and only evidence available with respect to Polimaster's breach of RAE's exclusive license. Polimaster's assertion that these sales actually occurred on subsequent dates is irrelevant, and is entitled to no weight in light of Polimaster's failure to abide by its discovery obligations. Despite its obligation to produce all of its invoices relating to RAE's counterclaim, Polimaster produced none. In fact, Polimaster admits that in general, it produced "only documents that we believe support our position," in flagrant violation of the controlling rules. Under these circumstances, Polimaster will not be permitted to attack RAE's damages evidence on the basis of its own self-serving characterization of contracts and invoices that it failed to produce, despite a clear obligation to do so. It is axiomatic that when "weaker and less satisfactory evidence is offered when it was within the power of the party to produce stronger and more satisfactory evidence, the evidence offered should be viewed with distrust." Cal. Evid. Code § 412. This rule applies for even stronger reasons here, where Polimaster is in possession of these documents, and was obligated to produce them, but

information" or "source selection information" within the meaning of the Act. Chris Wrenn testified that a Coast Guard officer blind copied him on an email discussing the relationship between TSA, Polimaster and RAE because of confusion over the respective versions of the Polimaster devices supplied by TSA and RAE. There is no evidence that Mr. Wrenn ever asked to be copied on the email or did anything in response to receiving it. This testimony is patently insufficient to establish a violation of the Act on the part of the Coast Guard officer who sent the email, much less Mr. Wrenn or RAE.

⁵ Polimaster's efforts to attribute legal significance to the fact that RAE did not sue Polimaster in its action against TSA, and is asserting its claim against Polimaster in this arbitration as a counter-claim, are also specious. Among other things, Polimaster is outside the jurisdiction of the United States District Court in which RAE prosecuted its claims against TSA, and unlike the RAE-TSA contract, RAE's contract with Polimaster contains an arbitration clause.

did not do so apparently because it believes the documents do not support its position.

[67]. It is found that Polimaster breached the exclusive manufacturing license Polimaster granted RAE in the License Agreement.⁶

H. RAE Has Sustained Damages in Excess of \$2,412,432 from Polimaster's Breach of RAE's Exclusive Manufacturing License.

[68]. As a result of Polimaster's disregard of RAE's exclusive license to manufacture Polimaster's products for distribution in the United States, RAE has been damaged by at least \$2,412,432 in lost sales *to TSA alone*. The calculation of these damages is simple and unassailable. RAE's expert, Bjorn L. Malmlund, reviewed evidence (in the form of purchase orders and invoices) of Polimaster's sales to TSA obtained from TSA. Those sales should have been made by RAE. Mr. Malmlund took the prices RAE would have gotten from TSA for the products per the RAE-TSA contract and subtracted what it would have cost RAE to manufacture the products had Polimaster not usurped that role for itself. That calculation reflects damages in the amount of \$2,412,432 in lost sales to TSA alone.

[69]. The additional damages RAE has incurred based on Polimaster's other sales to TSA, and to other parties for "into the economic turnover in the territory of the USA" cannot be determined because Polimaster failed to meet its obligations under the discovery rules governing this arbitration. Rule 17(a) of the JAMS Comprehensive Rules required Polimaster to provide RAE with all non-privileged documents and other information relevant to the dispute or claim, including RAE's counterclaim for breach of its exclusive manufacturing license. Rule 17(d) provides that Polimaster, as it became aware of new documents or information, including experts who may be called upon to testify, continued to be obligated to provide RAE with all such relevant, non-privileged documents. Despite these obligations, which RAE met, Polimaster admits that it has not even tried to produce all relevant documents and evidence, and has instead, only produced "documents we believe support our position." Specifically, Polimaster admits that it did not produce its shipping invoices and contracts relating to licensed product for turnover into the territory of the United States, relevant evidence in Polimaster's sole possession necessary to document the full extent of the damages RAE sustained resulting from Polimaster's breach.

[70]. Polimaster's failure to comply with its discovery obligations undermines its entire case. Polimaster's misconduct has unfairly deprived RAE of the ability to prove the full extent of its damages. RAE is entitled to recover all of the damages reflected in the documentation produced by TSA - \$2,412,432.

I. Attorney's Fees and Costs.

[71]. Polimaster requested attorney's fees and costs in its demand. RAE requested attorney's fees in its counterclaim. RAE is found to be the prevailing party. Determination of attorney's fees and costs is reserved for further hearing.

⁶ TSA's purported termination of the TSA-RAE contract has nothing to do with the License Agreement, or RAE's counterclaim.

IV. Conclusion and Further Proceedings

- [72]. 1. Given that some portions of the testimony during this hearing were given subject to the protective order entered herein, this Interim Award shall remain confidential and is hereby sealed pending the completion of meet and confer efforts by counsel to determine whether any portion of it or the ensuing Arbitration Award ought hereafter to be sealed. A telephonic AMC shall be held at 8:30 a.m. on Thursday, July 19, 2007, to discuss this issue.
2. Polimaster has failed to prove its claims for misappropriation of trade secrets, unfair competition, and breach of contract and is not entitled to any relief herein, whether monetary, injunctive, or declaratory.
3. RAE has proven its counterclaim and is awarded damages in the amount \$2,412,432, which sum Polimaster shall pay to RAE.
4. RAE is the prevailing party and may file an application for attorney's fees and costs by July 20, 2007, together with any evidence and argument. Claimant may file opposition evidence and argument by August 3, 2007, and Respondents may reply by August 10, 2007. The matter shall be submitted for final decision at that time unless either party in its papers requests an oral hearing. If requested, the oral hearing shall be conducted by telephone conference on August 17, 2007, at 8:00 a.m. PST, unless counsel otherwise agree or the arbitrator otherwise orders upon good cause shown.
5. The further determinations to be made at any further hearing or based on written submissions shall be embodied in a Final Award which shall also incorporate the contents of the Interim Award. It is not intended that this Interim Award be subject to review pursuant C.C.P. §§ 1284 or 1285 *et seq.*

[73]. IT IS SO ORDERED.