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Assessing Damages Theories In Recent Trade Secret Verdicts

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Trade secret protection is more important than ever with increased employee mobility, blurred lines between technology collaborators and competitors, ease of transferring digital information, and challenges with enforcing patent rights.

From a litigation risk management perspective, trade secret damages can be a high-stakes undertaking given the multiple theories that can be applied, the wide ranges of claim amounts arising from different damages theories, and the potential for a willfulness multiplier.

In an earlier Law360 guest article, we provided an initial look at the Defend Trade Secrets Act and relevant case law developments at the time. In this article, we provide a brief update on filing statistics of trade secret cases in federal court and discuss two recent trade secret verdicts litigators need to be aware of from a damages perspective.

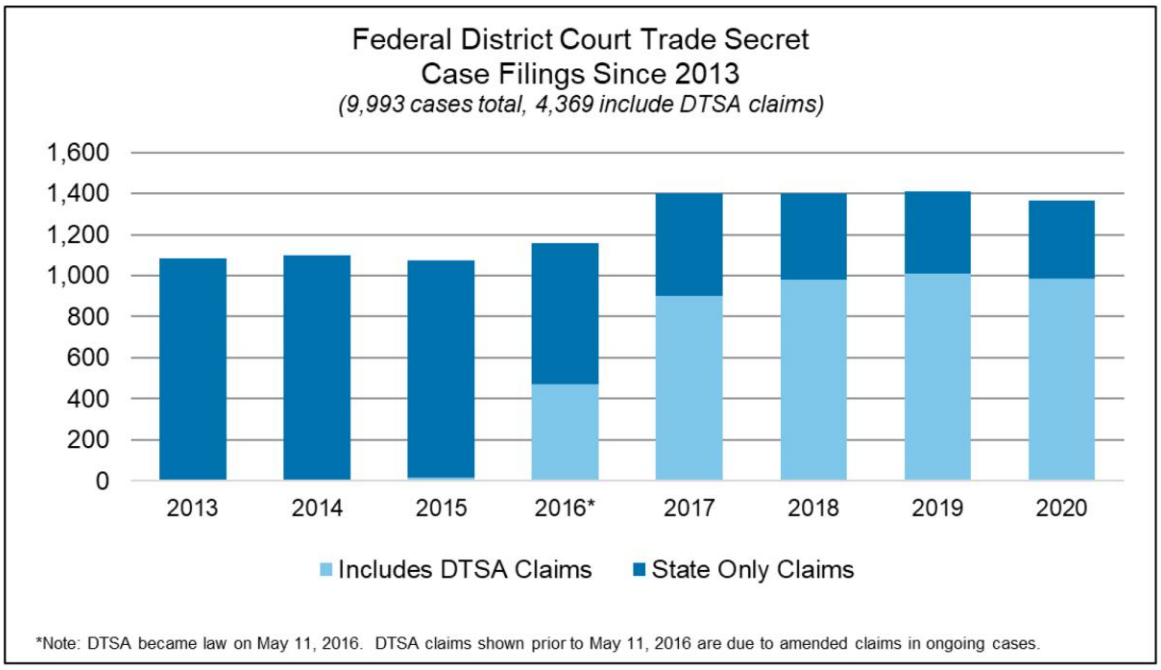
DTSA and Trade Secret Cases Filing Update

Plaintiffs can enforce their trade secret cases under state statutes, based on the Uniform Trade Secrets Act in all but New York, or under the recent federal DTSA. State claims can be filed in state courts and potentially in federal court depending on the parties and claims in the case. DTSA cases are filed in federal district court.

Additionally, trade secrets rights can be enforced in the U.S. International Trade Commission where the remedy is an exclusion order preventing products made using the misappropriated trade secrets from being imported into the U.S.[1] Figure 1 shows the yearly filing history of federal cases with trade secret claims, showing that a majority of federal trade secret case filings include DTSA claims. [2]

Thus far, we have observed only a handful of DTSA verdicts including damages that have been appealed, with no appellate opinions concerning damages as of the end of 2020.[3]

Figure 1 — Federal Trade Secret Misappropriation Filing Statistics (2013-2020)



Trade Secret Damages — Recent Case Law Developments

It is important to monitor and understand both DTSA and applicable state law case verdicts and rulings to optimally develop case filing and litigation management strategies. The remainder of this article will focus on two recent and notable cases that provide insight into damages under state laws and the DTSA.

Avoided Costs Theory: Syntel v. TriZetto

In February 2015, after a terminated contract between Syntel Best Shores Mauritius Ltd. and TriZetto Group and a subsequent lawsuit filed by Syntel in the U.S. District Court for the Southern District of New York, TriZetto filed counterclaims for trade secret misappropriation under both New York law and the DTSA, alleging that Syntel employees illegally downloaded hundreds of TriZetto's key business documents, mostly related to TriZetto's Facets Core Administration software used for health plan administration.[4]

TriZetto pursued multiple theories for damages that were awarded by a jury on Oct. 27, 2020, as detailed in Figure 2 below.

Figure 2 — Damages Theories and Jury Awards to TriZetto

Theory	Damages	Awarded Claim[5]	Methodology[6]
Unjust enrichment (avoided costs)	$284.9 million	DTSA	TriZetto's R&D spend on Facets, excluding client funded R&D, from 2004 to 2014
Reasonable royalty	$142.4 million	New York law	Lump sum royalty based on 50/50 profit split of avoided costs
Lost profits	$8.5 million	*Not awarded*	Single lost project to Syntel ($27 million Syntel revenue)

Syntel filed a motion for judgment as a matter of law, a new trial or remittitur in December 2020, taking issue with the disconnect between TriZetto's claimed avoided costs and lost profits damages. Syntel claimed that TriZetto used an avoided costs theory to multiply the actual harm and to obtain a "compensatory damages windfall more than 27 times its actual claimed lost profits and more than 10 times the total revenue Syntel earned."[5]

Syntel also claimed that a "nontraditional proxy remedy of avoided costs" was an improper theory of damages because actual damages and disgorgement of Syntel's profits were easily calculable in this case.[6]

Syntel echoed many of the same arguments concerning TriZetto's reasonable royalty calculation, which was based purely on avoided costs.[7] TriZetto claimed a lump-sum reasonable royalty under New York law based on a 50/50 split of TriZetto's research and development spend relating to its Facets software.

Interestingly, this methodology effectively used an avoided costs theory as a basis for a reasonable royalty, despite the court's finding that avoided cost damages are not available for the New York trade secret misappropriation claim, under the 2018 New York Court of Appeals decision in E.J. Brooks Co. v. Cambridge Security Seals.[8]

While the court has not yet ruled on Syntel's motion, there are several key takeaways that litigators should consider based on the damages theories presented to, and awarded by, the jury.

First, submitting multiple damages theories with a wide range of potential damages does not necessarily imply that the theories are unreliable and can be an effective strategy for educating the trier of fact on all potential forms of economic harm and unlawful gains. However, each theory must be reliably tied to the facts of the case and should be presented in a manner that avoids the possibility of double recovery.

Second, litigators should evaluate damages theories early in the litigation process. The choice of damages theories can affect discovery efforts, and information learned during discovery can help focus which damages theories can be best supported or rebutted by facts from the case.

Third, counsel should consider the merits of entering a damages claim based on the trade secret owner's development costs as a proxy for the defendant's avoided costs. The court's ruling on motions for judgments as a matter of law may help validate this nontraditional proxy remedy as a viable damages theory. Avoided costs should be considered when they can be accurately determined and properly attributed to the trade secrets at issue, even in cases where lost profits or disgorgement are easily calculable.

Fourth, this case illustrates the flexibility of reasonable royalty claims in trade secret misappropriation cases, and litigators should carefully consider whether a reasonable royalty claim should be proffered. In this case, even though avoided development costs were not allowed by law under the New York state claim for misappropriation, the avoided development costs were used to enter a claim for reasonable royalty.

We also note that the flexibility of a reasonable royalty opinion extends beyond being able to use a measure of damages that is barred by law under an unjust enrichment claim, as observed in the 2018 Steves and Sons Inc. v. JELD-WEN Inc. case, in which the U.S. District Court for the Eastern District of Virginia commented that evidence of damages that would be considered speculative under an unjust

enrichment claim were more appropriate under a reasonable royalty claim of damages.[9]

Trade Secrets and Reasonable Royalty in California: Ajaxo v. E-Trade

Our second case relates to the long-running Ajaxo Inc. v. E-Trade Financial Corp. suit in which Ajaxo sued E-Trade for the misappropriation of its internet-based stock-trading software in 2000 in the California Superior Court for the County of Santa Clara under the California Uniform Trade Secret Act, or CUTSA. The case resulted in three trials and appeals.

Figure 3 — Ajaxo's Damages Theories

Trial	Theory	Damages	Awarded Claim	Methodology
Trial 1	Unjust Enrichment	N/A	*Not Awarded*	N/A
Trial 2	Unjust Enrichment	$301.0 million	*Not Awarded*	¼ of the profit generated from all new accounts during relevant time period
Trial 3	Reasonable Royalty (Model 1 of 2)	$24.2 million	*Not Awarded*	$700,000 master license and 50% of each $510,000 runtime fee for 92 customers
	Reasonable Royalty (Model 2 of 2)	$41.5 million		$700,000 master license and 80 runtime licenses at $510,000 based on user capacity
	Reasonable Royalty (Alternative Model)	$3.3 billion	*Not Awarded*	$15 monthly service fee per customer for E*Trade's entire customer base for six years

The first trial resulted in a partial nonsuit on damages for insufficient evidence and Ajaxo was not awarded damages for misappropriation.[10] Ajaxo appealed the trial court's decision and was granted a new trial on damages for misappropriation. In the second trial Ajaxo's unjust enrichment claim asserted that E-Trade's misappropriation was responsible for 25% of the profit generated from all new accounts during the relevant time period, totaling $301 million.

However, E-Trade introduced evidence showing that the relevant business line, wireless trading, actually realized a loss of $2.4 million during the same time period. The trial court awarded Ajaxo no damages, concluding that E-Trade's data indicated the net enrichment was less than zero.[11] With no unjust enrichment damages awarded Ajaxo asked the trial court to award reasonable royalties under Section 3426 of the CUTSA. The motion was denied.

Ajaxo appealed the trial court's decision to deny a reasonable royalty, arguing that neither unjust enrichment nor actual loss were provable under Section 3426 of the CUTSA, which permits a court to order payment of a reasonable royalty only if actual damages or unjust enrichment is not provable.

The California Court of Appeal, Sixth District, concluded that "where a defendant has not realized a profit or other calculable benefit as a result of his or her misappropriation of a trade secret, unjust enrichment is not provable within the meaning of §3426," and the matter was remanded to the trial court to exercise its discretion in ordering payment of a reasonable royalty.[12]

In the third trial Ajaxo proffered two reasonable royalty theories: $65.7 million, comprised of two components based on an Ajaxo license agreement and assumptions of distribution and user metrics, and

$3.3 billion, based on an end-user subscription model. E-Trade contended that there was insufficient evidence to calculate a royalty with the main reason being the absence of any definition of the misappropriated trade secret or evidence of its economic value.

The trial court ultimately rejected Ajaxo's reasonable royalty opinions, concluding that Ajaxo's reasonable royalty was excessive in amount and relied on speculative, unproven and counterfactual assumptions.[13] Ajaxo subsequently appealed for a new trial based on inadequate damages; however, the court of appeals concluded that Ajaxo did not demonstrate an abuse of discretion in the trial court's denial of its motion for a new trial.

This case provides multiple key takeaways for trade secret owners. First, under Section 3426 of the CUTSA, reasonable royalty damages may be awarded if unjust enrichment was considered but no profits were earned by the defendant. This suggests trade secret owners should carefully consider entering a reasonable royalty claim in the event actual loss or unjust enrichment are not proven.

Second, if plaintiffs plan to rely on prior license agreements to establish a royalty rate, they should consider the technical and economic comparability of the agreements to the hypothetical negotiation and trade secret at issue. They should do so while accounting for any differences if they are not directly comparable, as is often done under the analysis derived from the factors in the 1970 Southern District of New York decision Georgia Pacific v. U.S. Plywood Corp., when plaintiffs seek a reasonable royalty in patent infringement cases.

Lastly, practitioners should recognize, as this case illustrates, that even though reasonable royalty claims may be more flexible, the claims must be based on reasonable assumptions that are supported by the facts of the case and avoid undue speculation or overreaching relative to the economic realities of the market and technology at issue.

Conclusion

With the increasing importance of trade secret protection and risk of misappropriation in today's environment, it is vital to be aware of the remedies available under both state law and the DTSA. The above cases serve to illustrate the potential wide range of damages theories and monetary outcomes that can occur in trade secret cases. Litigators and their clients should be aware of the nuances associated with trade secret damages remedies and recent precedents to ensure successful results throughout litigation procedures.

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[1] Based on CRA analysis of the ITC's 337Info database, there were no investigations instituted in 2020 (through December 21, 2020) that contained trade secret misappropriation claims.

[2] CRA analysis, based on Lex Machina search conducted on January 7, 2021, and includes cases filed between January 1, 2013 and December 31, 2020.

[3] Based on review of dockets for the 16 DTSA cases with a damages verdict shown in Lex Machina, five have been appealed (three are still under appeal, one is stayed due to bankruptcy, and one case settled).

[4] Syntel Sterling Best Shores Mauritius Limited and Syntel, Inc. v. The TriZetto Group, Inc. et al., 1:15-cv-00211, TriZetto Corporation & Cognizant Technology Solutions Corporation's Answer to Amended Complaint and First Amended Counterclaims, June 13, 2016.

[5] Syntel Sterling Best Shores Mauritius Limited and Syntel, Inc. v. The TriZetto Group, Inc. et al., 1:15-cv-00211, Syntel's Memorandum in Support of its Motion for Judgment as a Matter of Law, a New Trial, or Remittitur Pursuant to Federal Rules of Civil Procedure 50(B) and 59, December 4, 2020, p. 25.

[6] Ibid, p. 24.

[7] Syntel Sterling Best Shores Mauritius Limited and Syntel, Inc. v. The TriZetto Group, Inc. et al., 1:15-cv-00211, Syntel's Memorandum in Support of its Motion for Judgment as a Matter of Law, a New Trial, or Remittitur Pursuant to Federal Rules of Civil Procedure 50(B) and 59, December 4, 2020, pp. 27-30.

[8] Syntel Sterling Best Shores Mauritius Limited and Syntel, Inc. v. The TriZetto Group, Inc. et al., 1:15-cv-00211, Order, October 15, 2020, p. 1.

[9] Steves and Sons, Inc. v. Jeld-Wen, Inc., E.D.Va. 3:16-cv-00545-REP, Memorandum Opinion, May 10, 2018.

[10] Ajaxo, Inc. v. E*Trade Financial Corp.48 Cal.App.5th 1 (6th Dist. 2020).

[11] [11] Ajaxo, Inc. v. E*Trade Financial Corp., 187 Cal.App.4th 1295, 115 Cal. Rptr.3d 168 (6th Dist. 2010).

[12] Ajaxo, Inc. v. E*Trade Financial Corp. 48 Cal.App.5th 1 (6th Dist. 2020).

[13] Ibid, p. 24.