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Introduction

- Shawn has more than 20 years of experience providing dispute advisory services to organizations and their counsel.
- He has testified in more than 40 different cases at deposition, trial, and arbitration as an expert witness and has served as a court-appointed receiver. Shawn has been qualified as an expert witness in federal district and bankruptcy courts and state courts across the U.S.
- His intellectual property litigation case experience includes matters involving lost profits, reasonable royalty, incremental profits, fixed and variable costs, product line profitability, valuation, diminution in value, unjust enrichment, and apportionment.
- Shawn has worked on litigation matters involving misappropriation of trade secrets, patent infringement, trademark infringement, trade dress infringement, copyright infringement, false advertising, unjust enrichment, breach of license/technology agreement, and transfer pricing.

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Plaintiff's Expert's Perspective

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Remedies Available to Plaintiff

- Equitable relief (preliminary injunction or permanent injunction)
- Monetary damages (compensatory, unjust enrichment, or restitution damages)
- Legal fees
- Most of these cases are filed in state court, which have varying state laws impacting damages remedies

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Monetary Damages Remedies Available to Plaintiff

- Plaintiff's actual loss (make the plaintiff "whole" after the alleged event)
- Defendant's unjust enrichment (measuring the financial gain realized by the defendant)
- Valuation of trade secrets
- Reasonable royalty
- Depends on facts and circumstances of each case

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Section 1.4 of the UTSA

Section 1.4 of the UTSA states that a trade secret “means information, including a formula, pattern, compilation, program, device, method, technique, or process that

> (i) derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can **obtain economic value from its disclosure or use**, and
>
> (ii) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.”

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Section 3(a) of the UTSA

“Damages can include both the actual loss caused by misappropriation and the unjust enrichment caused by misappropriation that is not taken into account in computing actual loss. In lieu of damages measured by any other methods, the damages caused by misappropriation may be measured by imposition of liability for a reasonable royalty for a misappropriator’s unauthorized disclosure or use of trade secret.”

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Section 3(b) of the UTSA

"If willful and malicious misappropriation exists, the court may award exemplary damages in an amount not exceeding twice any award under Subsection 3(a)."

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Plaintiff's Actual Loss (1 of 2)

- Profits that the plaintiff would have received but for the defendant's act of misappropriation (including lost sales on convoyed/ancillary products or services that would be sold together with the product or service using the trade secret)
- Plaintiff's increased costs caused by defendant's act of misappropriation
- Value of the trade secrets to the plaintiff as of the date of the misappropriation if they had been destroyed; otherwise their diminution

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Plaintiff's Actual Loss (2 of 2)

- Decline in the value of the plaintiff's business
- Plaintiff's costs of research and development of the trade secret
- Plaintiff's cost to restore the effects of the misappropriation of the trade secret
- Price erosion because the plaintiff had to lower prices to compete with the defendant's use or disclosure of the trade secret

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Unjust Enrichment (1 of 2)

- Defendant’s profits on sales attributable to use of the trade secrets through increased revenue
- Defendant’s saved research and development
- Defendant’s time savings and/or acceleration to market
- Defendant’s cost efficiencies and increased operating profits

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Unjust Enrichment (2 of 2)

- Defendant's risk reduction and increased business value from lower risk associated with future cash flow
- Value of the trade secrets taken by the defendant as of the date of the misappropriation

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Valuation of the Trade Secret (1 of 2)

- Cost approach. The general principle of the cost approach is that a prudent investor would pay no more for a trade secret than the cost necessary to replace and/or protect the trade secret. The value of the trade secret is determined by aggregating the costs (direct, indirect, developer's profit, and entrepreneurial incentive) involved in its development.
- Market approach. The market approach is based on an analysis of trade secret acquisition transactions (sales comparison method) or trade secret licenses (relief from royalty method) to value the subject trade secret(s).

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Valuation of the Trade Secret (2 of 2)

- Income approach. The income approach is used to estimate a value of a trade secret if the trade secret produces any measure of either operating income or license income.
- There are three primary components of an income approach (1) projected amount of income attributable to trade secret; (2) duration of the income projection period – remaining useful life of the trade secret; and (3) income capitalization rate (discount rate minus growth rate)

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Reasonable Royalty

- Reasonable royalty = royalty base x royalty rate
- A reasonably royalty can generally be based on a percentage of gross revenue, percentage of net revenue, percentage of cost savings, percentage of profits, per unit, lump sum, or some other basis agreed to by the parties
- Calculate a royalty rate paid by a third-party licensee to a third-party licensor

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Methods Used to Calculate Reasonable Royalty Rate

- Comparable uncontrolled transaction method (market approach)
- Incremental profit method (income approach)
- Differential income method (income approach)
- Comparable profit margin method (income approach)

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Comparable Uncontrolled Transaction Method

- This analysis compares the intangible asset to third-party comparable uncontrolled transaction involving the license of similar intangible assets.
- This market-derived, third-party license royalty rate analysis considers factors such as:
  1. The relevant time period of the third party licenses
  2. The financial condition of both licensor and licensee parties
  3. The exclusivity of the license
  4. Any relevant government regulations
  5. Any non-monetary compensation included in the license
  6. The remaining useful life of the licensed intangible asset

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Incremental Profit Method (1 of 2)

- Using a weighted average cost of capital analysis, the analyst compares the owner/operator to other companies in the marketplace that don’t own the intangible asset.
- The investment method considers the expected return (profits) from all of the company assets (including both tangible assets and intangible assets), including the infringed intangible asset.
- A weighted average return on assets (based on the returns of other companies) is applied to the assets of the alleged infringing company. This results in an estimate of the profits that the company would earn if it did not utilize the infringed intangible asset.

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Incremental Profit Method (2 of 2)

- This profits measure (in other words, as if no infringement event occurred) is then compared to the actual profits of the infringing company. This comparison results in a measure of the incremental profits from the alleged infringement.
- This measure of infringement-related incremental profits can then be used to estimate a reasonable royalty rate.

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Differential Income Method

- The analyst uses a discounted cash flow analysis in which the analyst prepares two alternative cash flow projections.
- The first cash flow projection is prepared to reflect the owner/ operator’s prospective results of operations with the effects of the damages event.
- The second cash flow projection is prepared to reflect the owner/operator’s prospective results of operation without the effects of the damages event.
- The difference between these two analyses indicates the damages amount. The differential income (that is, the difference between the two cash flow analyses) is divided by the owner/operator’s annual revenue to estimate a reasonable royalty rate.

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Comparable Profit Margin Method

- Also known as the analytical method
- A reasonable royalty rate can be based on the expected (or historical) profit margin of the owner/operator company compared to a normal profit margin (based on guideline companies operating in the same or similar industry that do not use a comparative intangible asset).