RICO REPORT

The Intersection of RICO, Trade Secrets, and the Defend Trade Secrets Act

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[CAL STEIN]

Hello and thank you for joining me on this special installment of the RICO Report where we're going to talk with two of my excellent colleagues here in the Troutman Pepper Boston office about the intersection between trade secret law and RICO with a particular focus on the Defend Trade Secrets Act. My name is Cal Stein and I'm a partner in the White Collar and Litigation Practice Groups at Troutman Pepper. I represent clients in white collar criminal and government investigation matters as well as in complex civil lawsuits and in RICO litigation. As I mentioned I am very pleased to be joined today by two of my wonderful colleagues here in Boston, Will Taylor and Jackie Essinger. Will is a Partner in our Business Litigation Department and Jackie is an Associate in that department. Will, let's start with you, it's great to have you here. Why don't you introduce yourself.

[WILL TAYLOR]

Well Cal thanks very much for having us here today. I'm a Commercial Litigation Partner in the Boston Office and I handle complex business disputes both locally, nationally and internationally and I've had the good fortune of practicing with Cal and Jackie in RICO and trade secret matters.

[CAL STEIN]

Terrific. Thank you for those kind words Will. And now Jackie it's great to have you here as well. Why don't you introduce yourself.

[JACKIE ESSINGER]

Thanks Cal it's great to be here. My practice is similar to Will's. I focus on complex commercial litigation here in Boston but also practice nationally as well. I'm frequently involved in RICO contract cases, cases involving business torts and trade secret misappropriation cases.

[CAL STEIN]

Well thank you both so much for being here to talk about the Defend Trade Secrets Act or the DTSA as I think we'll be calling it in the context of RICO. Now the DTSA is a federal criminal and civil statute and the violation of the DTSA among the offenses listed as racketeering activity in the RICO statute at 18 U.S.C. 1961. So that is why we are going to be talking about it in this RICO podcast. This is a topic that is pretty narrowly focused. And more narrowly focused than many we have discussed on this podcast already. But I think appropriately so, given the relative newness of the law and the many interesting legal questions and issues that have arisen and will continue to arise in these cases. Like many RICO practitioners, I have plenty of experience with fraud-based RICO cases but the trade

secret-based RICO cases that we are going to discuss here today are relatively new. So we are fortunate here who have been litigating trade secret and DTSA cases for some time. So before we jump into our discussion about the DTSA and DTSA RICO cases, I want to start by providing just a little bit of context. Congress enacted the Defend Trade Secrets Act in May of 2016. The DTSA is found in Title 18, Chapter 90 and it includes 9 subsections – Sections 1831 – 1839 and it includes both criminal and civil provisions. When it enacted the DTSA, Congress also amended the RICO statute to add violations of the DTSA to the definition of racketeering activity. Interestingly, though, Congress did not specify that any violation of the DTSA constituted racketeering activity, only violations of §1831 titled Economic Espionage, and §1832, titled Theft of Trade Secrets. We will talk about this distinction in greater detail in a little bit. But with that context, I do want to get into the substance of the topic. And so I want to first turn to you Will and let's start with the big picture. Generally, what does the DTSA do and how does it help protect trade secrets?

[WILL TAYLOR]

Yeah Cal, thanks for that introduction because it is important to know that this is a new statute, only 6 years old, but the concept of trade secrets has existed for a long, long, long time in common law and in fact it was the desire to modernize the way that trade secrets were being protected which led to the Congress passing the Defend Trade Secrets Act. To over-simplify the Defend Trade Secrets Act is exactly as it sounds – it is to protect confidential and proprietary information and that provides the owner of the trade secret with a business advantage. There's some real teeth to this statute and I'll just briefly say that Cal mentioned 1831 and 1832, which are two different sections of the DTSA, §1831 the espionage, economic espionage angle, that really is focused on the involvement of a foreign party. Whether it's a foreign government or a foreign agent or a foreign instrumentality. §1832 goes to the same concept – the stealing of the trade secrets – but doesn't have that foreign aspect.

[CAL STEIN]

Thanks Will. So I mentioned before there were both criminal and civil components of the DTSA. The criminal components captured in the two sections Will just discussed – §1831 and §1832. I want to turn now to the civil components of the DTSA and I'm going to turn to you, Jackie, for this. What do the civil components of the DTSA entail and how do they differ from the criminal part of the statute.

[JACKIE ESSINGER]

There's really two main elements that plaintiff needs to prove to show trade secret misappropriation under the civil component and then there's of course damages. But first the owner needs to show that it owns the trade secret and then second, that the trade secret is misappropriated. The definition of a trade secret is really quite broad under the statute. It's really all types of information. A quintessential example I'm sure we all think of is you know the recipe for Coca-Cola. But more often what we see in litigation involves customer lists or pricing information but it also can be processes or techniques, designs, prototypes, methods, really just any kind of tangible or intangible information. But the plaintiff also needs to show that it took reasonable measures to keep that information secret. So if Coca-Cola had poster boards up in the factory with the recipe and didn't do much to stop employees from bringing phones in, then that wouldn't be a reasonable protection of the trade secret. And then also the trade secret has to derive economic value from not being generally known. So that's the

first element – trade secret. And then the second one is misappropriation. So misappropriation occurs when a person acquires a trade secret by improper means or disposes or uses that trade secret that was acquired by improper means. And improper means can really be a number of things. It can be theft. It can be bribery. It can be misrepresentation. It can be breach of a duty to maintain the confidentiality of the secret. So taking the example of Coca-Cola, if they have all employees sign NDAs and keep the recipe to a small group of people and don't allow phones around the recipe but an employee accesses it and takes a picture of it with their cell phone and then sends it to a friend, that would be misappropriation. So that's the misappropriation element and then I'll just discuss about damages quickly. So a plaintiff who wins may be entitled to money damages and those money damages can be for, you know the actual loss. So something like lost profits. It could be unjust enrichment. You know that's looking at whether the defendant gained or saved through the misappropriation or it could be a reasonable royalty and that would look at what a hypothetical licensor would have paid to use the trade secret.

[CAL STEIN]

Thanks Jackie. And we're going to talk a little bit more later about the distinction between the criminal side of the statute which really does, as Will mentioned, require theft of trade secrets versus the civil side where misappropriation which can include some other things is all that is needed that Jackie mentioned. What I want to talk about now is I do want to bring this overview of the DTSA statute within the ambit of RICO. And I want to start again with the big picture. Will and Jackie, you guys follow the case law regarding the DTSA pretty carefully. And there haven't been that many RICO cases yet where a plaintiff has alleged violations of the DTSA as the underlying for racketeering activity. But Will, from your review of the cases and following of the law, what can you tell us about what those few cases that have been brought typically look like?

[WILL TAYLOR]

As a starting place it's really simple as far as the ingredients of a trade secret case that might come under the ambit of RICO. And it typically involves an employee or employees and a competitor. That means that the employees of a trade secret owner, so in the situation that Jackie just referred to, so employees of Coca-Cola, taking the trade secrets from Coca-Cola and going to a competitor or somebody else who is going to use them. That's sort of the typical fact pattern and if not, Coca-Cola is like an off-site example and it is a legitimate one. Just three days ago a chemist from Coca-Cola was convicted for 14 years in prison for stealing trade secrets related to how the cans were manufactured and protected. So in that case the chemist was a long-time employee of Coca-Cola and the trade secrets had been developed by Coke and a few other companies, and the chemist took the trade secrets and was convicted of giving them to third-parties in China.

[CAL STEIN]

So that's a really helpful paradigm for how we can think about some of these cases. Jackie you've also read the cases and followed this law. What are the typical types of conduct that we might see in these DTSA RICO cases?

[JACKIE ESSINGER]

So you know every case is different but just some examples of the type of conduct we saw because you know the conduct is really everything. That's the crux of it, what do the plaintiffs allege defendants actually did. And so you know in one case we saw a former employee taking 27,000 files from the plaintiff/employer before setting off to draw in a competing business. In another a group of employees left to start their own, new competing business and they relied on an employee still working for plaintiff to syphon materials to the employees that left. And then in a final example, former employees took some marketing material from the plaintiff/employer to their new company and simply slapped a new logo on the documents and started using them to compete with the plaintiff.

[CAL STEIN]

That's all really helpful in thinking about the DTSA. And the DTSA, since we keep seeing these same types of cases with the same ingredients over and over, there's pretty good insight and plaintiffs know exactly what they have to prove to succeed in a DTSA case. Which brings up a point that the three of us discussed while preparing for this podcast. And actually a question that you guys asked me which is why would you even bother, right? Why would you bother bringing DTSA claims under RICO. It's harder to plead, it's harder to prove. And in thinking about that there are really two answers to that question. The first is damages. There are enhanced damages under both statutes but RICO offers more. As Jackie mentioned earlier, the DTSA offers up to double damages. RICO offers up to triple damages. The DTSA uses the term may. A Court may award exemplary damages in an amount not more than 2x the amount of the damages proven. RICO's triple damages provision uses the word shall. The Court shall award them or a person injured shall recover 3 fold. So in short, RICO offers plaintiffs an opportunity to get more damages and an easier path to getting the Court to award them. In addition and the other topic we really talked about here is the scope of the statutes. And RICO, as we know from discussions in prior episodes, was enacted for the purpose of casting a wider net in terms of defendants that could be reached. Think back to when RICO was passed. It was passed specifically to combat organized crime. Where the bosses or the higher ups were often a step or two away from the actual malfeasance. And prosecutors and plaintiffs were having difficulty reaching them. So RICO was enacted to capture anyone who participates, for example, in the conduct of a RICO enterprise. So it's not hard to imagine a scenario where a plaintiff seeking to assert DTSA claims would want to use RICO to broaden the scope and the reach of the lawsuit against additional defendants that it would otherwise not be able to reach under the DTSA itself. So while there are additional pleading requirements and proof requirements when you wrap up a DTSA case in RICO, there really are some significant benefits or potential benefits for plaintiffs and that's why we've seen some of these cases and I expect that we will see more. And all of that is actually a nice segue way into one of the main discussion points that we want to focus on and it has to with what conduct would actually constitute racketeering activity under the RICO statute? And more pointedly, whether RICO's definition of racketeering activity embraces both criminal and civil violations under the DTSA or just criminal violations under the DTSA. And unfortunately this is a bit of an open question as Courts that have analyzed this have come down differently on the issue. So Will why don't you take us through some of the reasoning we've seen from the courts when they have found that only criminal violations of the DTSA constitute racketeering activity.

[WILL TAYLOR]

The courts have applied sort of classic statutory analyses. They look first to RICO and say which portions of DTSA did it specifically address and as Cal mentioned at the outset of this podcast it specifically addressed Sections 1831 – the economic espionage section and the trade secret misappropriation of §1832. It did not address §1836 which is the civil section that Jackie described earlier. So from a starting place the courts were saying, okay, the RICO amendment applies to the criminal section of the DTSA not the civil sections. Then it looked at the language of §1832 and it compared it to §1836. So it compared the criminal section versus civil section and it noticed that the sort of key difference between the two is that §1832, the criminal section, really focused on facts. The knowing taking of something or the knowing receipt of something that you knew was taken from the trade secret honor. It really focuses on that knowing conduct. The civil section is much broader. It uses terms like use and misappropriation and says use and misappropriation are alone enough to establish civil liability. But the courts have pointed out use and misappropriation are not in and of themselves enough to establish criminal liability. Just for discussion sake, and Jackie and Cal feel free to disagree with me, there two different concepts are theft versus use.

[CAL STEIN]

I think that is a helpful concept and a helpful distinction to make and your description of how those courts came down you know makes some sense in and of itself. Jackie, I want to turn to you to talk about the other courts, the ones that say no civil violations of the DTSA do constitute racketeering activity. How did those courts reach that decision?

[JACKIE ESSINGER]

There are a few cases holding that pattern of just use of a trade secret is sufficient to plead racketeering activity. For example just last year the Central District of California denied a defendant's motion to dismiss and concluded that pleading use of a misappropriated trade secret qualified as racketeering activity under RICO. In this case we have that prototypical fact pattern where former employees allegedly stole and used various trade secrets including customer lists and pricing models to set up a competing business. And in denying the defendant's motion to dismiss, the court concluded that plaintiff demonstrated racketeering pattern through allegations that defendants used the trade secret on numerous occasions and also continued to use that information to market an almost identical product.

[CAL STEIN]

So that all makes sense but let's bring this back to the practical. Why does it matter? Why does it matter from a RICO standpoint whether its criminal violations of the DTSA or both criminal and civil? And Will you talked about the distinction between theft and use and certainly it's harder to prove theft, one would think, than it is to prove mere use. But is that really it? Is it that simple as to why this matters so much.

[WILL TAYLOR]

I'm actually going to answer that by throwing it back at you. So you handle a lot more criminal cases than I would and I'll say you know the word theft is sort of overused in the sense that people use it in a variety of contacts, you stole this, you stole that. The legal term theft does have some meaning. So to put it back into your camp as a lot of experience in criminal

cases, isn't it meaningful that there is the additional evidentiary threshold for a theft case than there is in a civil context?

[CAL STEIN]

I think you're right. There's no question that theft connotes a lot more than mere use. And I think we see that from the drafters of the DTSA itself. They separated the two for a reason and required proof of theft for the criminal violation and only mere use for the civil violation. That's why I asked if it's really that simple because it does seem that simple on the one hand but certainly this is an issue that is going to continue to be resolved by courts. And it's a little strange to see courts coming down so differently on this one issue. And based on some of that emerging case law, as Jackie said, there are some cases that say you know look a single fact is not going to make a pattern of racketeering activity which of course is a requirement of the RICO statute. So I want to ask you Jackie, there has been this kind of concept of a theft plus model that has emerged. And by that I mean RICO plaintiffs needing to plead a theft of a trade secret in violation of the DTSA so violating the criminal section but also some sort of other unlawful conduct with it that constitutes racketeering. What do you think about that Jackie? Have you seen that in the cases?

[JACKIE ESSINGER]

Yeah, I think that's right. Theft alone as you and Will just talked about is harder to prove a pattern of that. So if you're not in a jurisdiction where the court is likely to say that a pattern of use is sufficient under RICO, you really do need to plead theft. Plus I think paring the theft with something like wire fraud or mail fraud often makes sense because you know in a lot of these cases the plaintiffs are alleging that defendant downloaded and transmitted the trade secrets through emails or some other electronic means so that they could then make use of them. But the wire fraud, mail fraud combined with theft might be sufficient to make up for not having a pattern of theft.

[CAL STEIN]

So now let's pivot to discuss another one of these issues that's come up in the case law. And that is how a plaintiff that wants to bring a RICO claim due to a DTSA violation can plead or has pled, another one of the critical elements of the RICO statute, that of the RICO enterprise. And before we jump in, let me briefly give an overview of that element under RICO law. As we know, the RICO statute requires any RICO plaintiff to prove the existence of a "enterprise" and broadly speaking the reason for this is that RICO does not target the enterprise itself. Which could be and often is legitimate. Rather the RICO statute targets the individuals who misuse or wrongfully acquire the enterprise. And there are a number of different ways that a plaintiff can prove or allege the existence of an enterprise and we will spend an entire episode of this podcast talking about that. But for present purposes, the most common type of RICO enterprise is something called an association in fact enterprise. Which basically and broadly means there's a group of entities or individuals who are associated together and in many jurisdictions there is also the requirement that they exist for some purpose other or independent from the alleged RICO violation and we will get to that in a moment. But again I do want to start broadly, the entire concept of an enterprise that engages in a pattern of racketeering activity, embraces the idea that multiple parties are involved and that whatever misconduct is occurring is in fact occurring over a lengthy period of time. And Will you talked earlier about the typical ingredients we see in these DTSA RICO cases but looking more

broadly to your DTSA experience, how does that paradigm of multiple parties and misconduct over time, how does that paradigm jive with what you have seen in DTSA cases more generally?

[WILL TAYLOR]

There seems to be a natural fit between the sort of typical fact pattern we see in DTSA cases and this enterprise requirement. Because as I mentioned earlier, the fact pattern we see not just in RICO cases but in a lot of trade secret law, is an employee taking information to give to a competitor or to create a competitor or to start a competitor with other employees from the former employer. So it's not to say that's the exclusive fact pattern. It's certainly possible that a single actor would take the trade secrets and then go out on his or her own. But more often than not clearly as the technology gets more and more sophisticated and it would be hard to do the competitive activity alone, I would expect the pattern we've seen so far would hold. That being that there really is often this enterprise setup in order to carry out the acts that constitute trade secret theft.

[CAL STEIN]

That makes perfect sense. And so because these trade secret or these DTSA allegations are consistent with this concept of an enterprise, I agree with you Will. There is a natural connection there. I want to flip now to talk about the issue I mentioned a moment ago which is the purpose of the enterprise. And as I mentioned, some jurisdictions require a RICO enterprise to exist for a purpose other than the alleged violations of the statute and the specifics of the legal decisions on this particular topic are very nuance. So we're not going to get into them here today. But for now I want to talk about it in the context of the DTSA/RICO cases that we've seen. And we have seen plaintiffs being challenged by pleading an enterprise purpose in these DTSA/RICO cases that's separate from the racketeering activity, i.e., the DTSA violation itself. So Jackie I know you and I have discussed a case where this came up. Can you talk about that case a little bit.

[JACKIE ESSINGER]

Sure and this is the case I mentioned earlier out of the Central District of California and it's a good example of this point. So at first plaintiff alleged that the common purpose of the enterprise was to steal trade secrets to harm the plaintiff. And the court said this wasn't good enough and it conflated the purpose of the enterprise with the pattern of racketeering. And so it granted the defendant's motion to dismiss and dismiss the RICO claims. But the court allowed plaintiff to replead and in its Amended Complaint the next time plaintiff alleged that the enterprise purpose was to direct business away from plaintiff to defendant's new company. And the court this time denied defendant's motion to dismiss and concluded that this allegation sufficiently stated a common purpose apart from the racketeering activity. So these two opinions are good examples to look at for how to properly plead this element and it really was a pretty subtle, small change that the plaintiff had to make but it made all the difference in that case.

[CAL STEIN]

Yeah, subtle and small but at the same time it seems that it's pretty straight forward how a plaintiff has to plead the difference in the purpose and one that probably exists in many of the

cases. It doesn't strike me as a big list but more of a pleading requirement. What's your take on that Will?

[WILL TAYLOR]

Agreed and here is where you know we as lawyers have got to remember the reality of the situation. The reason somebody or somebodies steal trade secrets is not for the fun of it. There's no benefit in and of itself of taking a trade secret. You take a trade secret cause you want to be able to develop your own business or you want to compete with the existing business or you want to harm the existing business.

[CAL STEIN]

What next guys? We mentioned a few times today that there just haven't been all that many DTSA cases period because it's a relatively new statute. At least there haven't been that many yet. Which means there will be even fewer DTSA/RICO cases. But when I hear that what it means to me is that the DTSA/RICO story is not yet written. I want to hear from you guys about what you think is going to come next in terms of DTSA/RICO cases and judicial decisions on that. And let's start with you Jackie. What do you think is coming?

[JACKIE ESSINGER

Sure so I definitely agree. I think we'll see more RICO/DTSA cases and as the law develops we'll likely see it applied to wider fact patterns which will lead to more RICO plaintiffs trying to weaponize the statute. Additionally in particular I think these cases will increase because as Cal mentioned earlier with RICO you can get more damages and reach more defendants than in a typical DTSA case. So even though a RICO plaintiff has a secret battle to prove a claim, those non-discretionary higher damages and attorneys' fees are going to be really enticing and make it worth asserting a claim. So I think you'll start to see a lot more RICO claims being pled along with a DTSA claim.

[CAL STEIN]

What about you Will? What do you think we're going to see?

[WILL TAYLOR]

Well this is it's a prediction and a question for you. So the prediction is that as you alluded to earlier, that plaintiffs will be more attentive to pleading the sort of theft plus situation. That means theft plus some other predicate act like mail and wire fraud which is the recognized predicate act. The reason being is that it can be difficult, as we talked about today, to show a pattern of theft because it might just require one single act. Like in one fell swoop you take the trade secret and you're out the door. So there's not multiple instances of theft. Now I'll say it does happen sometimes that bad actors are accused of downloading trade secrets over a period of time. There you might actually have a pattern of theft. But as we said earlier it can be difficult to show. So let me ask you, with that prediction in mind, you're the mail and wire fraud guy, is a bad actor or accused bad actor who is accused of stealing trade secrets, most likely in today's world those trade secrets are then sent over email or taken across state lines and given to a competitor. What kind of things was the bad actor doing with the trade secrets compromise the predicate act that could get at the pattern that a plaintiff would need to show.

[CAL STEIN][

I think you're exactly right on the statutes of the predicate act that you referenced, the mail and wire fraud statutes. Conceptually it really shouldn't be all that difficult for plaintiffs to add mail and wire fraud allegations and pair those with DTSA allegations to form a pattern. As you mentioned, emailing, using data rooms or other file transfer programs that are becoming more and more prevalent. Those types of things are typically the stuff of wire fraud allegations. So conceptually it's not that difficult or hard to see those being added. But it does add a new pleading requirement which is often attacked even at the motion to dismiss stage. Because as we know fraud allegations, including mail and wire fraud, have to be pled with particularity under Rule 9(b). So to your prediction, one practical thing that may come out that is more mail and wire fraud allegations and therefore more motion to dismiss practice trying to cut off these cases before they get started.

[WILL TAYLOR]

One other point we were talking about sort of how plaintiffs will react to the case law they've seen so far, relates back to the statutory analyses I talked about earlier. And I reduced it in very simple terms to theft versus use. The theft concept comes from the criminal section, again, §1832. Now as I hopefully said earlier that was an over-simplification. The bad acts that are targeted by that section are far broader than your sort of classic theft. They also relate to when someone knowingly does a variety of other actions like destroy the trade secrets, photocopy them, replicates it, transmits it, delivers it, sends it, mails it, communicates it, conveys it. So a lot of the acts that I think would probably apply to the mail and wire fraud predicate that you just spoke about are also spoken about in the explicit language of §1832. So I think I've had some plaintiffs who were following this DTSA/RICO case law develop so far will likely be able to take advantage of that language. Now a note of caution is that some courts have already said that if they use that language I just talked about like destroying, communicating, conveying and analyze that to just use, that's not going to fly. The court really don't want to criminalize the serial use of a trade secret. So when the plaintiff who stole all the trade secrets related to the development of bricks, if every single time the brick was manufactured, the courts don't regard that as a separate bad act that could qualify as a predicate act under RICO. That could qualify as a use that is prohibited by the civil portion of it but the court so far have been leery of saying those individualized uses are what constitutes a predicate act.

[CAL STEIN]

And what you're really talking about Will is the development of the pattern of racketeering element of RICO in these DTSA cases and actually my prediction of what's coming next focuses on that as well. I refer to a recent case that came out of Washington, D.C. where the plaintiff alleged 12 separate predicate acts that were all centered around a single scheme to misappropriate trade secrets and the court, at the motion to dismiss stage, the defendant argued that yeah, there are 12 acts here but they only are part of the single scheme that caused a single injury to a single defendant and they cited some pretty well-settled Supreme Court precedent that suggests it's really hard for plaintiff to state a RICO claim when there's only a single scheme, single injury and a single victim. And the judge agreed. And the judge's decision in that case to dismiss the case, was driven by the specific factual circumstances there. But I think given the nature of trade secret misappropriation and DTSA based allegations, given that all we've talked about today, it really wouldn't be surprising to

me to see other defendants try to pursue a similar line of argument at the motion to dismiss stage, especially given the success here in that case. And if we see that and other judges start to agree, it will be an interesting development in DTSA/RICO law. And with that we are about out of time here today. So I want to bring this discussion to a conclusion. Will and Jackie I really want to thank you guys for joining me on the podcast and I also want to thank everyone for listening. I hope you will join us for our next regularly-scheduled installment in which we will be discussing the RICO enterprise elements. If you have any thoughts or comments about this series, I invite you to contact me directly at callan.stein@troutman.com and if you have any thoughts or comments about this episode you can contact me or you can contact Will directly at william.taylor@troutman.com or Jackie at jacklyn.essinger@troutman.com. You can subscribe and listen to other Troutman Pepper podcasts wherever you listen to podcasts, including on Apple, Google and Spotify. Thank you for listening and stay safe.