

Determining Injury From Trade Secret Misappropriation At ITC

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Most companies rely extensively on trade secrets as a means to protect important business information, strategies and practices from competitors. American companies, especially those with manufacturing and fabrication facilities abroad, are becoming increasingly aware of the potential for misappropriation of their trade secrets. An alternative to traditional enforcement actions in state or federal court can be found through investigations instituted before the U.S. International Trade Commission pursuant to Section 337 of the Tariff Act of 1934.



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Although the majority of Section 337 investigations involve allegations of patent infringement, U.S. companies should not overlook the fact that a growing number of parties have successfully alleged other types of unfair acts besides patent infringement.[1] In particular, Section 337(a)(1)(A) declares “[u]nfair methods of competition and unfair acts in the importation of articles ... into the United States, or in the sale of such articles by the owner, importer, or consignee, the threat or effect of which is —

- (i) to destroy or substantially injure an industry in the United States;
- (ii) to prevent the establishment of such an industry; or
- (iii) to restrain or monopolize trade and commerce in the United States.”[2]

The commission has long interpreted this portion of Section 337 to include trade secret misappropriation among the “[u]nfair methods of competition and unfair acts” that it declares unlawful and does not shy away from excluding foreign articles from entry into the U.S. on such a basis.[3] For example, in April 2015, the commission reaffirmed its commitment to pursuing investigations based on the theft of trade secrets by issuing an exclusion order that enjoined a respondent from importing into the U.S. its products using the complainant’s trade secrets for a period of 10 years.[4]

When the alleged unfair act is infringement of granted intellectual property under a federal statute (for example, a U.S. patent, copyright, trademark, etc.), a complainant must establish importation, infringement, and the existence of a domestic industry. On the other hand, in order to establish a nonstatutory unfair act — such as trade secret misappropriation — Section 337 requires that the complainant prove all of the foregoing elements and, in addition, demonstrate that the alleged unfair

act causes an actual injury or a threat of injury to a domestic industry.[5]

In this article, we discuss the types of evidence required to establish injury to a domestic industry in such cases.

Establishing a Domestic Industry for Trade Secret Misappropriation

A complainant may satisfy the domestic industry requirement for a trade secret misappropriation claim by establishing either that:

1. the domestic industry that is the “target” of the trade secret misappropriation exists and has been or is threatened to be “destroy[ed] or substantially injure[d]” by the trade secret misappropriation, or
2. the “establishment” of such a domestic industry has been “prevent[ed]” by the trade secret misappropriation.[6]

Injury to a Developed Domestic Industry

The commission has defined a developed domestic industry as “that portion of complainant’s domestic operations devoted to utilization of the confidential and proprietary technology at issue which is the target of the unfair acts or practices.”[7] Injuries to the complainant’s domestic industry due to the misappropriation of trade secrets can include lost sales/profits, price erosion, loss of reputation, or lost customer relationships.[8] In determining whether certain unfair methods or acts have had the effect of destroying or substantially injuring a domestic industry, the commission has considered a broad range of factors, including (1) the respondent’s volume of imports and penetration into the market; (2) the complainant’s lost sales;[9] (3) underselling by the respondent; and (4) the complainant’s declining production, profitability, and sales.[10]

Injury to a Nascent or Embryonic Domestic Industry

In determining whether certain unfair methods and acts create a “threat” of destroying or substantially injuring a domestic industry, the commission has identified two types of parties that generally are protected from such unfair acts: “(i) parties which have just begun manufacturing operations and for which section 337 violations would have the effect or tendency of frustrating efforts to stabilize such operations; and, (ii) parties which are about to commence production and for which section 337 violations would have the effect or tendency of frustrating efforts to found a business.”[11]

The former category of parties — referred to as “nascent” industries — are parties that have begun manufacturing a product within the industry threatened or affected by the unfair acts, but have not yet stabilized their operations.[12] And the latter category of parties — referred to as “embryo” or “embryonic” industries — are parties that have not yet started manufacturing a product within the industry threatened or affected by the unfair acts, but have established a “readiness to commence production.”[13]

In *Diamond Coated Textile Machinery*, for example, a “nascent” industry was found to exist in which the complainant was manufacturing products within the identified domestic industry but an economic down-turn “prevented it from expanding its operations [and] maturing into a viable domestic industry.”[14] And in *Ultra-Microfused*, the “readiness” requirement for an “embryonic” industry was construed as requiring some “overt act which can be interpreted as an unmistakable indication of a

readiness to commence production.”[15] Accordingly, prevention of the establishment of a domestic industry may be found where the unfair acts of the respondent frustrate the complainant’s efforts to move beyond such “nascent” or “embryonic” stages of development.

In this context, the commission has considered certain conditions or circumstances from which probable future injury can be inferred, including foreign cost advantages and production capacity, the ability of the imported product to undersell the domestic product, or substantial foreign manufacturing capacity combined with the respondent’s intention to penetrate the U.S. market.[16]

Types of Evidence to Establish Injury

The evidence required to establish injury will depend upon the nature of the trade secrets at issue. In general, to qualify as a trade secret the information in question must have commercial value, and must not be generally known. In addition, the owner of this information must demonstrate that it has taken steps to prevent the disclosure or dissemination of this information. Many different types of information could potentially meet these requirements. However, a useful distinction can be drawn between technical trade secrets and business trade secrets.

Technical trade secrets can include scientific results, technologies, production processes, formulas or “know-how.” A company that has developed a valuable new technology may choose to protect it either by applying for patent protection, or by maintaining it as a trade secret. But even if a company has applied for a patent, it may still possess valuable “know-how” regarding how best to use or deploy this technology, and may elect to protect that know how as a trade secret.

Technical trade secrets, like patents, enable a company either to produce a superior product, or to produce a product less expensively. The possessor of such a trade secret will generally be the only firm in the market possessing such advantages, and as a result, it will enjoy competitive advantages. It can expect to win a higher market share, to charge a higher price, to enjoy wider profit margins, and/or to enjoy a better reputation than its competitors. The consequences flowing from misappropriation of a technical trade secret by a competitor involve the loss of these advantages. The types of injuries that follow include lost sales, price erosion, and loss of reputation. Loss of reputation can include the loss of the original trade secret owner’s reputation as a seller of unique and innovative products. If the entity that misappropriated the trade secret bungles the initial implementation of the technology, the trade secret owner’s loss of reputation can include a reduction in the willingness of a buyer to consider the purchase of products embodying the technology. The evidence needed to show injury in such cases relates to efforts to develop and sell products embodying the technical information in question, attempts to emphasize the features enabled by the technology in sales or marketing materials and activities, or indications that the information has been used in a production, research or testing setting.

Business trade secrets can include a wide range of commercially sensitive business intelligence. Such secrets can include information about specific market opportunities identified by the trade secret owner, information about the owner’s cost structure or pricing strategy, information about the owner’s plans and business strategies, customer lists, or information about specific customer requirements or plans. One of the important characteristics of such confidential information is that it can generally be used most effectively against its original owner. Thus, a misappropriator seeking to use such information in order to gain sales will tend to take sales disproportionately from the original trade secret owner. The types of injuries flowing from such misappropriation will include lost sales, lost customer relationships, and/or price erosion.

The evidence needed to show injury from misappropriation of business trade secrets generally relates to the marketplace behavior of the alleged misappropriator. It is often helpful to demonstrate that the misappropriator is targeting existing or potential customers of the original trade secret owner, or is winning sales from the original trade secret owner in repeated head-to-head selling situations. Also extremely helpful are documents demonstrating that the misappropriator is using trade secret information in formulating competitive bids or pricing strategy.

In *Crawler Cranes*, Sany Heavy Industry Co. Ltd., a Chinese heavy machinery manufacturing company, was accused of, inter alia, misappropriating the trade secrets of Wisconsin-based Manitowoc Cranes. Sany was accused of misappropriating both business and technical trade secrets, including Manitowoc's marketing and business plans for certain crawler cranes, cost and pricing information, manufacturing process and procedures, and engineering design standards and plans.

The commission first rejected Sany's argument that the alleged trade secrets were not protectable because they were generally known ideas that lacked economic value. For example, with respect to a business trade secret regarding pricing, the Commission found that "Manitowoc spends a substantial amount of time and resources setting its dealer discount prices ... [and] determines the cost and pricing information on a model-by-model basis." [17] Similarly, the commission found that "Manitowoc's [technical trade secrets] for processing large weldments are valuable because they are important to the quality of the crane and they took many years to develop." [18] In addition, the commission determined that Manitowoc took appropriate steps to preserve the confidentiality of its secrets and limited outside dissemination only to certain customers. [19]

Conclusion

In summary, proving injury in trade secrets cases is a fact-intensive exercise. Counsel and economic experts preparing to demonstrate actual or threatened substantial injury to established or nascent domestic industries in such investigations should marshal evidence using the following checklist:

- lost sales to respondent;
- respondent's import volume;
- underselling;
- price erosion;
- reduced profits;
- declining domestic production;
- foreign cost advantages and production capacity;
- marketing campaigns targeting the owner's customers; and
- respondent's demonstrated intentions to penetrate the U.S. market.

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[1] Gary Hnath & James Gould, Litigating Trade Secret Cases at the International Trade Commission, *AIPLA Quarterly Journal* 19, pp. 87–122 (1991). See, for example, *Certain Crawler Cranes and Components Thereof*, USITC Inv. No. 337-TA-887.

[2] 19 U.S.C. § 1337(a)(1)(A).

[3] See, for example, *Certain Cast Steel Railway Wheels, Processes For Manufacturing Or Relating To Same And Certain Products Containing Same*, USITC Inv. No. 337-TA-655, Initial Determination, at p. 12 (October 2009) (“Cast Steel Railway Wheels”).

[4] *Certain Crawler Cranes and Components Thereof*, USITC Inv. No. 337-TA-887, Comm’n Op. at p. 70 (April 2015) (“Crawler Cranes”).

[5] *Certain Rubber Resins & Processes for Mfg. Same*, USITC Inv. No. 337-TA-849, Comm’n Op., at p. 10 (February 2014) (“Rubber Resins”).

[6] *Cast Steel Railway Wheels*, at p. 80 (“injury or destruction”); *Certain Caulking Guns*, USITC Inv. No. 337-TA-139, Initial Determination, at pp. 54–55 (November 1983) (“prevention of establishment”).

[7] *Certain Processes for the Manufacture of Skinless Sausage Casings and Resulting Product* USITC Inv. No. 337-TA-169, Initial Determination, at p. 341 (July 1984).

[8] *Certain Electric Power Tools, Battery Cartridges, and Battery Chargers Contents*, Inv. No. 337-TA-284, Initial Determination, at p. 246. (June 1989); *Certain Grain Oriented Silicon Steel (“Silicon Steel”)*, Docket No. 1479.

[9] With regard to lost sales specifically, due to patent infringement, the Commission has recognized that: “a patent is a lawful monopoly, and the owner of a valid patent is entitled to 100 percent of the domestic market for the product covered by the patent. Thus, all sales of infringing articles covered by a patent rightfully belong only to the patentee. Similarly, any share of the market for a patented article held by an infringer represents a market share that rightfully belongs only to the patentee.” *Certain Spring Assemblies and Components Thereof and Methods for their Manufacture*, USITC Inv. No. 337-TA-88, Comm’n Op., at p. 43. (July 1981). Depending on the nature of the product and the industry, even the loss of a single sale may amount to a substantial injury under Section 337. See, for example, *Certain Papermaking Machine Forming Section for the Continuous Production of Paper and Components Thereof*, USITC Inv. No. 337-TA-147, Initial Determination, at p. 115 (February 1984); *Certain Steel Rod Treating Apparatus And Components Thereof*, USITC Inv. No. 337-TA-97, Comm’n Op., at p. 61 (December 1981); and *Certain Large Video Matrix Display Systems and Components Thereof*, USITC Inv. No. 337-TA-75, Comm’n Op., at p. 23 (June 1981).

[10] *Certain Electric Power Tools, Battery Cartridges, and Battery Chargers Contents*, USITC Inv. No. 337-TA-284, Initial Determination, at p. 246 (June 1989) (“Electric Power Tools”).

[11] *Certain Ultra-Microfused Freezing Attachment*, USITC Inv. No. 337-TA-10, Comm’n Op., at p. 10 (April 1976) (“Ultra-Microfused”).

[12] *Certain Airless Paint Spray Pumps and Components Thereof*, USITC Inv. No. 337-TA-90, Comm’n Op., at p. 16 (November 1981).

[13] Ultra-Microfused, at p. 10.

[14] Certain Composite Diamond Coated Textile Machinery Components, USITC Inv. No. 337-TA-160, Initial Determination, (May 1984).

[15] Ultra-Microfused, at p. 10.

[16] Electric Power Tools, at p. 248. See also, Certain Air Impact Wrenches, USITC Inv. No. 337-TA-311, Initial Determination, at p. 139 (May 1991).

[17] Crawler Cranes, at p. 48.

[18] Crawler Cranes, at p. 51.

[19] Crawler Cranes, at p. 38. See also, Crawler Cranes, at p. 34 (citing Sausage Casings, Initial Determination) (The protective steps included having employees sign confidentiality agreements, marking documents with sensitive information as “confidential,” and securing access to Manitowoc’s computer system.).

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