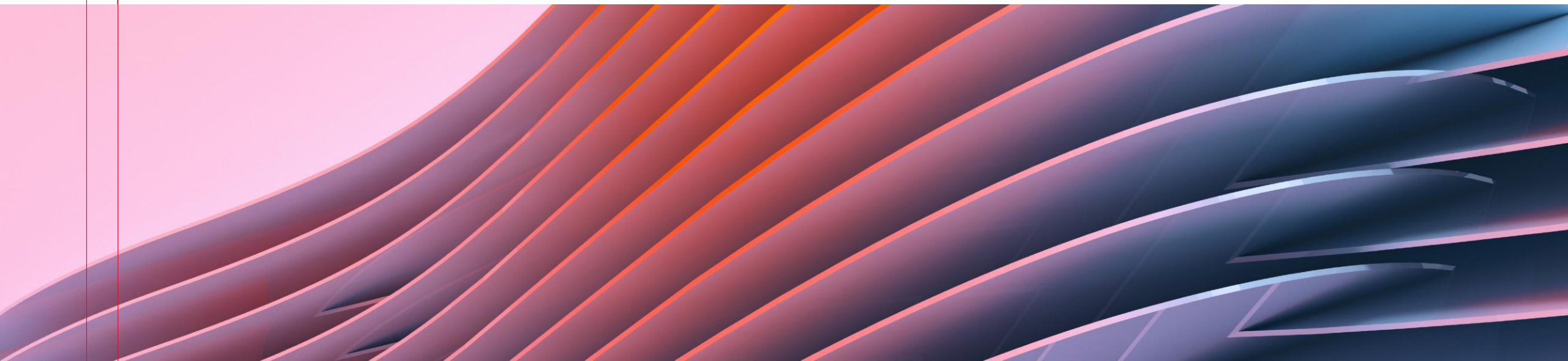
APRIL 10, 2024

Trade Secret Update: 2024 Legal Developments and Trends

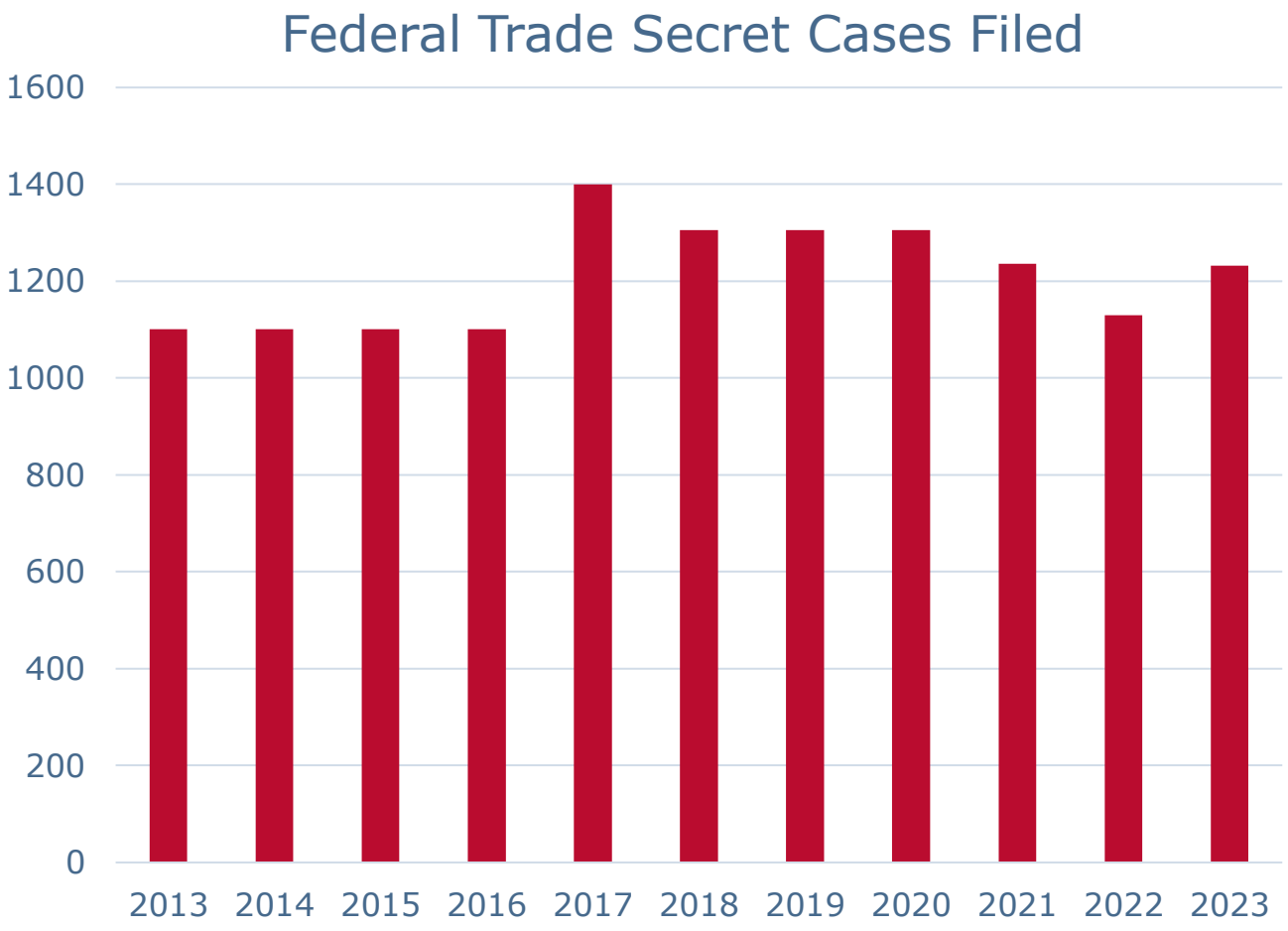


Agenda

1. Rise in Trade Secret Litigation
2. Recent and Anticipated Trade Secret Decisions
3. Circuit Split on Recovery of Avoided Costs as Unjust Enrichment Damages
4. Current Climate Surrounding Non-Compete Agreements
5. NDA Protections for Trade Secrets
6. Trade Secrets and Generative AI

Rise in Trade Secret Litigation

Trade Secret Cases on the Rise



Source: Lex Machina and Law360

2013–2016
Trade secret filings remain steady at roughly 1,100 case annually.

2017–2020
Trade secret filings increase to over 1,300 case annually with a peak year following the 2016 enactment of the DTSA.

2021-2022
Trade secret filings drop during the pandemic.

2023
Trade secret filings increase again.

Why do you believe there has been an increase in trade secret litigation?

A. Increased employee mobility
B. Portability of electronically stored information
C. More avenues to invalidate patents
D. Expansion of trade secret cases by Defend Trade Secrets Act
E. All of the above

What accounts for the increase in trade secret litigation?

A. Increased employee mobility
B. Portability of electronically stored information
C. More avenues to invalidate patents
D. Expansion of trade secret cases by Defend Trade Secrets Act
E. All of the above

Increase in Trade Secret Filings

- According to Lex Machina, between 2019 and 2023, trade secret plaintiffs in federal cases that went to trial won 86% of case (~30% higher than rate across all federal cases).
- Trade secret cases rose as patent litigation cases began to fall. Law360 attributes the drop to changes in patent law providing more avenues to invalidate patents, making litigation more unpredictable.
- The Defend Trade Secrets Act permits a cause of action for misappropriation outside the U.S. under certain circumstances.

Significant Trade Secret Damages Awards

	Initial Award	Status
Appian v. Pegasystems (May 2022)	$2.01 billion	Appeal Pending Oral argument -- November 2023
Epic Systems Corp. v. Tata (July 2022)	$940 million Trial court reduced to $420 million	Award reduced to $280 million on appeal.
Motorola v. Hytera (Feb. 2020)	$764 million (over $400 million in punitives) Trial court reduced to $540 million	Appeal Pending Oral argument -- December 2023.
House Canary v. Title Source Inc. (May 2018)	$740 million ($470 million in punitives)	Texas Fourth Court of Appeals reversed the $740 million judgment and indicated House Canary was permitted either to seek judgment on a $201.6 million breach of contract claim or retry the entire case.

Recent and Anticipated Trade Secret Decisions

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Can a compilation that includes some information that can be found from public sources qualify for trade secret protection?

Yes.

No.

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Yes.

No.

Allstate Insurance Co. v. Fougere, 79 F.4th 172 (1st. Cir. 2023).

- Allstate filed suit against two former agents for trade secret misappropriation, claiming the agents had retained "book of business" spreadsheets that included Allstate customer data.
- The customer data included names, addresses, email addresses, policy types, renewal dates, and insurance premium information.
- The trial court, rejecting defendants' argument that the information could not qualify for trade secret protection because it could be obtained from publicly available sources, granted Allstate's summary judgment motion.

Allstate Insurance Co. v. Fougere

The First Circuit affirmed the district court ruling, finding that

> the inclusion of some information in compilations which could have been obtained from public sources does not mean the compilations were not trade secrets[.]

79 F.4th at 189.

Allstate Insurance Co. v. Fougere

The court reasoned that a trade secret finding was appropriate because

> the compilations would not have been known outside of Allstate, and, to the extent they were duplicable, could only be recreated at immense difficulty.

79 F.4th at 190.

Appian Corporation v. Pegasystems, Inc. and Zou

Circuit Court of Fairfax County, Virginia (Civil Action No. 2020-07216)

- Appian and Pegasystems are archrivals in high-end process automation software.
- On May 9, 2022, jury awarded $2.036 billion for trade secret theft and $23 million in attorneys' fees.
- Unjust enrichment theory – defendant was able to improve its software and compete better.
- Trial court required that Appian prove only Pega's total revenues from all products, forcing Pega to prove any revenues not caused by alleged misappropriation.

Appian v. Pegasystems

Appeal Arguments:

- Pega argues on appeal that Appian should have the burden of proof on unjust enrichment, and that trial court improperly shifted burden of proof on damages.
- Trial court's jury instruction required the plaintiff to prove defendant's sales, with the defendant having to prove any portion of those sales not caused by misappropriation. Is this inconsistent with plaintiff's burden to prove causation?
- Oral argument held in November 2023.

Motorola Solutions, Inc. v. Hytera Communications Corp., 436 F.Supp.3d 1150 (N.D. Ill. Jan. 31, 2020)

- Motorola sued Hytera for theft of thousands of Motorola's technical and confidential documents.
- Motorola alleged that Hytera used the documents (trade secrets and source code) to develop a 2-way radio that was functionally indistinguishable from Motorola.
- Motorola sought and was awarded damages of $764 million for Hytera's *world-wide* sales of the radio.

Motorola v. Hytera

- The initial award was reduced to $540 million.
- Hytera appealed to the Seventh Circuit, arguing that the trial court erroneously awarded Motorola damages for Hytera's non-US sales and improperly disgorged *all* of Hytera's profits.
- Oral argument held in December 2023.

Circuit Split on Recovery of *Avoided Costs* as Unjust Enrichment Damages

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Whether Avoided Costs Are Recoverable as Unjust Enrichment Damages

Circuit courts are split on whether unjust enrichment damages in the form of *avoided costs* should be granted in trade secret cases when the avoided costs "proxy" bears no relationship to the plaintiff's harm or the defendant's gain.

Avoided Costs as Unjust Enrichment Damages in the Third Circuit

PPG Industries v. Jiangsu Tie Mao Glass, 47 F.4th 156 (3rd Cir. 2022).

- Affirmed damages award based on plaintiff's development costs as a proxy for defendant's avoided costs even when defendant sold no products incorporating misappropriated technology and plaintiff suffered no actual loss.

- Because defendant "used" the trade secrets, plaintiff was entitled to avoided costs as unjust enrichment damages.

Avoided Costs as Unjust Enrichment Damages in the Seventh Circuit

Epic Systems v. Tata Consultancy Systems, 980 F.3d 1117 (7th Cir. 2020).

Affirmed unjust enrichment award of $140 million because defendant's benefit was a "significant head start" in operations (through competitive market analysis), which the jury could value based on avoided research and development costs, even though trade secrets were not used to make actual sales.

Second Circuit Rejects Avoided Costs as Unjust Enrichment Damages

In *Syntel v. TriZetto,* 68 F.4th 792, 813 (2nd Cir. 2023), the Second Circuit found that awarding avoided costs as unjust enrichment without corresponding harm to the trade secret owner "unhinges avoided costs from the [DTSA]'s compensatory moorings. . . ."

Syntel v. TriZetto

- TriZetto licensed trade secrets related to software development for the healthcare industry to a subcontractor, Syntel.
- Litigation was filed after the business relationship dissolved.
- Jury found Syntel misappropriated TriZetto's trade secrets and awarded damages for avoided development costs and lost profits.

Syntel v. TriZetto

- On appeal, the Second Circuit acknowledged actual losses and unjust enrichment damages can be recovered. But "avoided cost" damages are appropriate *only* when tied to lost value of a trade secret or a defendant's gain of a benefit not compensable by a lost profits award.
- Second Circuit affirmed the award of lost profits to TriZetto and permanent injunction enjoining Syntel from using TriZetto's trade secrets.
- However, the court determined that the trade secrets had increased in value and TriZetto had not suffered damage to justify (unjust enrichment award) for avoided development costs.

Petition for Writ of *Certiorari*

- In an effort to resolve the circuit split, a petition for writ of certiorari was filed in *Tata Consultancy Services Ltd. v. Epic Systems Corp.*

- On November 20, 2023, the U.S. Supreme Court denied the petition.

Current Climate Surrounding Non-Compete Agreements

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Non-Compete Agreements

- Unlawful in California, Minnesota, North Dakota, and Oklahoma.
- New York City considering potential ban on non-compete agreements.
- State law varies on enforceability, duration, and scope.
- FTC has proposed national ban on non-compete agreements, and a final vote on this proposal is expected in April 2024.
- If approved, compliance will be required 180 days after the final rule is published.

FTC Non-Compete Clause Rule at 3505 - 3506

a. Trade Secret Law

Trade secret law provides employers with an alternative means of protecting their investments in trade secrets. Trade secret law is a form of intellectual property law that protects confidential business information.[300] It also serves as an alternative to the patent system, "granting proprietary rights to particular technologies, processes, designs, or formulae that may not be able to satisfy the rigorous standards for patentability."[301] Even where information meets standards for patentability, companies may choose to rely on trade secret law and not obtain a patent, because they wish to keep information out of the public domain.[302]

FEDERAL TRADE COMMISSION

16 CFR Part 910

RIN 3084–AB74

Non-Compete Clause Rule

AGENCY: Federal Trade Commission.
ACTION: Notice of proposed rulemaking.

NDA Protections for Trade Secrets

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Key Considerations for NDAs

1. Definition of Confidential Information
2. How the Information May (or May Not) Be Used
3. Protective Measures By the Receiving Party
4. Duration / Term (based on jurisdiction)
5. Obligations Upon Termination
6. Choice of Law and Venue
7. Remedies for Breach

Typical Remedies for Breach of NDA

- Money damages are available for breach of NDA.
- Equitable remedies, including injunctive relief, are available to prevent further breaches and to bar disclosures of confidential information.
- Courts are ill-equipped to "unring the bell" when confidential information has been released in the public domain. The disclosing party is usually limited to money damages for the breaches.
- Courts, in their discretion, may award equitable relief when contemplated by the specific language in the applicable non-disclosure agreement.

What remedy is available following a patent filing based on information disclosed under an NDA?

A. No remedy at all, because court cannot "unring the bell" after non-public information is made public

B. Money damages

C. Correction of inventorship under patent laws.

D. Transfer of patent ownership (depending upon NDA language).

E. Depending upon circumstances, any of the above may apply

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SiOnyx LLC v. Hamamatsu Photonics K.K., 981 F.3d 1339, 1352 (Fed. Cir. 2020).

- SiOnyx, a startup, and Hamamatsu, an established manufacturer interested in the SIOnyx technology, entered into an NDA to allow them to share confidential information relating to SiOnyx's technology and joint development opportunities.

- After Hamamatsu severed the relationship with SiOnyx, Hamamatsu filed for, and was awarded, several patents based on the confidential information shared under the NDA.

SiOnyx LLC v. Hamamatsu Photonics K.K.

- Hamamatsu also went on to develop and bring to market products based on this technology and the awarded patents.

- SiOnyx sued Hamamatsu for unjust enrichment, breach of contract, ownership of the patents that Hamamatsu was awarded, and injunctive relief to prohibit Hamamatsu from practicing the patents in question.

SiOnyx LLC v. Hamamatsu Photonics K.K.

- *SiOnyx* held that, a court, in its discretion, can transfer patent ownership as an equitable remedy for breach of an NDA, and the court's decision turned on the particularized patent ownership language in the NDA:

> The Receiving Party acknowledges that the Disclosing Party . . . claims ownership of the Confidential Information disclosed by the Disclosing Party and *all patent, copyright, trademark, trade secret, and other intellectual property rights in, or arising from, such Confidential Information*.

Id., 981 F.3d at 1351.

Trade Secrets and AI

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Potential Trade Secret Protection for Generative AI Output

- At least conceptually, AI-generated content can be subject to trade secret protection if the confidentiality requirements are satisfied.
- Unlike patent and copyright, there is no requirement under the Defend Trade Secrets Act, for example, that an inventor, developer, or generator of a trade secret be a "natural person" or that the origin of the idea even be identified.
- The output of generative AI in a "closed" platform therefore may be protected as a trade secret.

Trade Secrets and ChatGPT

- April 7, 2023: “Samsung’s trade secrets have reportedly leaked because employees shared too much info with ChatGPT”
- Samsung engineers at its semiconductor arm unintentionally leaked confidential data – including source code and internal meeting notes – while using ChatGPT to fix errors in their source code.
- The confidential data is now stored on servers in the possession of OpenAI.
- OpenAI terms of use do not provide for confidentiality of user information.

Questions?

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Full bio