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Opinion

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Protecting the crown jewels: How to deal with international trade secrets theft

Corporations are implementing broad-based litigation strategies to combat technology theft by foreign competitors.

By Kent Gardiner, William Sauers

In this three-part series, we present a hypothetical case study on fictitious U.S. company "SFilm," drawn from a range of actual litigation experiences, that lays out the varied elements of an international trade secret strategy, and identifies the most common pitfalls that arise.

"We've now concluded our patents in Asia are worthless."

This is the sentiment from many general counsel of top corporations who find themselves the target of competitors, particularly non-U.S. companies, whose core business strategy involves stealing technology to "leapfrog" substantial investments that U.S. companies have made for years, if not decades. Their technology ambitions are consistent with those of their governments. As China treks through the second year of its five-year plan to transition from "Made in China" to "Designed in China," a report from the U.S. Chamber of Commerce called the roadmap for China's efforts an intricate web of new rules "considered by many international technology companies to be a blueprint for technology theft on a scale the world has never seen before."

According to the report, China seeks to "enhance original innovation through co-innovation and re-innovation based on the assimilation of imported technologies." The government has stated it will target seven key industries for this technology advance:

1. Clean energy technology
2. Next-generation IT
3. Biotechnology
4. High-end equipment manufacturing
5. Alternative energy
6. New materials
7. Clean energy vehicles

To achieve this goal, the Chinese government and private sector will invest nearly $2 trillion by the end of 2015.

This technology march, by China and other emerging countries, has been accompanied by a rise in trade secret theft litigation, particularly in these core industries. In response to this growing threat of technology theft, many corporations, including those holding the lion's share of America's technological brain trust, have begun to invest more of their technology protection resources in trade secrets. These companies have come to realize that outside the U.S. legal protections for patent portfolios, designed to prevent competitors from practicing inventions that have been disclosed to them by the patents, are unreliable. Trade secrets, in contrast, are by definition not disclosed to competitors, thus potentially giving the innovator competitive advantages over the long term. Unfortunately, most companies have highly developed patent protection systems and resources, while their trade secrets infra-

structure is significantly less so. It is becoming clear that the trade secrets portfolios of major companies are underappreciated, underdeveloped and underprotected. And, they're leaking.

If your business leaders have pitched your board of directors on the justification for multimillion dollar projects on the assumption that "no one else has this," only to discover afterward it isn't true, you are not alone. U.S. corporations have made massive capital investments in research, technology and plants around the world on the assumption that their technology gives them a competitive advantage, only to learn later that competitors have neutralized that competitive advantage through theft of key technologies.

Then comes the fight. What starts as a simple flash drive gone AWOL, or a former employee making curiously effective sales calls, might appear to be a simple, discrete and containable problem. But more frequently, the problem turns out to be much bigger. Much more systematic theft has occurred, not only through the vehicle of defecting employees but also through computer system hacking, theft from equipment suppliers or joint venture partners and surreptitious surveillance of plant sites. And worse yet, the thief increasingly is a foreign company with little incentive to either play by the rules of U.S. litigation or to respect U.S. court judgments for damages and injunctive relief. Accordingly, handling trade secret theft as if it were any other typical lawsuit, in which one files, litigates and waits for a verdict, is not nearly sufficient to tackle the complex maze of concerns that arise in these international cases.

The battle that companies must fight is instead a multi-pronged, cross-disciplinary, simultaneously-executed strategy. It requires the right muscle from the very beginning to force the thieves to participate in a system of justice and recovery that they have no incentive to recognize. In the end, it must leave the thieves with no alternative but to pay the appropriate damages and return the stolen technology.

Case study: SFilm

SFilm has invested $750 million in developing a new method to make solar film that creates a multitude of new applications and vastly increases the potential market for solar products. Based on this breakthrough, SFilm built a new manufacturing plant. While the product has proven to be extremely profitable in the year since the factory opened, it will be years before SFilm recoups its R&D and plant manufacturing costs. One year after the plant became operational, a Chinese company began selling solar film at a substantially reduced cost. Testing showed that the product has similar qualities to SFilm's. While the Chinese company had manufactured traditional solar panels in the past, it has never been known as an innovative company and has never filed for any patents on its products.

Moreover, customers are reporting that they have received sales calls from a number of former employees of the company regarding this competitor, who are making claims about the technical similarities of the respective products. An internal investigation uncovers that at least one of the former employees appears to have copied internal documents on a USB drive just prior to leaving the company.

SFilm's natural instinct is to assume (or at least hope) that the theft is limited to a single rogue employee, and thus can be dealt with quickly and discretely. But the company decides, wisely as it turns out, to build a strategy on the assumption that much more widespread theft of its technology has occurred, with much more active involvement by its Chinese competitor. SFilm realizes that an effective strategy, resulting in meaningful recovery of damages for the investments it has made in developing its trade secrets and effective return of the technology, hinges on its ability to craft and execute a broad-based litigation strategy involving both civil and criminal dimensions, as well as a parallel diplomatic/political strategy aimed at bringing appropriate pressure to bear and serving notice on its competitors and their governments that it is prepared to stand and fight to protect its technology.

Bring the fight

SFilm must first evaluate how and where to bring the fight. Given that the thief was a foreign company in a country with limited respect for U.S. judgments, SFilm must plan for a comprehensive litigation

approach, including federal district court litigation, government involvement and foreign action.

Trade secret misappropriation is a state law question, and as a result, such cases are often brought in state courts. However, because SFilm's defendant is located in another country, instituting federal litigation is likely preferable, as federal courts have more resources and experience to handle international issues, such as the Hague Convention and multi-country enforcement. It also may be easier for SFilm to enforce the decisions and verdict from a U.S. district court depending on the applicable international treaties and principles of comity.

If SFilm is unable to establish jurisdiction in district court, or if there are serious concerns regarding enforcement, whether stemming from a default judgment or the defendant's home country's disinclination to respect the judgment of a U.S. court, an action at the U.S. International Trade Commission (ITC) may be preferable. Among the relevant and key differences that the ITC affords is the ability to bring an action against the offending goods that are imported into the U.S. As a result SFilm need not establish personal jurisdiction over the defendant.

In addition, a successful ITC action will result in an exclusion order that prevents products manufactured with the stolen trade secrets from entering the U.S. SFilm also would benefit from the relative speed of ITC actions, as they generally take no more than 18 months. Of course, there are a number of unique considerations related to ITC actions, including the need to establish a domestic industry, an independent government attorney who is a party to the action and the possibility of presidential override.

Concerned not only about ongoing competition from the thief, but also about further dissemination of its trade secrets, SFilm seeks injunctive relief to force the return of its trade secrets and cessation of their use by the defendant. It determines its best chance of obtaining those goals is a U.S. district court action, due to the available remedies and a strong chance of establishing personal jurisdiction over the defendant. Litigation on the merits and implementation of a parallel political strategy are soon to follow, and these are the subjects of the next two installments of this series.

5 ways to fight back against international trade secret theft

How a company can win big at trial, while preserving its reputation abroad.

By Kent Gardiner, William Sauers

In part one of this series, we outlined the plight of a hypothetical U.S. company, SFilm, which designed an innovative flexible solar film and invested $750 million in a new plant to capitalize on its breakthrough technology. A Chinese company stole critical trade secrets covering the new technology, and entered the market with a competing product, thereby placing SFilm's entire business in jeopardy. SFilm began to

fight back by commencing federal court trade secrets litigation in a district with jurisdiction over the foreign defendant.

In this second installment of SFilm's story, we explore the various defenses the Chinese defendant throws up, both in the U.S. and its home country, to elude responsibility for its theft, and how SFilm fights back.

Fight the fight

The Chinese defendant comes back swinging. It shows up to defend itself in the federal court case out of fear that failure to do so will result in contempt orders impairing its broader interests in the U.S. But once it appears, it engages in wholesale obstruction of SFilm's efforts to prove its case.

It produces electronic discovery that reeks of tampering. It claims it no longer has control over key witnesses—its own employees who paid SFilm employees for trade secrets and had since mysteriously left the company or been turned over to separate counsel. And it brings antitrust counterclaims against SFilm, claiming that the U.S. company was trying to monopolize the market.

The defendant also opens up a new front in its war against SFilm in China. It appeals to the relevant government agencies to open investigations of SFilm, both for unfair competition and for theft of the Chinese company's trade secrets. It also launches an intensive public relations campaign against SFilm in the local press.

These counter-attacks are not a surprise. SFilm knew the Chinese defendant would aim to distract attention from the primary case at hand and try to create off-setting leverage. SFilm was ready with a comprehensive litigation and diplomatic strategy to take the battle to the Chinese defendant on all fronts. Here is how SFilm fights the fight:

1. Prove spoliation.

SFilm is suspicious of the dearth of electronic evidence from the files of the key defendant witnesses. SFilm takes aggressive discovery, including analysis of metadata, and uses forensic expertise to analyze records retention and gaps. SFilm proves intentional destruction of massive amounts of relevant evidence. After multiple motions and an evidentiary hearing, SFilm persuades the court to issue findings of spoliation and order an adverse inference at trial regarding defendant's destruction of material evidence.

2. Inspect the plant.

SFilm uses the defendant's obstructionist approach to discovery to its own advantage, persuading the court to order a physical inspection of the defendant's plant in China. SFilm conducts the inspection with the jury trial in mind, knowing that the inspection findings not only will help it uncover facts but also help it tell a broader story that the jury will want to hear.

SFilm sends its counsel over for the inspection, but it also sends its technology experts and a videographer to the plant. The team is able to return to the States with new ammunition for SFilm's case. They can now graphically display the scope of theft: The defendant had built an almost identical plant, right down to the workarounds in SFilm's own plant. The Chinese company indisputably stole the blueprints to SFilm's facility, as the video dramatically captures. For SFilm's counsel, closing arguments nearly write themselves.

3. Help the U.S. government help you.

Early on, the Federal Bureau of Investigation (FBI) and Department Of Justice launched investigations into the employees who had absconded with SFilm's technology and sold it to the defendant. These agencies continue to gather evidence from SFilm regarding its trade secrets, which helps the DOJ to return indictments against the defendant and key employees for criminal theft of trade secrets.

In addition, several witnesses under criminal investigation refused to testify in SFilm's civil litigation, repeatedly invoking their Fifth Amendment privilege. As a result, the court ordered the issuance of adverse instructions to the jury regarding the witnesses' refusal to testify. The adverse instructions serve as another opportunity for the jury to understand the depth and scope of the theft.

4. Watch your back in the defendant's home country.

Given its size, the Chinese market is critical to SFilm's future. The expectation, indeed the certainty, that the defendant will slander SFilm in China thus carries serious risks. SFilm knows it must protect its long-term business interests no matter what happens with the U.S. litigation. What to do?

Recognizing that the protection of American technology is the most important goal of U.S. trade policy, it seeks help from the powerful U.S. government agencies responsible for this effort, including the Office of the U.S.Trade Representative, the State Department and the White House Office of the IP Czar. They will ensure that the Chinese government is also aware that in stealing SFilm's technology, the defendant is putting the critically important U.S.-China political relationship at risk.

Second, SFilm engages sophisticated counsel in China, who are experienced in both regulatory and political processes, to represent SFilm's interests in China. As a result, SFilm is ready to respond to the Chinese government with information about the defendant's theft, to counter the negative press propagated by the defendant and to disprove the defendant's charges against SFilm. As a result, SFilm is able to obtain a stay of any Chinese regulatory actions pending the outcome of the U.S. litigation.

5. Win big at trial.

The only acceptable settlement for SFilm requires substantial compensation for its technology development and a full return of its trade secrets. Since the defendant won't even acknowledge its theft, much less pay for it, SFilm deploys an aggressive strategy to take the case to trial. It presents its liability evidence and an investment-driven damages theory that seeks to recover damages from the defendant for avoiding the millions of R&D dollars that SFilm expended in developing its innovations. Its case is aided by the very tactics the defendant used to evade detection and responsibility, including adverse inferences from spoliation and Fifth Amendment invocations, an effort to impede access to certain witnesses during discovery and the devastating impact of the plant inspection videotapes.

The jury returns a verdict fully in favor of SFilm, finding willful theft of trade secrets, and substantial damages. The jury rejects the antitrust counterclaims entirely in the face of vivid evidence of rampant theft. The court enters a comprehensive injunction against further use of SFilm's trade secrets and a multi-year worldwide production ban on sales of defendant's competing products. In the wake of this comprehensive victory, the Chinese government closes its investigations of SFilm, and opens an investigation into the defendant. SFilm is able to declare a major victory.

But did SFilm really win? Immediately after the jury's damages verdict and the court's imposition of a broad production injunction, SFilm must prepare itself for defendant's response and its international implications. We will explore the company's next steps to fully secure its victory in the third and final installment of this series.

Winning the final fight against international trade secret thieves

Five steps to overcome a defendant's aggressive post-verdict actions and obtain compensation.

By Kent Gardiner, William Sauers

In the third and final installment of this trade secret litigation series (be sure to check out part one and part two), we visit hypothetical U.S. company SFilm as it pursues its hard-fought relief against a Chinese competitor that had stolen its most valuable trade secrets. After winning a federal jury trial, pursuing multiple nonlitigation efforts and cooperating in the U.S. government's investigation of the defendant's actions, SFilm may finally obtain financial compensation and return of its technology. But the fight is far from over. SFilm faces yet further obstacles from the defendant, running the gamut from corporate reorganizations designed to shield assets to protracted enforcement litigation designed to run up costs.

Facing a large jury verdict and a federal government investigation normally would cause a defendant to surrender. But the Chinese company has every incentive to delay and impede enforcement of SFilm's judgment. For SFilm's competitor, there is no "plan B" because there never was any business model other than to steal trade secrets.

Unlike in typical litigation, where resolutions can be encouraged by appealing to long-term or mutually advantageous business goals, the Chinese company is convinced there is nothing to be gained by backing down. It responds to the U.S. judgment with press statements that the jury was misled, and that it will prevail on appeal. But behind the scenes, it engages in subtle maneuvers designed to thwart any possible recovery.

What does it do? First, it manipulates its vast corporate structure. It then uses that new array of subsidiaries and affiliates to declare large, unprecedented dividends to the "shareholders." It also forms a series of spinoff corporations to move assets out of its own corporate name.

It then refuses to post a bond to secure the judgment for the appeal. Recognizing that the lack of a bond will allow SFilm to start collection efforts, the Chinese defendant manipulates its customers and the supply chain. It moves the point of sale from the U.S. to China and engages resellers to move the goods to the existing U.S. customers. This effort is designed to thwart customs actions against incoming goods.

The Chinese company also enters into prepayment schemes with its customers, where, for a discount off the price, the customers send the money to China in advance payment for ordered goods. This impedes garnishment actions against the U.S. customers. And it starts to move money out of U.S. banks and into local and regional Chinese financial institutions.

The Chinese company's actions are not limited to the courtroom or the corporate boardroom. The company engages a public relations firm and places articles in friendly forums, all railing against the "unfairness" of U.S. the legal system, questioning the intelligence of the individual jurors and pointing out how the defendant's story was not heard in the U.S. The articles play up the notion of American imperialism and a biased court system to try to sway public opinion away from the real issue—the technology theft.

The Chinese company's attempt to portray itself as the victim of a bullying and biased U.S. legal system has a specific agenda—to try to build a political case in

China that will ensure that any enforcement attempts by SFilm in China are thwarted based on "public policy" considerations.

How can SFilm respond to the multifaceted legal, corporate and media attacks? Here are several actions SFilm takes to respond to these aggressive post-verdict actions.

1. Issue post-verdict discovery. The post-judgment litigation rules allow for broad post-judgment discovery into the Chinese company's ability to pay the damage award. This is done as soon as possible after the verdict, even though SFilm does not have a complete picture as to the other side's financial structure. Immediate discovery requires the placement of a document hold on the adverse party and allowing SFilm to generate a comprehensive picture of its competitor's assets over time, including just before the verdict.

2. Start collection efforts against the adverse party's customers. Too often, plaintiffs hesitate to start immediate collection efforts, knowing the issue will not be fully resolved until the appeal is decided. When a bond is not posted, however, collection can begin immediately. In addition to obtaining monetary results (such as collecting accounts receivable due to the adverse party), SFilm undertakes a vigorous collection enforcement plan to provide more discovery into efforts undertaken to avoid judgment, and counteract aggressive moves to institute prepayment or reseller schemes. SFilm's collection efforts put enormous pressure on the Chinese company because customers begin to question whether the defendant will be able to meet their supply needs in the future.

3. Begin trying to freeze assets in banks and other financial institutions. It is possible to begin actions against foreign banks with offices located in the U.S. that may hold the defendant's money. Moreover, in certain circumstances, the actual location of that money (i.e., whether it is physically kept in the U.S. branch or a foreign main office) is irrelevant. Asset recovery laws give SFilm wide latitude to attempt to collect assets with a U.S. presence, which in some cases allow money from overseas to be collected.

4. Pursue "turnover" proceedings. Most plaintiffs believe enforcement against an international company requires "domestication" of that judgment in the foreign country. True, but most states also have laws that allow a U.S. court to order a defendant to disgorge assets to the plaintiff to satisfy a judgment. In these cases, the actual location of the defendant is irrelevant; by virtue of personal jurisdiction over the defendant, the court has the authority to transfer the assets. If the company refuses, it faces possible contempt proceedings and even more onerous remedies.

5. Pursue a PR strategy. The multifaceted public relations strategy involving the media and government actors discussed in prior installments of this article does not end when the jury returns a verdict. SFilm knows that foreign companies are more and more willing to aggressively protest a perceived "unfairness" of the American judicial system when they lose. These protestations must be answered, both to ensure that SFilm's positions are accurately portrayed, and to keep political and business pressure on the defendant until the award is paid.

These are just some of the strategies SFilm employs to counteract the attempts at enforcement evasion by an unrepentant defendant. SFilm knew the case would not end after the verdict, and it rightly planned and budgeted for this work *before* the verdict.

SFilm wins its fight. The Chinese defendant faces actual enforcement of the award through attachment of its assets; a customer base that begins to erode through lack of confidence that the Chinese company will stand behind its business commitments if it is so willing to flout the law; and increasing hostility from its own government as it attempts to maintain good political relations with the U.S. and to convince the world it will protect IP rights. The Chinese company finally agrees to an appropriate monetary settlement and to return SFilm's stolen secrets. SFilm's technology-driven competitive advantages in the marketplace are restored; its capital investments protected; and its stock price moves sharply upward. The fight has been well worth it.

Unfortunately, the hypothetical story of SFilm is not

an exception to the rule. Its battle to protect its trade secrets and fight on an international stage to recover its technology and appropriate damages was critical to its survival. Fortunately, SFilm crafted a broad-based litigation, business and political strategy both at home and abroad, all facets of which contributed to securing its victory. SFilm appreciated not only the challenges of international legal enforcement of IP rights, but also the opportunities inherent in international government peer pressure associated with protecting technology. SFilm's legal innovation matched its product innovation.

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