

TRADE SECRET LAW EVOLUTION PODCAST, EPISODE 43

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Jordan Grotzinger: 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 [00:00:30] your company's most valuable assets. I'm your host, Jordan Grotzinger.

Hi, everybody. Happy New Year. Welcome to a new season and episode of the Trade Secret Law Evolution Podcast. This is episode 43. Hope everyone had a nice holiday break. We're going to discuss two cases today. One is about the proper venue for criminal prosecution [00:01:00] of trade secret theft, and the other concerns calculating damages for trade secret misappropriation.

The first case, both are out of the Eleventh Circuit, came down on January 12th. We don't normally talk about criminal cases in this podcast, but the facts of this one were interesting enough that it caught my attention and thought it was worth discussing. The issue in the case was whether an accused can be tried [00:01:30] in a venue where he didn't commit any of the elements of the crime. In that case, the defendant was a software engineer and fisherman who obtained the coordinates of artificial fishing reefs in the Gulf of Mexico from a website owned by a business that sells those coordinates. The defendant remained in Mobile, Alabama, during the relevant events, but he was tried in the Northern District of Florida, where the website's, I'll [00:02:00] call it the website, office is located. The jury convicted the defendant of theft of trade secrets, and the district court enhanced the sentence.

The website sells the coordinates of these artificial reefs that are placed in various locations in the Gulf of Mexico by fishermen, and the coordinates of those reefs are usually not shared to prevent overfishing. The website has its office in Pensacola, Florida, but the [00:02:30] servers where the website and data are hosted are in Orlando. The website obtains the coordinates in two ways. First, it harvests data from public records, but it doesn't sell those coordinates. It shares them for free. Second, it finds the coordinates for private reefs by launching boats equipped with sonar equipment from its base in Pensacola to trawl the Gulf of Mexico. After processing the raw [00:03:00] data, the website offers the private reef coordinates for a price.

The defendant is a software engineer who lives in Mobile and fishes most of the year. When he visited the website, he used a web application that allowed him to see the coordinates of private artificial reefs, and he later accessed the coordinate data, again, after additional security measures had been installed to

prevent what he was doing. [00:03:30] Through a mutual acquaintance, the defendant contacted the website's owners and told them he was able to access the coordinates, and he also posted on Facebook that he had the coordinates. The website owners then upgraded its security again, but the defendant was still able to access the coordinates.

The defendant and the owners of the website negotiated about the defendant possibly helping them with the security issues in exchange [00:04:00] for better coordinates for grouper, which is a type of large fish, but they never made a deal, and the owners contacted law enforcement. Officers executed a search warrant for the defendant's home and saw he had accessed the website over 4,500 times and accessed Facebook records establishing that he had sent pictures of the coordinates to his friends on Facebook Messenger, and then the agents seized the defendant's electronic equipment.

The defendant waived his Miranda [00:04:30] Rights, the right to remain silent, et cetera, and admitted to the agent that he disagreed with the website's business, accessed the website after its security was upgraded, and wrote the Facebook posts and "infiltrated" the website. He was indicted by a federal grand jury on three counts in the Northern District of Florida, one, for violation of the computer fraud and abuse act, two, theft of trade secrets, and three, [00:05:00] transmitting a threat through interstate commerce with the intent of extorting a thing of value. We're going to focus on the trade secret count.

The defendant moved to dismiss all counts, including the trade secret count, for improper venue, arguing that he was a resident of Mobile and resided there during all of the events relevant to his indictment. Although the website was headquartered in Pensacola, which is in the Northern District of Florida, [00:05:30] its servers where the coordinate data was stored were in Orlando, which is in the Middle District of Florida. Therefore, he argued, venue was improper in the Northern District of Florida, because all of the prohibited conduct occurred in the Southern District of Alabama, and the data that was accessed was in the Middle District of Florida. But the district court denied the motion, so the defendant was found guilty of trade secret theft, and his sentence was enhanced. [00:06:00] The defendant appealed.

The Eleventh Circuit noted that the Sixth Amendment of the Constitution guarantees defendants the right to be tried in the district in which the crime was committed. "Venue is proper at the locus delicti, which is determined by the nature of the crime alleged and the location of the act or acts constituting it," and "in performing this inquiry, a court must initially identify the [00:06:30] conduct constituting the offense, the nature of the crime, and then discern the location of the commission of the criminal acts." Based on the case of U.S. versus Rodriguez-Moreno, "We perform a two-step venue inquiry. First, we identify the essential conduct elements of the theft of trade secrets count. Then, we discern the location of the commission of the essential conduct [00:07:00] elements, which are the only relevant elements for venue, and

determine whether the location of their commission is the same as the location of the trial."

Here, the court held, they are not. Criminal theft of trade secrets requires five elements. One, the defendant must intend to convert, that is steal, proprietary information to the economic benefit of anyone other than the owner. Two, the [00:07:30] proprietary information must be a trade secret. Three, the defendant must knowingly steal, take without authorization, or obtain by fraud or deception, trade secret information. Four, the defendant must intend or know that the offense would injure the owner of the trade secret. And five, the trade secret must be related to a product that is in interstate or foreign commerce. For purposes of venue, " [00:08:00] The essential conduct element of the crime is that the defendant must steal, take without authorization, or obtain by fraud or deception, trade secret information, so that conduct must have taken place in the same location as the trial."

The defendant was prosecuted for theft of trade secrets in the Northern District of Florida, but he remained in Mobile, which, as I said, is in the Southern District of Alabama, [00:08:30] during the commission of the crime. Also, the data was taken from servers located in the Middle District of Florida. So, the court held, while "venue would be proper in the Southern District of Alabama, where defendant was located when he took the trade secrets, venue was not proper in the Northern District of Florida, because the defendant never committed any essential conduct in that location." In so holding, the court rejected [00:09:00] the government's argument that the effects of a crime are a permissible basis for venue.

The court found that the cases supporting that argument are distinguishable, having involved subjects like failure to pay child support and obstruction of justice. But the court said, "Both of those offenses contained an essential element of the crime that we understood to be defined in terms of the effects of the act. That is, the location of the effects of the crime [00:09:30] is proper venue, because the very nature of the crime is affecting or endeavoring to affect the due administration of justice. The activities prohibited under the statute are those intended to influence the administration of justice, where the affected judicial proceeding is being held or has been held."

The theft of trade secret statute, on the other hand, "does not define any essential conduct element of the offense in terms of its effect [00:10:00] on the owner of the trade secret." That is, "a plain reading of the statute reveals that there is no requirement that the owner of the trade secret realize a loss." Thus, venue is improper in the Northern District of Florida. Interestingly, "The remedy for improper venue is vacatur of the conviction." That means to vacate the conviction. "Not acquittal or dismissal with prejudice. And the [00:10:30] Double Jeopardy Clause is not implicated by a retrial in a proper venue after we vacate a conviction for improper venue."

The next case, also out of the Eleventh Circuit, gets into the weeds a bit, but you don't see the issue addressed a lot, and it's important. That is, what kinds of costs must be deducted for calculating an award of lost profit damages [00:11:00] in trade secret cases? In this case, the parties competed in the business of selling software to process invoice for alcohol sales. After the defendant entered the market and the plaintiff lost a lot of business, the defendant was found liable by a jury for trade secret misappropriation, and the jury awarded compensatory and punitive damages. The defendant challenged the damage award on the ground that the jury didn't deduct its fixed [00:11:30] and marginal costs from revenue in calculating damages.

The Eleventh Circuit first looked to the Florida Uniform Trade Secrets Act damages statute, which provides, "Damages can include both the actual loss caused by misappropriation and the unjust enrichment caused by misappropriation that is not taken into account in computing actual loss." The issue here is what [00:12:00] constitutes actual loss. The defendant contends that the plaintiff can recover only lost profits. That is, the revenue it would've received from its lost customers less the costs it would've incurred servicing those customers. The plaintiff further contends that Florida law requires that the defendant subtract both fixed and marginal costs from its revenue to calculate lost profits.

[00:12:30] The court explained what fixed and marginal costs are. "Fixed costs don't, at least directly, vary based on output volume, while marginal costs measure the change in cost associated with a change in output." Thus, fixed costs "are those that remain essentially the same regardless of the number of a company's customers or products. These may include rent, utilities, salaries, depreciation, [00:13:00] insurance, property taxes, R&D, et cetera. Marginal costs, on the other hand, are tied directly to output volume. They are often defined as the costs associated with producing one more unit of output or servicing one more customer, and they are calculated by dividing the change in total cost by the change in output. When calculating marginal costs over a change in output volume during which [00:13:30] fixed costs remain constant, marginal costs will depend on only on the change in variable costs."

First turning to fixed cost, the court held that they do not need to be deducted from revenues to calculate lost profits. "We start with the text of the Florida Uniform Trade Secrets Act damages provision," which, again, permits damages for "the actual loss caused by misappropriation." [00:14:00] The evidence doesn't clearly show that the plaintiff incurred any reduction in its total fixed costs. Accordingly, no fixed cost savings offset its misappropriation-based losses. Given that, the court said, it's not clear to us why the plaintiff should have to deduct fixed cost that it would have incurred anyway, and that therefore, weren't at all related to [00:14:30] the defendant's conduct or the plaintiff's response.

Additionally, the court held, "The Florida Uniform Trade Secrets Act permits recovery only of those losses that are caused by misappropriation. Here, there is no clear causal link, because the plaintiff's fixed cost remained unaffected by the defendant's misappropriation. If we were to require the plaintiff to deduct [00:15:00] fixed costs from lost revenues anyway, we would underestimate the magnitude of plaintiff's loss caused by the defendant's misappropriation. That outcome seems contrary, not only to common sense, but also, and more importantly, to the Florida Uniform Trade Secret Act plain text."

Now, as to marginal costs, "Missing from the trial record is any evidence that [00:15:30] the plaintiff's marginal costs were actually zero. Had the plaintiff clearly presented that evidence, it might have been entitled to an award that didn't account for those costs, but plaintiff presented only evidence that its marginal costs were minimal, and minimal doesn't equal zero." Thus, "Because the plaintiff didn't provide any evidence from which a reasonable jury could conclude that its marginal costs were zero, the district court [00:16:00] erred in denying the defendant's judgment as a matter of law motion on damages."

In sum, "Although the Florida Uniform Trade Secrets Act damages provision doesn't require fixed cost deduction, plaintiff was required to deduct its marginal costs. Because it didn't conclusively prove that its marginal costs were zero, it wasn't entitled to its full amount of lost revenues. So, on [00:16:30] remand, the district court should requirement and accounting of marginal costs to enable a proper lost profits calculation."

And now, for the first takeaways of 2022. One, venue for a criminal prosecution of trade secret theft is where the essential conduct took place, not where the effects of the theft were felt. Two, under the Florida Uniform Trade Secrets Act, [00:17:00] and therefore likely in many other venues, or I should say states because all but two adopt the Uniform Trade Secrets Act, fixed costs, that is costs that don't vary based on output volume, need not be deducted from revenues for lost profit calculation, because these costs or losses aren't caused by the misappropriation. On the other hand, takeaway three is that marginal costs, [00:17:30] which measure the change in cost associated with a change in output, and therefore are causally connected to misappropriation, should be deducted. All right, everybody. Until next month, thanks for listening.

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, so we value your feedback. Let us know how we can be more helpful to you. Send [00:18:00] us your questions and comments. You can reach me by email at [grotzingerj@gtlaw.com](mailto:grotzingerj@gtlaw.com) or on LinkedIn. And 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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