Jordan Grotzinger (00:05):

Welcome to the Trade Secret Law Evolution Podcast, where we give you comprehensive summaries and takeaways on the latest developments and trends in trade secret law. We want you to stay current and ahead of the curve when it comes to protecting your company's most valuable assets. I'm your host Jordan Grotzinger.

Jordan Grotzinger (00:21):

Hey, everybody. Welcome to episode 38 of the podcast. Here with me today is my former guest. I'm glad to have him back, Justin Victor. How are you?

Justin Victor (00:36):

I'm fantastic. It's good to be returning to the office. It's even better to be returning to this podcast.

Jordan Grotzinger (00:43):

Great. Well, we're excited to have you. I can see that you're in the office. When did you start going back in?

Justin Victor (00:50):

I've been trying to go in at least two or three days a week this past month. I'd say my first return to the office was about three, four months ago, but we are expecting our second any day now. I apologize. I have my phone on. My return to the office may be cut off shortly by our second being born.

Jordan Grotzinger (01:14):

Oh, wow. Well, that's much more exciting than anything we're going to say today. That's awesome. That's really exciting. Yeah, if the phone rings and you got to jump out, I will happily take over and you do your thing. Congratulations. I hope everything goes smoothly. That is terrific.

Justin Victor (01:35):

Thank you.

Jordan Grotzinger (01:35):

Let's jump into the substance. Today, we're going to start by talking about President Biden's July 9th, 2021 executive order and the potential impact, the implementation of the order may have on trade secret protection. We're also going to discuss a recent case analyzing whether the plaintiff's allegations in a complaint were sufficient to survive a motion to dismiss. The issue in that case and what we do here is essentially take a deep dive into the statutory definition of the term use within the federal Defend Trade Secrets Act.

Jordan Grotzinger (02:20):

So Justin, you want to start off by talking about the executive order?

Justin Victor (02:25):

Certainly. It's important to start with context. Throughout President Joe Biden's campaign, he vowed that he was going to take measures that would eliminate and reduce the barriers for employees to seek

higher wages and get better benefits from their employers. On July 9th, 2021, President Biden took a concrete step towards that promise with the sweeping executive order.

Justin Victor (02:53):

Now, the executive order covered a variety of topics. It wasn't just focused on non-competes, but President Biden specifically signaled through this executive order that he was going to curtail the use of employer's use of non-competes. The executive order declares that a whole of government approach is necessary to address overconcentration, monopolization and unfair competition in the American economy. Of particular interest to many employers is the executive orders directive to the Federal Trade Commission, which encourages the FTC to use its rulemaking authority to restrict and reduce, or even ban, certain types of non-compete agreements.

Jordan Grotzinger (03:38):

Right. The FTC, I'm just going to speak for a minute here about what rulemaking means for those not familiar with administrative law or the administrative process. The executive branch of government includes various administrative agencies that are responsible for a particular subject matter. The FTC, the Federal Trade Commission, is the agency responsible for this subject matter, among others. These agencies have what's called rulemaking authorities to promulgate rules governing their subject matter. That is what the President has directed the FTC to do here with respect to non-competes.

Jordan Grotzinger (04:27):

Specifically, the order provides that quote, "The chair of the FTC is encouraged to consider working with the rest of the commission to exercise the FTC statutory rulemaking authority under the FTC Act to curtail the unfair use of non-compete clauses, and other clauses or agreements, that may unfairly limit worker mobility."

Justin Victor (04:56):

Taking a step back, non-compete agreements have become commonplace. According to the Biden administration, approximately one half of private sector businesses require at least some segment of their workforce to execute a non-compete agreement. This impacts between 36 to 60 million workers in the United States. I want to focus on the rationale behind non-competes and how it ties in to trade secrets.

Justin Victor (05:25):

A non-compete is exactly what it sounds like. It prevents an employee, typically a former employee, from working for, or in a similar role, working for a competitor or working in a similar role for a competitor than the previous job that they had. One of the main justifications behind having non-compete agreements is that these individuals may have had access to trade secret information. They may just have knowledge of trade secret information. They might know what trade secrets are being developed. I mean, they could take something over to their new employer and this non-compete period, a period of a year or a period of two years, a period of six months, essentially would allow that information to become stale before they go work for a competitor. That's one of the public policy justifications behind non-competes.

Jordan Grotzinger (06:18):

To be clear, the July 9th order doesn't immediately change anything. That's important. Rather, the FTC has to exercise its rulemaking authority under the FTC Act to essentially accomplish this mission. As a practical matter, it could be months before the FTC announces any specific rules and challenges to the FTC's authority will likely follow whatever rules the commission ultimately promulgates.

Justin Victor (06:54):

That's a critically important point. First of all, we don't know what the rules specifically are going to be. Is it going to be all non-competes that are going to be attacked, only specific types of non-competes, only for specific workers? We're really going to have to look at what those rules are and the challenge of those rules to see what the impact is on employers.

Jordan Grotzinger (07:13):

Yeah, and this order is in line with a relative sea change happening at the state level. For example, the Illinois General Assembly recently unanimously passed a bill that will significantly affect the legality of post-employment, non-competition and non-solicitation agreements between employers and their Illinois employees entered into after January 1st, 2022. Among other things, the bill prohibits non-solicitation covenants with employees who have actual or expected earnings of $45,000 per year or less. Similarly, in California, my state, it has been the law for a long time that non-competes are essentially unenforceable and can only be used to the extent necessary to prevent trade secret misappropriation, but not to prevent employee mobility.

Jordan Grotzinger (08:14):

The way I just said that, that non-competes are only allowed insofar as necessary to prevent trade secret misappropriation, it's kind of a misnomer. I mean, the reality is they're not enforceable, but you can enforce against trade secret misappropriation. Your agreement, and of course, non-compete and non-solicitation agreements are ubiquitous all across the country, as I think you mentioned. But in these states, and presumably more to the extent the FTC acts consistently with the President's directive, while you might be able to call an agreement a non-solicit or a non-compete, those titles are really broader than it's going to have to be.

Jordan Grotzinger (09:10):

Your agreement can say you can't solicit using trade secrets. You can't compete using trade secrets. That's already the law in California and some of these other states. But in California, and it looks like shortly in Illinois and presumably other states, employers are going to be so restricted as well. Trade secret misappropriation law will stand and that protection remains vital. But, the trend is that employees are becoming more free essentially to compete. If you have a skill and you can get a job, you can go work the job, even if it's with a direct competitor and sometimes even by soliciting employees from your competitor. You just can't steal trade secrets.

Justin Victor (09:54):

That brings us to the takeaways related to the July 9 order. I think the first takeaway for employers is they need to really be able to take a step back and figure out where am I operating and what are right now, even before this FTC order gets promulgated, what are the laws within the specific state that I operate in and how has this sea change nationwide, how has that impacted the enforceability or the legality of the restrictions that I have with my employees? I think now is a really good time to take a step back and see if the restrictions you have in place to protect trade secrets are in fact enforceable.

Jordan Grotzinger (10:37):

Yes, that is a good idea. You sort of touched on this in what you just said. I know we have a disclaimer at the end of every podcast, but let me just insert it here because I just spoke pretty broadly on what the law is in some of these states. This podcast is not legal advice. You need to look at the law in your particular state based on what the current rules are and you should be tracking how they might change based on this executive order and any new rules promulgated by the FTC.

Justin Victor (11:13):

The second takeaway we had related to this order is we need to see now what happens. An executive order is in place. There's been directives given to the chair of the FTC. Let's see what the FTC does. Let's see how broad the rule is, how broad the directives are, how narrow it is and what the specific challenges are to any potential proposed rule and how that will impact non-competes going forward. This is an evolving topic and I anticipate will be discussed on this podcast again. If I'm lucky enough, maybe I'll be invited back to provide updates later on once we see what happens.

Jordan Grotzinger (11:51):

Absolutely. I hereby invite you back right now. We'll even tolerate crying in the background.

Jordan Grotzinger (12:00):

The final takeaway, even though it's not really a takeaway from this executive order per se, because it's something companies should always be thinking about. But now, as always, you should ensure that the steps you're taking are sufficient to protect your trade secret information, particularly to the extent that the law is trending away from non-competes and non-solicits. But the bottom line is, you don't have to tie trade secret protection to employee mobility. Even if the law was that was black and white and was that employees can go wherever they want, the minute after they leave one company, they can go to a direct competitor that same hour, even if it was that clear. It's not. It's not black and white. The law differs from state to state. You can always have trade secret protection independent from employee mobility. That can always be built into contracts.

Justin Victor (13:08):

The next topic we're going to discuss is a recent Third Circuit decision from June of 2021. In this Third Circuit decision, the plaintiff was a pharmaceutical company that initiated litigation against two defendants. First, the former vice president of product development and a competitor pharmaceutical company that hired the former vice president alleging claims of trade secret misappropriation, breach of contract and tortious interference. The district court dismissed the plaintiff's claims four times allowing the plaintiff lead to amend three different times to meet the pleading requirements to sufficiently alleged a claim for misappropriation of trade secrets.

Jordan Grotzinger (13:52):

The third amended complaint, and a third amended complaint is actually your fourth complaint, because the original complaint is not numbered. It goes original, first amended, second amended, et cetera, when amendments are allowed. The third amended complaint, which also was dismissed by the district court, the trial court, alleged that shortly after the defendant former vice-president joined the defendant competitor, the competitor began developing "microsphere technology" products that the defendant competitor previously had not been developing or had experience with.

Jordan Grotzinger (14:30):

Now, microsphere technology is an injection technology for medication that eliminates the rapid delivery of high concentrations of drugs to the application site on the body. Instead, allows for a slower release of potentially irritating or highly-concentrated drugs.

Justin Victor (14:52):

The defendant competitor had announced that through product development it had invested $6 million in this technology. Now, the plaintiff saw that and they alleged that this rapid development in technology could not possibly have occurred without the misappropriation of the plaintiff's trade secrets. The plaintiff explained in the third amended complaint that they had invested over $130 million in such technology to get a product off the ground and had assigned 20 to 40 full-time employees to develop this technology. Therefore, based on the statements made by the defendant that they had developed this technology with only a $6 million investment in a short timeline, it must have been the result of misappropriation.

Jordan Grotzinger (15:38):

Not withstanding that, not withstanding the substantial monetary and labor investment by the plaintiff, the district court dismissed the third amended complaint and held that while the plaintiff had identified trade secrets, it failed to adequately allege how the defendants "used" those trade secrets. Specifically, the opinion stated that the complaint was speculative because it failed to explain why the plaintiff was the only potential source of information related to that microsphere technology or the development of the competitive product.

Justin Victor (16:19):

The Third Circuit reversed disagreeing with the district court's dismissal of the third amended complaint. The Third Circuit explained that it's reversal centered on the district court's definition of use or used. The district court defined the concept of used or used as replicating, replicating technology. To go to the code for a second under the Federal Defend Trade Secrets Act, specifically code section 1839 5(b), which defines misappropriation as, "The disclosure or use of a trade secret of another without express or implied consent."

Justin Victor (17:04):

Reviewing the statutory language of the DTSA, the Third Circuit found that the term use, while undefined within the statute, should be more broadly defined to include any exploitation of the trade secret that is likely to result in injury. Thus, marketing goods that embody the trade secret or employing the trade secret in manufacturing or to accelerate research or development, all constitute use under the statute.

Jordan Grotzinger (17:38):

By rejecting the district court's narrow definition of use, the Third Circuit found that the plaintiff had adequately alleged that the defendants used the plaintiff's trade secrets because the court was supposed to construe all reasonable inferences in favor of the plaintiff, including the two-decade investment and the $130 million it took to develop the microsphere technology compared to the defendant's compressed timeline with a much more minimal investment.

Jordan Grotzinger (18:10):

Justin, let's start going over the takeaways from this case.

Justin Victor (18:14):

Well, the first takeaway relates to the term use. The term use when it comes to misappropriation under the federal statute, should be given a broad definition, a broad interpretation by courts when considering and analyzing what conduct by a defendant constitutes misappropriation.

Jordan Grotzinger (18:36):

The second takeaway is that the test in the Third Circuit is that, specifically, improper use is, "Any exploitation of the trade secret that is likely to result in injury." Thus, marketing goods that embody the trade secret or employing the trade secret in manufacturing or to accelerate research or development, constitute use under the Defend Trade Secrets Act. We've been talking about the Third Circuit. Just for your information, that circuit includes Pennsylvania, New Jersey, Delaware, and the Virgin Islands. Hopefully, Justin, we get to litigate a case in the Virgin Islands over this issue. Also, I mentioned that the geographic scope of the circuit, but this test is logical. It makes practical sense. We expect it to be followed by other circuits.

Jordan Grotzinger (19:33):

Justin, what's the final takeaway here.

Justin Victor (19:36):

The final takeaway is if at first you don't succeed, try, try, try again. Here the plaintiff was given four bites at the apple to adequately plead their case for misappropriation. Even when it was struck down by the district court, they were able to succeed at the circuit court level and go forward with their allegations of misappropriation.

Jordan Grotzinger (19:57):

Yeah. For better or for worse, and I suppose it's for better because the whole point of this law game is justice, is it not? Courts are liberal in allowing amended complaints to see if the plaintiff can allege some set of facts that might implicate a viable cause of action or legal claim. It's just usually hard for the defense side, for that reason, to deliver a so-called knockout punch where you move to dismiss on the pleadings. Meaning not on the evidence or the summary judgment stage later, but on the pleadings and get a case dismissed for good. It happens. It's on the much rarer side. This is an example of a court allowing the plaintiff to refine its allegations over and over again to give that plaintiff the opportunity to allege a viable legal claim, if it can. That is what happened here.

Jordan Grotzinger (21:04):

Justin. Great to see you. It's always really fun doing this podcast with you. Do you know the sex of the baby yet?

Justin Victor (21:12):

We do. We're having a baby girl-

Jordan Grotzinger (21:15):

Awesome.

Justin Victor (21:15):

... any day now. My son is 18 months.

Jordan Grotzinger (21:18):

Oh, wow.

Justin Victor (21:19):

It's been a wild pandemic.

Jordan Grotzinger (21:21):

Hands are full. That's amazing. I'm super happy for you. Please keep me posted. I'll definitely be checking in soon. Thanks, everybody. Have a good one.

Jordan Grotzinger (21:35):

Okay, that's a wrap. Thanks for joining us on this episode of the Trade Secret Law Evolution Podcast. As the law evolves, so will this podcast. We value your feedback. Let us know how we can be more helpful to you. Send us your questions and comments. You can reach me by email at grotzingerj@gtlaw.com or on LinkedIn. If you like what you hear, please spread the word and feel free to review us. Also, please subscribe. We're on Apple Podcasts, Stitcher, Spotify and other platforms. Thanks, everybody. Until next time.

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Announcer #2 (22:27):

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