Trade Secret Law Evolution Podcast

Episode 55

Greenberg Traurig, LLP

Speaker 1 (00:00):

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Jordan Grotzinger (00:18):

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.

(00:39):

Welcome to episode 55 of the Trade Secret Law Evolution Podcast. Today we're going to be talking about one case that deals with a very common issue. We've addressed trade secret identification but also avoided cost damages, which we've also addressed. But the interesting thing about this case is that the ruling was opposite of the other avoided cost cases that we've discussed and I recall. So the case we're talking about is out of the Second Circuit in New York from last month, and here's a summary. The defendant developed software used by healthcare insurance companies, including a certain software platform that automates and manages healthcare administrative tasks like claim processing and billing. And we're going to call that platform Platform with a capital P, very creative.

(01:39):

The defendant licenses the software to over a hundred million people, but installing, upgrading, and customizing the Platform to fit a client's particular needs requires significant time and skilled personnel. So the defendant also provides customization and implementation consulting services to clients, and in that task, it sometimes utilizes subcontractors including the plaintiff. The parties entered into a master services agreement MSA, whereby the plaintiff agreed to support the Platform customers in exchange for an annual payment, and the defendant gave the plaintiff's employees access to its trade secrets to perform Platform-related services for the defendant.

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Now, you know that I don't name company or party names in this podcast. You can always look up the case. But as I'm saying plaintiff and defendant, one thing that's interesting here is, as you'll see, it was actually the defendant who in effect wound up being the plaintiff here and getting the recovery as a cross complainant. But I'm just going to keep the word, defendant. So parties had this MSA, later a competitor of the plaintiff bought the defendant company and as a result, the plaintiff terminated the MSA and requested payment of rebates owed under the contract, but the defendant refused to pay and also raised concerns about the plaintiff continuing to use its trade secrets post-termination.

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So the parties sued each other for violation of the Defend Trade Secrets Act, the DTSA, and related claims. That of course is the federal trade secret law. Discovery revealed that "The plaintiff was actively creating a repository of the defendant's trade secrets on its own or of its own to be used in future work." The defendant presented expert testimony indicating that the plaintiff avoided expending roughly $285 million in research and development costs through its misappropriation. The defendant spent almost twice that to make the Platform. The defendant's damages expert testified at trial that the $285 million figure represented, "a portion of the overall research and development costs, specifically those costs for the period between 2004 to 2014 excluding client-funded research and development." The expert also testified that the defendant lost $8.5 million in profits.

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Case went to the jury, jury found for the defendant and awarded just about $285 million in compensatory damages and doubled that amount about 570 million in punitive damages. And importantly, the court issued a permanent injunction preventing the plaintiff from using the defendant's trade secrets, that will come into play later. The plaintiff appealed on the ground that the defendant hadn't identified its trade secrets specifically enough and that the court erred in allowing avoided costs as unjust enrichment damages. So the two issues, first one was trade secret identification. As to trade secret identification, the Second Circuit said, "Under both the DTSA and New York law, a claimant bears the burden of identifying a purported trade secret with sufficient specificity. The specificity requirement places a defendant on notice of the basis for the claim being made against it and allows a fact finder to determine whether certain information is, in fact, a trade secret."

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Here, the court held the defendant provided extensive testimony including expert testimony identifying the trade secrets. For each trade secret, the defendant explained, "one, what the trade secret was, two, how the secret was developed, three, the value of the secret to the defendant, and four, that the secret was maintained as confidential." And the jury was provided with an exhibit identifying each asserted trade secret by name. This the court held was enough for sufficient trade secret identification. The second issue was the propriety of avoided costs as unjust enrichment damages. And the court said, "The DTSA's broad compensatory damages provision allows a court to award, one, damages for actual loss caused by misappropriation, and two, damages for any unjust enrichment caused by the misappropriation ... that is not addressed in computing damages for actual loss, or three, in lieu of damages measured by any other methods ... a reasonable royalty for the misappropriator's unauthorized disclosure or use of the trade secret. The statute thus permits a plaintiff to recover both its actual losses and a misappropriator's unjust benefit caused by misappropriation, so long as there is no double counting."

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Now, the parties conceded that avoided costs are recoverable as damages for unjust enrichment under the DTSA but dispute whether they were available under the facts of this case. And the court said to answer that question, "One needs to consider the entirety of the DTSA's remedial scheme, not each provision in isolation. The DTSA awards compensatory damages to aggrieved trade secret holders whose injuries are not adequately addressed by lost profits. It provides a tool to make trade secret holders hold by further awarding damages for any unjust enrichment caused by the misappropriation ... not addressed in computing damages for their actual loss, i.e., in instances where the value of the secret is damaged or worse yet is destroyed." But the court said, "The amount of avoided cost damages recoverable must still derive from a comparative appraisal of all of the factors of the case among which are the nature and extent of the appropriation and the relative adequacy to the plaintiff of other

remedies. Awarding avoided costs in the absence of such a comparative appraisal risks producing an unjust windfall for trade secret holders."

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Accordingly, the Second Circuit said, "For purposes of deciding whether unjust enrichment in the form of avoided costs was permissibly awarded in this case, the relevant question is: did the plaintiff's misappropriation injured the defendant beyond its actual loss of $8.5 million in lost profits?" The court noted, "Reading the statute's compensatory damages provision otherwise, as focusing exclusively on the plaintiff's saved expenses to award avoided costs, ignores the extent to which plaintiff's misappropriation injured the defendant and impermissibly discounts the comparative appraisal that governs equitable trade secret remedial determinations."

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The court explained, "Under that reading, avoided costs would be available as unjust enrichment damages in any case of misappropriation, even where a trade secret owner suffers no compensable harm beyond its lost profits or profit opportunities. If accepted, that view would permit avoided costs awards that are more punitive than compensatory." Here the court said, "There is no dispute that the plaintiff unjustly benefited from misappropriating the defendant's trade secrets to a customer i.e., earning $27 million in revenue, corresponding to $823,899 in profits. But critically, those profits were the only enrichment the plaintiff unjustly gained at the defendant's expense and they were addressed in computing damages for the defendant's actual loss. The defendant's expert testified that the actual loss the defendant suffered post DTSA from the plaintiff using its trade secrets to service the customer was 8.5 million in lost profits. Thus, through its misappropriation, the plaintiff realized $823,899 in unjust profits at the expense of the defendant's $8.5 million profit opportunity."

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But the court said the defendant "suffered no compensable harm, supporting an unjust enrichment award of avoided cost. The district court's permanent injunction ended the plaintiff's use of the defendant's trade secrets and therefore its ability to profit from any avoided costs. Further, the plaintiff's misappropriation did not diminish much less destroy the secrets' continued commercial value to the defendant. In fact, the defendant has retained the profitable use of its trade secrets. The Platform is worth even more today than it was when the misappropriation occurred. Accordingly, the defendant is not entitled to avoided costs as a form of unjust enrichment damages in this specific case."

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And the court reasoned, "To be sure, future cases may present a range of factual scenarios concerning a defendant who has realized only modest profits from its misappropriation of trade secrets but has, nevertheless, been enriched by avoided costs in a larger amount at the expense of the secret holder. This might depend on, for example, the extent to which the defendant has used the secret in developing its own competing product, the extent to which the defendant's misappropriation has destroyed the secret's value for its original owner, or the extent to which the defendant can be stopped from profiting further from its misappropriation into the future. But in this case, perhaps unusually none of those circumstances supports awarding the defendant $285 million of the cost it spent in developing the misappropriated secrets. The defendant's valuable trade secrets are still that valuable and secret."

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And, "Most of the cases the defendant and the district court employed to support awarding avoided costs concerned claimants who at least to some degree lost the value of their misappropriated trade secrets. Avoided costs compensated for that loss." Thus, the court concluded, "as a matter of law, an unjust enrichment award of avoided costs was unavailable because the plaintiff's unjust gain was fully

addressed in computing damages for the defendant's actual loss." And the defendant suffered no compensable harm beyond that actual loss.

(14:07):

So what are the takeaways? On trade secret identification to sufficiently identify a trade secret at trial. Proffer evidence on one, what the secret was, two, how the secret was developed, three, the value of the secret to the owner, and four, that the secret was maintained as confidential. And as you know if you follow this podcast that essentially tracks the definition of a trade secret. Following this map, of course, also can help with sufficiently pleading a trade secret as opposed to proving it at trial. And secondly, as to avoided cost damages, in the Second Circuit, avoided cost damages are not available under the DTSA where the "unjust gain was fully addressed in computing damages for the defendant's actual loss." Rather, there would have to be some loss of value of the owner's trade secret. That is a well-reasoned opinion and it'll be interesting to see what other circuits and state courts say about that issue.

(15:13):

So unfortunately today we have no co-host. I figured this was one case and we just bang this out, but one of my favorite parts of the podcast is the interesting fact or fun fact thing. So I'll give you one right now. I think some episodes ago I talked about how another passion of mine besides trade secret law is handling pro bono innocence cases for wrongfully convicted people. And I actually, I work on one of those cases with our great producer, Katharine Heller's sister Caroline, who runs our global pro bono program. So the fun fact is this because I'd already said that. Last week I appeared on a show called The Breakfast Club with Charlamagne tha God and DJ Envy and my friend and colleague Jason Flom about a pretty prominent wrongful conviction case. It's very interesting. You can find it on The Breakfast Club's YouTube channel. Check it out. Thanks, everybody. Talk to you next month.

(16:21):

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 us your questions and comments. You can reach me by email at 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.

Speaker 3 (16:51):