

## **“Navigating the Challenges in Measuring Damages in Misappropriation of Trade Secrets Matters”**

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October 8, 2018

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## **Abstract**

The purpose of this discussion is to understand unique considerations when estimating damages in misappropriation of trade secrets cases. There has been a significant increase in the number of trade secrets cases filed in the U.S. This discussion includes an analysis of plaintiff's damages remedies in trade secret cases, including plaintiff's actual loss, defendant's unjust enrichment, valuation of trade secrets, and reasonable royalty, and defendant's rebuttal strategies for reducing and/or eliminating plaintiff's damages. Some of the critical issues facing damages experts in misappropriation of trade secrets legal include quantifying future damages, analyzing the impact of apportionment, estimating reasonable royalty, time-frame for measuring damages, allocation of expenses in quantifying defendant's profits, double-counting, and valuation of early-stage trade secrets.

## **Introduction**

Trade secrets litigation is on the rise particularly due to an increase in the unauthorized use of electronic information through mobile devices and data storage from corporate insiders or partners (employees, management, board of directors, consultants, independent contractors, suppliers/vendors), competitors, and perpetrators of cyber espionage/data theft (hackers, organized criminals, foreign governments).<sup>i,ii</sup>

Calculating damages in a misappropriation of trade secrets matters can be a complex exercise due to the varying federal and state laws that apply to these cases encompassing employment, intellectual property, tort, contract, and white-collar criminal law. Both the DTSA and the states adopting elements of the Uniform Trade Secrets Act ("UTSA") allow for multiple types of damages that are based on different calculations and permits recovery based on several types of remedies.<sup>iii, iv</sup> Many of these cases also have numerous legal claims besides misappropriation of trade secrets claims, which include unjust enrichment, Computer Fraud and Abuse Act ("CFAA"), Stored Communications Act ("SCA"), unfair competition, conversion, breach of contract (confidentiality/non-disclosure agreement), tortious interference, breach of fiduciary duty, copyright infringement, patent infringement, whistleblower, etc.

An important case regarding damages for misappropriation of trade secrets, *University Computing Co. v. Lykes-Youngstown Corp.*, 504 F.2d 518 (5<sup>th</sup> Cir. 1974) "stressed that 'each case is controlled by its own peculiar facts and circumstances,' and that courts should remain '**flexible and imaginative**'" [emphasis added] when estimating the plaintiff's proper damages.<sup>v</sup>

A 2016 report issued by the U.S. Chamber of Commerce states that "publicly traded U.S. companies own an estimated \$5 trillion worth of trade secrets."<sup>vi</sup> Prior to the enactment of the DTSA, misappropriation of trade secrets cases were generally brought in state court and appealed via local circuits to the U.S. Supreme Court. U.S. litigation statistics show a large increase in cases of misappropriation of trade secrets: the number of such cases doubled between 1988 and 1995; doubled again from 1995 to 2004; and is expected to double again by 2017.<sup>vii</sup> According to the Federal Bureau of Investigation ("FBI"), the number of economic espionage and theft of trade secrets cases handled by its Counterintelligence Division increased by 60 percent from fiscal year 2009 to the end of fiscal year 2013.<sup>viii</sup>

## NAVIGATING THE CHALLENGES IN MEASURING DAMAGES IN MISAPPROPRIATION OF TRADE SECRETS MATTERS

According to Lex Machina’s Trade Secrets Litigation Report 2018, the number of trade secrets cases filed in federal district court were at a consistent level of approximately 900 cases per year until 2017, when the number of trade secrets filings increased by 30 percent to 1,134.<sup>ix</sup>

According to a study by PwC and the Center for Responsible Enterprise and Trade (“CREATe.org”), the impact of trade secrets misappropriation and economic espionage in the U.S. has been estimated to be between approximately \$180 billion and \$540 billion, which represents between 1 and 3 percent of the U.S. gross domestic product.<sup>x</sup> Factors behind the increase in the trade secrets litigation include (1) digital technology and sharing of information; (2) a mobile workforce; (3) the rising value of intellectual property – which include trade secrets; (4) the adoption of the DTSA and the UTSA; (5) the flexible definition and characteristics of trade secrets; (6) increase in international threats and outsourcing to foreign companies; (7) organized crime; and (8) weakened patent protection laws.<sup>xi</sup>

There is also expected to be an increase in international trade secrets litigation due to the adoption of the Directive on the Protection of Trade Secrets (the “Directive”) by the European Union in 2016.<sup>xii</sup> It is expected that EU member states will start implementing the Directive in 2018.<sup>xiii</sup>

Below is a list of the top fifteen (15) disclosed settlements of litigation matters involving trade secrets’ legal claims:<sup>xiv</sup>

Rank	Amount	Settlement Payee	Case Name
#1	\$1.1 billion (VW agreed to pay \$100 million and buy at least \$1 billion of auto parts from GM)	General Motors Corp	<i>General Motors Corp. v. Lopez de Arriortua</i> , 2:96-cv-71038-NGE, E.D. Mich. (January 1997)
#2	\$400 million paid by IBM to settle trade secret and antitrust claims (IBM agreed to license \$140 million in Compuware software and buy \$260 million in Compuware services)	Compuware Corp.	<i>Compuware Corp. v. IBM Corp.</i> , 2:02-cv-70906-GCS, E.D. Mich. (March 2005)

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#3	\$340 million paid by AT&T to settle trade secret, patent and bankruptcy claims relating to the failed “At Home” broadband business Multiple actions settled (May 2005)	Bondholders’ Liquidating Trust	Multiple actions settled (May 2005)
#4	\$290 million paid by Semiconductor Manufacturing International Corp. (“SMIC”) to settle trade secret, patent and breach of contract claims stemming from the 2005 settlement (see No. 8)	Taiwan Semiconductor Manufacturing Company (“TSMC”)	Multiple actions in California Superior Court and China settled (November 2009)
#5	\$288 million paid by Toshiba Corp. in 2006 to settle legal claims including misappropriation of trade secrets and infringement of patents pertaining to Lexar’s NAND flash-memory chips technology in the U.S. Original jury award was for \$465.4 million.	Toshiba Corp.	<i>Lexar Media, Inc. v. Toshiba Corp.</i> , CV-812458, California Superior Court, Santa Clara County (2005)
#6	\$275 million paid by Kolon Industries Inc. to DuPont Co. that included upfront and ongoing payments for trade secrets case involving fiber used to manufacture bulletproof vests and an \$85 million in criminal fines. The jury award was \$919 million <sup>xv</sup>	E.I. du Pont de Nemours	<i>E.I. du Pont de Nemours &amp; Co. v. Kolon Industries, Inc.</i> , 3:09-cv-00058, U.S. District Court, Eastern District of Virginia (Sept. 2011) – settled in April 2015
#7	\$245 million in Uber stock transferred to Waymo LLC and return of technology to Waymo LLC	Waymo LLC	<i>Waymo LLC, v. Uber Technologies, Inc.; Ottomotto LLC, and Otto Trucking LLC</i> (February 2018)

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#8	\$175 million paid by SMIC to settle trade secret and patent claims	TSMC	Multiple actions in U.S. District Court, California Superior Court, ITC, and Taiwan District Court settled (January 2005)
#9	\$130 million paid by Zillow for theft of trade secrets and confidential information regarding merger and new product plans	Move and National Association of Realtors	<i>Move and National Association of Realtors v. Zillow</i> , King County Superior Court, Washington (June 2016)
#10	\$75 million paid by Hilton to settle trade secret, fraud, unfair competition, conversion, and multiple other claims	Starwood Hotels	<i>Starwood Hotels &amp; Resorts Worldwide v. Hilton Hotels Corp.</i> , 09-cv-03862, S.D.N.Y. (December 2010)
#11	\$75 million paid by A10 in trade secret, patent and copyright action. The original jury award was \$112 million.	Brocade Communications Systems	<i>Brocade Communications Sys. Inc. v. A10 Networks Inc.</i> , 5:10-cv-03428, N.D. Cal. (August 2012)
#12	\$65 million cash paid by Alynham Pharmaceuticals, plus \$10 million promised in milestone payments, plus transfer of 150 patents and patent applications to Tekmira, plus royalty streams in future products	Tekmira Pharmaceuticals Corp.	<i>Tekmira Pharms. Corp. et al. v. Alynham Pharms. Inc., et al.</i> , 11-1010-BLS2, Business Litigation Session of the Massachusetts Superior Court (November 2012)
#13	\$61 million paid by Morningstar, Inc.	Business Logic	<i>Business Logic Holdings v. Ibbotson Associates</i> , 2009-CH-46687, Illinois Circuit Court, Cook County Law Division (July 2014)
#14	\$56 million paid by International Flavors & Fragrances	ZoomEssence, Inc.	<i>ZoomEssence, Inc. v. International Flavors &amp; Fragrances</i> , U.S. District Court of New Jersey (June 2017)

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#15	\$44.5 million paid by Grumman Systems Support Corp. in trade secret and copyright action	Data General Corp.	<i>Data General Corp. v. Grumman Data Systems, Inc.</i> , 4:93-cv-40087-NMG, D. Mass. (October 1995)
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This discussion will include the following sections:

- Definition of trade secret
- Definition of misappropriation
- Plaintiff’s remedies in misappropriation of trade secrets matters
- Plaintiff’s actual loss – making the plaintiff “whole”
- Defendant’s unjust enrichment – measuring the financial gain realized by the defendant
- Fair market value of trade secrets
- Reasonable royalty
- Defendant’s rebuttal strategies for damages calculations
- Observations from *Waymo v. Uber* and dealing with challenging cases when the technology has significant value at an early stage of development
- Trade secrets case law

### **Definition of Trade Secret**

The three most commonly used definitions of trade secrets are from the (1) DTSA; (2) UTSA and (3) U.S. Economic Espionage Act (“EEA”).

According to 18 U.S. Code §1839(3) of the DTSA, the term “trade secrets” is defined to be “all forms and types of financial, business, scientific, technical, economic, or engineering information, including patterns, plans, compilations, program devices, formulas, designs, prototypes, methods, techniques, processes, procedures, programs, or codes, whether tangible or intangible, and whether or how stored, compiled, or memorialized physically, electronically, graphically, photographically, or in writing if—

- (A) the owner thereof has taken reasonable measures to keep such information secret; and
- (B) the information derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable through proper means by, another person who can obtain economic value from the disclosure or the use of the information.”<sup>xvi</sup>

According to §1.4 of the UTSA, 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.”<sup>xvii</sup>

Some form of the UTSA has been formally enacted by 47 states and the District of Columbia, Puerto Rico, and the U.S. Virgin Islands. It is important to note that there are variations and

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significant differences among the states that have adopted UTSA.<sup>xviii</sup> The three state exceptions on the UTSA include New York and Massachusetts, and North Carolina.<sup>xix,xx</sup>

- New York generally follows the Restatement (Third) of Unfair Competition.
- Massachusetts' trade secret law is based on a combination of statutory law and common law principles; however, Massachusetts has recently adopted a version of the UTSA that will become law effective as of October 1, 2018.
- North Carolina has adopted a state statute, which codifies several of the key principles of the UTSA. North Carolina did not formally adopt the UTSA.<sup>xxi</sup>

Even though 47 states have adopted some form of the UTSA, there are significant differences in the state statutes for items such as the definition of a trade secret, definition of misappropriation, definition of improper, exemplary damages, awarding of attorneys' fees (non-uniform tests for bad faith), statutes of limitations, definition of a person, differences in damages measured by a reasonable royalty, adoption of inevitable disclosure doctrine, and so on. Additionally, some states did not enact all provisions of the UTSA and some states enacted unique statutory provisions.<sup>xxii</sup>

The EEA of 1996 is a federal criminal statute. According to §1839 of the EEA, a trade secret “means all forms and types of financial, business, scientific, technical, economic, or engineering information, including patterns, plans, compilations, program devices, formulas, designs, prototypes, methods, techniques, processes, procedures, programs, or codes, whether tangible or intangible, and whether or how stored, compiled, or memorialized physically, electronically, graphically, photographically, or in writing if—

- (A) the owner thereof has taken reasonable measures to keep such information secret; and
- (B) the information derives independent economic value, actual or potential, from not being general known to, and not being readily ascertainable through proper means by, the public.”<sup>xxiii</sup>

According to §757 of the New York First Restatement of Torts, certain factors are “to be considered in determining whether given information is one’s trade secrets are:

1. the extent to which the information is known outside of the business;
2. the extent to which it is known by employees and others involved in the business;
3. the extent of measures taken to guard the secrecy of the information;
4. the value of the information to the owner and its competitors;
5. the amount of effort or money expended on developing the information; and
6. the ease or difficulty with which the information could be properly acquired or duplicated by others.”<sup>xxiv</sup>

Trade secrets are not registered and/or identified with any government agency. Some examples of trade secrets include:

- Recipes (example – the formula for Coco-Cola soft drinks)
- Manufacturing processes
- Engineering drawings/blueprints/notebooks
- Algorithms (example – Google’s search algorithm)
- Measurements
- Test results
- New ideas
- Tools
- Negative information on unsuccessful experiments



- Databases/data compilations/data files
- Customer information
- Supplier information
- Pricing information
- Profit margin information
- Sensitive financial information
- IT systems and applications
- Strategic business plans/marketing plans, materials, and analyses
- Updates to existing products
- Surveys (example – *The New York Time's* Best-Seller List)
- Source code
- Virtual assets
- Other confidential and proprietary business information and know-how

## **Definition of Misappropriation**

The DTSA defines misappropriation as:<sup>xxv</sup>

- (A) “acquisition of a trade secret of another by a person who knows or has reason to know that the trade secret was acquired by improper means;
- (B) disclosure or use of a trade secret of another without express or implied consent by a person who—
  - (i) used improper means to acquire knowledge of the trade secret;
  - (ii) at the time of disclosure or use, knew or had reason to know that the knowledge of the trade secret was—
    - (I) derived from or through a person who had used improper means to acquire the trade secret;
    - (II) acquired under circumstances giving rise to a duty to maintain the secrecy of the trade secret or limit the use of the trade secret; or
    - (III) derived from or through a person who owed a duty to the person seeking relief to maintain the secrecy of the trade secret or limit the use of the trade secret; or
  - (iii) before a material change of the position of the person, knew or had reason to know that—
    - (I) the trade secret was a trade secret; and
    - (II) knowledge of the trade secret had been acquired by accident or mistake.”

Misappropriation is defined by the UTSA as:

- (i) “acquisition of a trade secret of another by a person who knows or has reason to know that the trade secret was acquired by improper means; or
- (ii) disclosure or use of a trade secret of another without express or implied consent by a person who
  - (A) used improper means to acquire knowledge of the trade secret; or
  - (B) at the time of disclosure or use, knew or had reason to know that his knowledge of the trade secret was
    - (I) derived from or through a person who had utilized improper means to acquire it;
    - (II) acquired under circumstances giving rise to a duty to maintain its secrecy or limit its use; or
    - (III) derived from or through a person who owed a duty to the person seeking relief to maintain its secrecy or limit its use; or

(C) before a material change of his [or her] position, knew or had reason to know that it was a trade secret and that knowledge of it had been acquired by accident or mistake.”<sup>xxvi</sup>

The UTSA states “For liability to exist under this Act, a Section 1(4) trade secret must exist and either a person’s acquisition of the trade secret, disclosure of the trade secret to others, or use of the trade secret must be improper under Section 1(2).”<sup>xxvii</sup>

The DTSA states that the term “improper means” –

- (A) “includes theft, bribery, misrepresentation, breach or inducement of a duty to maintain secrecy, or espionage through electronic or other means; and
- (B) does not include reverse engineering, independent derivation, or any other lawful means of acquisition.”<sup>xxviii</sup>

## **Plaintiff’s Remedies in Misappropriation of Trade Secrets Matters**

The remedies available to a plaintiff include equitable relief (preliminary injunction or permanent injunction), monetary damages (compensatory, unjust enrichment, or restitution damages), and legal fees.

According to §1836 3(b)(i) of the DTSA, states that “awards for damages include (I) damages for actual loss caused by the misappropriation of the trade secret; and (II) damages for any unjust enrichment caused by the misappropriation of the trade secret that is not address in computing damages for actual loss; or . . . (ii) in lieu of damages measured by any other methods, the damages caused by the misappropriation measured by imposition of liability for a reasonable royalty for the misappropriator’s unauthorized disclosure or use of the trade secret.”<sup>xxix</sup>

According to §2(a) of the UTSA, “Actual or threatened misappropriation may be enjoined. Upon application to the court, an injunction shall be terminated when the trade secret has ceased to exist, but the injunction may be continued for an additional reasonable period of time in order to eliminate commercial advantage that otherwise would be derived from the misappropriation.”<sup>xxx</sup>

The UTSA further states that “an injunction should last for as long as is necessary, but no longer than is necessary, to eliminate the commercial advantage or ‘lead time’ with respect to good faith competitors that a person has obtained through misappropriation. Subject to any additional period of restraint necessary to negate lead time, an injunction accordingly should terminate when a former trade secret becomes either generally known to good faith competitors or generally knowable to them because of the lawful availability of products that can be reversed engineered to reveal a trade secret.”<sup>xxxi</sup>

According to §2(b) of the UTSA, “In exceptional circumstances, an injunction may condition future use upon payment of a reasonable royalty for no longer than the period of time for which use could have been prohibited. Exceptional circumstances include, but are not limited to, a material and prejudicial change of position prior to acquiring knowledge or reason to know of misappropriation that renders a prohibited injection inequitable.”<sup>xxxii</sup>

According to §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 of use of trade secret."<sup>xxxiii</sup>

The UTSA states that the "reasonable royalty alternative measure of damages for a misappropriator's past conduct under Section 3(a) is readily distinguishable from a Section 2(b) royalty order injunction, which conditions a misappropriator's future ability to use a trade secret upon payment of a reasonable royalty. A Section 2(b) royalty order injunction is appropriate only in exceptional circumstances; whereas a reasonable royalty measure of damages is a general option. Because Section 3(a) damages are awarded for a misappropriator's past conduct and a Section 2(b) royalty order injunction regulates a misappropriator's future conduct, both remedies cannot be awarded for the same conduct. If a royalty order injunction is appropriate because of a person's material and prejudicial change of position prior to having reason to know that a trade secret has been acquired from a misappropriator, damages, moreover, should not be awarded for past conduct that occurred prior to notice that a misappropriated trade secret has been acquired."<sup>xxxiv</sup>

According to §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)."<sup>xxxv</sup> The DTSA has essentially this same provision for exemplary damages, §1836 3(c).<sup>xxxvi</sup>

According to §4 of the UTSA, "If (i) a claim of misappropriation is made in bath faith, (ii) a motion to terminate an injunction is made or resisted in bad faith, or (iii) willful and malicious misappropriation exists, the court may award reasonable attorney's fees to the prevailing party."<sup>xxxvii</sup>

According to §6 of the UTSA, "An action for misappropriation must be brought within 3 years after the misappropriation is discovered or by the exercise of reasonable diligence should have been discovered."<sup>xxxviii</sup>

Some examples of differences regarding remedies among states include:

- Alabama Code Section 8-27-4 states that "Recovery of any profits and other benefits conferred by the misappropriation that are attributable to the misappropriation (in establishing the misappropriator's profits, the complainant is required to present proof only of the misappropriator's gross revenue, and the misappropriator is required to present proof of his or her deductible expenses and the elements of profit attributable to factors other than the trade secret., and . . . the actual damages suffered as a result of the misappropriation."<sup>xxxix</sup>
- The New York Court of Appeals in *E.J. Brooks Co. v. Cambridge Security Seals*, 2018 N.Y. Lexis 1080 (N.Y. Ct. App., May 3, 2018) did not allow recovery of damages as "measured by the costs the defendant avoided due to its unlawful activity." The plaintiff attempted to quantify its damages based on the costs the defendant had avoided when it misappropriated the trade secret. The decision was due to premise that the New York common law is based on "compensatory" damages, which is based on the plaintiff's actual loss instead of unjust enrichment.<sup>xl</sup>
- California Uniform Trade Secrets Act Code Section 3426.3(b) states that "If neither damages nor unjust enrichment caused by misappropriation are provable, the court may

order payment of a reasonable royalty for no longer than the period of time the use could have been prohibited.”<sup>xli</sup>

The SCA relates to unlawful access to stored communication, which include:

1. “Intentionally access without authorization a facility through which an electronic communication services is provided; or
2. Intentionally exceeds an authorization to access facility; and thereby obtains, alters, or prevents authorized access to a wire or electronic communication while it is electronic storage in such system shall be punished.”<sup>xlii</sup>

The damages provision for the SCA states, “The court may assess as damages in a civil action under this section the sum of the actual damages suffered by the plaintiff and any profits made by the violator as a result of the violation, but in no case shall a person entitled to recover receive less than the sum of \$1,000. If the violation is willful or intentional, the court may assess punitive damages. In the case of a successful action to enforce liability under this section, the court may assess the costs of the action, together with reasonable attorney fees determined by the court.”<sup>xliii</sup>

The CFAA relates to fraud and related activity in connection with computers, which includes intentionally accessing a computer without authorization or exceeds authorized access.<sup>xliii</sup> The CFAA does not require that the information taken to be a “trade secret” or actually used or misappropriated by the defendant.

The CFAA has different definitions for loss and damage. The CFAA defines the term “loss” to mean any “reasonable cost to any victim, including the cost of responding to an offense, conducting a damage assessment, and restoring the data, program, system, or information to its condition prior to the offense, and any revenue lost, cost incurred, or other consequential damages incurred because of interruption of service.”<sup>xliii</sup> Neither loss of goodwill nor loss of business opportunities and revenues resulting from the use of improperly acquired information constitute “loss” as contemplated by the CFAA. The CFAA defines the term “damage” to mean any “impairment to the integrity or availability of data, a program, a system, or information.”<sup>xliii</sup>

The EEA is a federal statute for criminal prosecution of theft of trade secrets. The primary objectives of the EEA are to protect national and economic security. According to §1831 of the EEA, an individual can be sentenced to prison for up to 15 years and receive criminal fine up to \$5,000,000 and any organization that commits economic espionage will be fined the greater of \$10,000,000 or 3 times the value of the stole trade secret to the organization for economic espionage. The penalties for commercial trade secret theft include an individual can be sentenced to prison for up to 10 years and an organization can receive a fine up to \$5 million.<sup>xliii</sup>

According to Lex Machina Trade Secret Litigation Report 2018, there were 157 trade secret cases in 2017 that resulted in damages awards: Some notable damages were noted:<sup>xliii</sup>

- 103 cases included element for actual damages or lost profits (65.6%)
- 47 cases included element for punitive damages (29.9%)
- 7 cases included element for reasonable royalty (4.5%)

The Supreme Court of Texas in *Southwest Energy Product Company v. Toby Berry-Helfand and Gery Muncey*, No. 13-0986, Oct. 2015, stated that “Damages in misappropriation cases therefore

can take several different forms including the value of the plaintiff's lost profits, the defendant's actual profits from the use of the secret, the value a reasonable prudent investor would have paid for the trade secret, the development costs the defendant avoided by the misappropriation, and a reasonable royalty."<sup>xlix</sup>

It is generally recommended that damages be measured on an individual trade secret basis and to disaggregate damages among trade secrets or other legal claims. It is not a requirement that a damages expert disaggregate among trade secrets; however, if the court awards damages for only some of the trade secrets instead of all of the trade secrets, this could present a problem if the damages were not disaggregated among the various trade secrets.

### **Plaintiff's Actual Loss – Making the Plaintiff “Whole”**

A common goal when estimating plaintiff's actual loss damages in a trade secrets litigation matters is to attempt to the make the plaintiff “whole” after experiencing the alleged damages event, which may include:

- 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
- 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/remedy 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 of the trade secret

The Delaware Chancery court stated in *Agilent Technologies v. Kirkland*, 3512-VCS (Del. Ch. 2-18-2010), that “Compensatory damages in actions for trade secret misappropriation, and in analogous patent infringement cases, are generally determined by ‘the difference between the plaintiff's position before and after the misappropriation of his secret. The loss suffered by the plaintiff, such as lost profits, is the usual indicator of damages. . . .”<sup>i</sup>

The AICPA Guide to Intangible Asset Valuation states that “Compensatory damages are also called actual damages. This is the amount of compensation that is necessary to restore the injured party to the economic condition he or she was in before the damages event. If the claimant [plaintiff] receives an award of the compensatory damages, then the claimant should be made whole from the effects of the wrongful act.”<sup>ii</sup>

#### **Plaintiff's Lost Profits**

The plaintiff's lost profits are calculated first by determining lost revenue and then deducting the incremental costs that would have been incurred in producing the lost revenue. The American Institute of Certified Public Accountants (AICPA) Practice Aid 06-4, titled “Calculating Lost Profits,” states “Lost ‘net’ profit is computed, in general, by estimating the gross revenue<sup>iii</sup> that would have been earned but for the wrongful act reduced by avoided costs. Avoided costs are defined as

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those incremental costs (or saved expenses) that were not incurred because of the loss of the revenue.”<sup>iii</sup>

The following methods are generally used to calculate lost revenue:

- The before and after method – the damages expert compares the before results of operations to the after results of operations
- The yardstick (or benchmark) method – the damages expert calculates the plaintiff’s revenue using a “yardstick” to compare the subject business to other similar businesses, industry averages or other relevant guidelines
- The but for (or sales projection) method – the damages expert calculates the plaintiff’s expected revenue without the alleged misappropriation of trade secrets to actual revenue after the harmful event
- An approach based on the terms of the underlying agreement (confidentiality agreement, non-compete agreement, non-disclosure agreement, etc.)

The lost revenue is generally calculated from these models by taking the projected “but for” revenue, minus the plaintiff’s actual revenue during the loss period.

The U.S. District Court of Central District of California stated in *Beiner Enterprises, Inc. v. Adam Caldwell, Inc., et al.*, CV13-08723-AB, that “In the context of this case, a lost profits calculation is the most appropriate measure of damages. Lost profits must be determined to a reasonable certainty as the amount ACI would have earned but for BEI’s breach, minus saved expenses.”<sup>iv</sup>

The AICPA Lost Profits Practice Aid 06-4 states the following with regard to the before and after method:<sup>lv</sup>

- “This method compares the plaintiff’s performance before the event or action causing lost profits to the plaintiff’s performance after that event or action.”
- “The plaintiff’s prior experience, which can be determined from the plaintiff’s historical accounting records, is generally subject to dispute less than other components of the calculation. In addition, the plaintiff’s experience subsequent to the to the defendant’s act can be determined, at least up through a date near to the date at which the calculation is made, from the plaintiff’s historical accounting records.
- “The practitioner, however, should consider other factors [such as seasonality, unusual/non-recurring factors, capacity considerations, market share, etc.] that could have affected the plaintiff’s level of revenues and demonstrate how those factors have been taken into consideration.”

The AICPA Lost Profits Practice Aid 06-4 states the following with regard to the yardstick method:<sup>lvi</sup>

- “This method utilizes a ‘yardstick’ that is used to estimate what the revenues and profits of the affected business would have been. Examples of possible yardsticks that might be employed in the calculation include the following:
  - The performance of the plaintiff at a different location
  - The plaintiff’s actual experience versus past budgeted results
  - The actual experience of a similar business unaffected by the defendant’s actions
  - Comparable experience and projections by nonparties
  - Industry averages
  - Pre-litigation projections”
- “When using this method, the practitioner will need to demonstrate the plaintiff’s operations are sufficiently comparable to the ‘yardstick’ used. This could require that the yardstick company be in the same geographic area and/or operates under similar conditions.”
- “In addition, as with the ‘before and after’ method, the practitioner may need to consider other factors that could have caused the plaintiff’s performance to differ from the yardstick selected and show how those factors have been taken into consideration.”

The underlying theory of lost profits damages calculated using the “but for” method is that “but for” for the defendant’s misappropriation of trade secrets, the plaintiff would have received a higher level of revenue and profits. The “but for” method may consider the following:<sup>lvii</sup>

- Company financial projections/budgets/forecasts prepared prior to the harmful event
- Establishing support for the underlying foundation for the company financial projections/budgets/forecasts prepared prior to the harmful event
- The plaintiff’s market share it would have attained but for the misappropriation of trade secrets (estimating revenue based on market trends)
- Economic modeling
- Impact of changes in price and volume

The AICPA Lost Profits Practice Aid 06-4 states the following with regard to calculation based on the terms of the contract: “In some instances, the lost profits calculation is made in relation to a specific contract. In that instance, many of the elements of the calculation may be set forth in the contract document, i.e., the number of units to be sold, unit prices, etc. In this situation, a model might be developed that calculates the revenues anticipated under the terms of the contract.”<sup>lviii</sup>

After determining the amount of lost revenue, the damages expert will need to calculate the costs associated with the generation of lost revenue. In calculating plaintiff’s lost profits, profits are generally measured on a contribution margin basis, which is generally measured as lost revenue minus incremental costs. The AICPA Lost Profits Practice Aid 06-4 states that, “The costs that should be deducted from lost revenues in order to calculate lost profits are generally referred to as avoided costs. *Avoided costs* are those costs that would have been incurred in connection with the generation of the lost revenues but were not incurred.”<sup>lix</sup> Incremental costs are the costs associated with producing the additional number of the ‘but for’ sales volume level.

The damages expert can use several methods of cost estimation in his/her analysis of the incremental costs that should be deducted from lost revenue. Some of the key considerations include:<sup>lx</sup>

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- Analysis of cost structure for cost of goods sold and operating expenses (direct costs and indirect costs) in the determination of fixed versus variable (costs may be fixed, variable, or semivariable)
- Use of nonstatistical methods of cost estimation (account analysis, direct assignment, accounting estimates, cost accounting allocations, ratio analysis, graphical approaches, industrial engineering, etc.) or statistical methods of cost estimation (such as regression analysis, attribute sampling, survey data, etc.)

The AICPA Guide to Intangible Asset Valuation states that, “Incremental expenses should represent only those expenses that were not incurred because the lost revenue was not realized. The most obvious example of an incremental expense is direct production costs. Other examples of incremental expenses that may be deducted from the lost revenue estimate include selling expenses, the variable component of overhead expenses, marketing expenses, advertising expenses, and any royalties that would have been paid on foregone production.”<sup>lxix</sup>

Historical and future lost profits may be calculated in misappropriation of trade secrets matters,<sup>lxxii</sup> however, it is important for the plaintiff’s attorney and damages experts to review the relevant state’s statutes and substantive case law for situations in which the damages expert is calculating future lost profits. It is also important for the damages expert to consider the portion of profits attributable to the trade secret(s).

The plaintiff is generally only entitled to lost profits which are attributable to the subject trade secrets. Thus, in situations involving complex technology, a damages analysis may need to include an apportionment analysis. One of the key considerations is whether the misappropriated trade secret features drive the demand for the product.

Courts struggle with measuring the value reflected by discrete misappropriated trade secret features with multi-feature products. There is currently no generally accepted apportionment methodology. Some of the different apportionment methodologies include:

- Consumer surveys
- Usage surveys
- Market studies
- Conjoint analysis
- Product comparison (with and without the misappropriated trade secret feature)
- Relative value (based on economic contributions, costs, or price)
- Cost analysis
- Feature counting and isolation of the infringing and non-infringing elements

The apportionment process is evolving and still faces many uncertainties. Due to complexity of issues, standardization will take many years.

A risk-adjusted discount rate is applied to the plaintiff’s future lost profits. The discount rate includes a component for the time value of money (inflation) and risk inherent in future lost profits. The future lost profits are generally discounted back to the date of the misappropriation of trade secrets or the current date (such as date of report or trial).<sup>lxxiii</sup> The discount rate should include an analysis of the risk of the misappropriated trade secret(s).



There are some states that limit the loss period to a “head-start” period. There are also situations in which a court may award the monetary damages to compensation for the defendant’s past use of the trade secret in addition to a permanent injunction to prevent the defendant’s future use of the trade secret. Both an award of future lost profits and permanent injunction may be considered an impermissible double recovery.<sup>lxiv</sup>

### Fair Market Value of the Plaintiff’s Trade Secret(s)

According to an article published in *Inside Counsel*, “Where the market is damaged due to defendant’s disclosure of the trade secret, the plaintiff may also recover certain provable future profits based on historical data or the fair market value of the trade secret if the defendant had disclosed the trade secret publicly.”<sup>lxv</sup>

The valuation analysis should generally be calculated for each individual trade secret identified within the lawsuit.

The U.S. Court of Appeals for the Fifth Circuit in *Precision Planting & Metal Finishing Inc., et al. v. Martin-Marietta Corporation*, 435 F.2d 1262 (Fifth Cir. 1970), stated that the trial court undertook a process to analyze the fair market value of the trade secret, “There is no established market value in the present case in the sense that there were a number of transactions of the same or similar article, the consensus of which reflects the price at which willing buyers and sellers would act. Fair market value here is synonymous with the investment value of the trade secret; that is, what an investor judges he should pay for the return he foresees by virtue of owning the process, taking into account the facts, circumstances and information which is available at the time.”<sup>lxvi</sup>

The U.S. District Court in Minnesota in *Cardiovention, Inc. v. Medtronic, Inc.*, 483 F. Supp. 23 830 (2007), stated that, “Courts have recognized that a plaintiff’s actual damages can be measured by the value of the loss of the secret to the plaintiff under the circumstances.”<sup>lxvii</sup>

The compensatory damages in the trade secrets matter of *Wellogix, Inc. v. Accenture, L.L.P.*, (U.S. Court of Appeals, No. 11-201816) were estimated based on the lost business value due to the misappropriation of trade secrets. The plaintiff’s damages expert used a market approach to value the company based on prior transaction of a venture capital group’s 31-percent equity interest in the plaintiff near the date of the misappropriation.<sup>lxviii</sup>

In situations in which a plaintiff’s damages expert has estimated the damages based on entire fair market value of a company, this method is generally more appropriate when the entire value of the company is based on the misappropriated trade secret.

Please see the separate section on estimating the fair market value of trade secrets.

## **Unjust Enrichment – Measuring the Financial Gain(s) Realized by the Defendant**

In misappropriation of trade secrets cases, unjust enrichment generally “requires a showing that a plaintiff conferred a benefit on a defendant that the defendant knew about and that allowing the defendant to retain the benefit without payment would be unjust.”<sup>lxix</sup>

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The goal of calculating unjust enrichment in trade secrets litigation matters is to attempt to eliminate the benefit of the unlawful misappropriation of the ill-gotten benefits, profits, or advantages acquired by the defendant, which may include:<sup>lxx</sup>

- 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 (head-start damages)
- Defendant's cost efficiencies and increased operating profits
- Defendant's risk reduction and increased business value from lower risk associated with future cash flows
- Value of the alleged trade secrets taken by the Defendant as of the date of the misappropriation (defendant should have to pay for what was wrongfully taken by the defendant)

The Supreme Court of Texas in *Southwest Energy Product Company v. Toby Berry-Helfand and Gery Muncey*, No. 13-0986, Oct. 2015, stated that "Value to the defendant may be measured by the defendant's actual profits resulting from the use or disclosure of the trade secret (unjust enrichment), the value a reasonably prudent investor would have paid for the trade secret, or development costs that were saved."<sup>lxxi</sup>

The U.S. District Court in Minnesota in *Cardiovention, Inc. v. Medtronic, Inc.*, 483 F. Supp. 23 830 (2007), stated that, "Although unjust enrichment is typically measured by profits gained from the sale of the product containing the trade secret, courts have considered costs savings and increased productivity resulting from the use of the trade secret."<sup>lxxii</sup>

AICPA Practice Aid 06-4, titled "Calculating Lost Profits, states that, "**In certain situations, such as cases involving unfair competition or the misappropriation of trade secrets, an accounting of the profits realized by the defendant may be used as the measure of the plaintiff's lost profits** [emphasis added]. In obtaining an accounting of the defendant's profits, the plaintiff is only entitled to receive value of the unjust enrichment of the defendant through disgorgement, i.e., the defendant is required to surrender profits attributable to the misappropriation or bad act to the plaintiff. To the extent that profits are attributable to other factors, the defendant would not have to disgorge those amounts. In some jurisdictions (and for some causes of action), the plaintiff only has the burden to identify the revenues associated whereas the defendant has the burden to prove both the costs incurred in generating the revenues as well as apportioning the profits between the misappropriation and other profit generators."<sup>lxxiii</sup>

A well-known authoritative book written by Dan Dobbs and Caprice Roberts, Law of Remedies – Damages-Equity-Restitution, Third Edition, states that the defendant's unjust enrichment benefits may be measured based on the following:

1. The increased assets in the hands of defendant from receipt of property.
2. The market value of services or intangibles provided to defendant, without regard to whether defendant's assets were actually increased; that is, the amount which it would cost to obtain similar services, whether these services prove to be useful or not.
3. The use value of any benefits received, as measured by (i) market indicators such as rental value or interest or (ii) actual gains to defendant from using the benefits, such as gains identified in item 5.
4. The gains realized by defendant upon sale or transfer of an asset received from plaintiff.

5. The collateral or secondary profits earned by defendant by use of an asset received from plaintiff, or, what is much the same thing, the savings effected by the use of the asset.<sup>lxxiv</sup>

The UTSA states that, “As long as there is no double counting, Section 3(a) adopts the principle of the recent cases allowing recovery of both a complainant’s actual losses and a misappropriator’s unjust benefit that are caused by misappropriation.”<sup>lxxv</sup> Thus, the damages expert cannot use the same lost sales for calculating plaintiff’s lost profits and unjust enrichment of defendant’s profits.

The plaintiff typically has the burden of proving the defendant’s revenue and then the defendant generally has the burden to prove deductions and offsets from revenue. Typically, the misappropriator will need to prove that the expense item was paid, and it was attributable to the sales using the misappropriated trade secrets. Certain allowable deductions may include cost of materials, services, and labor incurred in producing the goods or services; insurance premiums; building repairs; allocated percentages of overhead costs; and selling, marketing, and advertising costs.

There are some jurisdictional differences on which expenses can be deducted from revenue. It is important for the plaintiff’s attorney to review the relevant state’s statutes and substantive case law for situations in which the damages expert is calculating an accounting of the defendant’s profits to determine which expenses should be deducted from revenue.

In general, a plaintiff’s lost profits calculation subtracts incremental expenses from revenue; whereas, an accounting of the defendant’s profits may be calculated by either (1) subtracting incremental expenses from revenue; or (2) subtracting fully allocated expenses (incremental and fixed expenses) from revenue. For example, U.S. courts are split on the issue of overhead allocation in an accounting of the defendant’s profits for an unjust enrichment calculation.<sup>lxxvi, lxxvii</sup>

It is important for the plaintiff’s attorney to review the relevant state’s statutes and substantive case law for situations in which the damages expert is calculating future unjust enrichment for defendant’s profits. According to a recent Business Valuation Resources program titled “Measuring Unjust Enrichment,” this program stated that “Future unjust enrichment is becoming more common.”<sup>lxxviii</sup>

## **Fair Market Value of Trade Secrets**

In misappropriation of trade secret cases, the standard of value usually is a fair market value type standard based on what a reasonable investor would have paid for the trade secrets. Fair market value is defined by the American Society of Appraisers (“ASA”) Business Valuation Standards’ Glossary as “the price, expressed in terms of cash equivalents, at which property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arm’s length in an open and unrestricted market, when neither is under compulsion to buy or sell and when both have reasonable knowledge of the relevant facts.”<sup>lxxix</sup>

There are three generally accepted approaches to valuing trade secrets:

- **Cost approach.** The cost approach is based on the economic principle of substitution. 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 involved in its development.

- **Market approach.** The market approach is based on an analysis of trade secret acquisition transactions or trade secret licenses to value the subject trade secret(s).
- **Income approach.** The income approach is used to estimate the value of a trade secret if the trade secret produces any measure of either operating income or license income.

### Cost Approach

There are four general cost components that generally should be considered in the cost approach analysis to value a trade secret:

1. **Direct costs.** “Direct costs include material, labor, and overhead costs incurred directly by the intangible asset creator.”<sup>lxxx</sup>
2. **Indirect costs.** “Indirect costs may also include material, labor, and overhead costs. In this case, these costs are incurred directly by the creator. . . The indirect costs are, of course, ultimately paid by the intangible asset creator. These costs are paid to individuals and organizations that are outside of the inventor’s organization.”<sup>lxxxi</sup>
3. **Developer’s profit.** “First, from the perspective of the developer of any intangible asset, the developer expects a return of all of the direct and indirect costs (including material, labor, and overhead costs) related to the development process. Second, the developer expects a return on all of the direct and indirect costs (including material, labor, and overhead costs) related to the development process.”<sup>lxxxii</sup>
4. **Entrepreneurial incentive.** “The entrepreneurial incentive is the amount of economic benefit required to motivate the intangible asset creator to enter into the development process. From the perspective of the creator, entrepreneurial incentive is often perceived as an opportunity cost.”<sup>lxxxiii</sup>

The following is a list of items to consider when using a cost approach to value trade secrets:

- Cost approach is sometimes used in situations when the trade secret does not generate an income stream or there is no guideline trade secret acquisition transaction or license market data
- Reproduction cost is the level of expenditures needed to reproduce an exact replica of the asset
- Replacement cost is the level of expenditures necessary to develop an asset with similar utility
- Value = Replacement Cost New – Physical Deterioration – Economic Obsolescence – Curable Functional and Technologies Obsolescence
- The conclusion under the cost approach may not reflect the value of the trade secret to its owner
- The cost approach is sometimes used to calculate the floor value of the subject trade secret

### Market Approach

The most common methods to value trade secrets using a market approach include:

1. **Sale comparison method.** This method relies on guideline acquisition transaction data of trade secrets.

2. **Relief from royalty method.** This method relies on guideline license transaction data of trade secrets. The royalty rate is generally applied to the trade secret owner's revenue or financial metric to estimate the trade secret value. This method is considered a hybrid market and income approach. The hypothetical royalty payment should reflect the amount that an operator or licensee would be willing to pay in an arm's length transaction to a third-party owner or licensor in order to obtain the use of the trade secret. Other royalty considerations may include changes in parties' competitive positions, nature and extent of use by defendant, availability of alternative trade secrets, and so on.

A market approach is rarely used to value trade secrets because of very limited acquisition and license transactions and the difficulty of comparing one trade secret to another trade secret. Trade secrets by their very nature are unique and secret. It is important for the damages expert to adjust for differences in the trade secret transaction data and the subject trade secret.

It is very difficult to find a large data set of guideline licensing data to value trade secrets. Additionally, many times license agreements for trade secrets are bundled with patent license agreements or other intellectual property agreements. In situations involving bundled license agreements, the damages expert will generally need to apportion among the various elements of intellectual property included in the license agreement.

### Income Approach

There are three primary components of an income approach used to value a trade secret:

1. Projected amount of income attributable to trade secrets
2. Duration of the income projection period – remaining useful life of the trade secret
3. Income capitalization rate (discount rate minus growth rate)

A discounted cash flow analysis is based on estimate of all future cash flows associated with the trade secret asset and then discounting those future cash flows by risk-adjusted discount rate.

Below is a summary of income approach valuation methods, which can be relied upon to value trade secrets:

1. **Valuation methods that quantify an incremental amount of revenue or a decremental amount of cost (also known as with-and-without method).** This method assumes that the "(a) the owner/operator will generate a greater amount of revenue by owning or operating the intangible asset compared to not owning or operating the intangible asset or (b) the owner/operator will experience a lower amount of cost by owning or operating the intangible asset compared to not owning or operating the asset. The owner/operator revenue could increase because the intangible asset results in new products, new customers, an increased market share, an increased total market, increased units sold, increased unit selling price, decreased products and so on. The owner/operator operating cost could decrease because the intangible assets results in decreased production cost, decreased selling expense, decreased administrative expense, decreased research and development expense, or decreased interest expense."<sup>xxxiv</sup> It is important that the benefits of the trade secret are only difference in both scenarios.
2. **Valuation methods that rely on a hypothetical agreement that the owner and the operator will share (or split) the expected profits associated with the commercial**

**exploitation of the trade secret (also known as profit-split method).** “That is, the owner and the operator agree to split the total business profit (often measured as earnings before interest and taxes) related to the intangible asset commercialization. Another way to conceptualize the profit split category of valuation methods is that the owner provides the intangible asset and the operator provides the working capital assets, the tangible personal property and real estate assets, and the routine intangible assets used in the business. Each party (the owner and the operator) receives a split of the total business operating profit commensurate with their relative contribution to that business.”<sup>lxxxv</sup> This method is somewhat similar to the relief from royalty market method. The primary difference is the derivation of the royalty rate.

3. **Valuation methods that rely on a differential level of income.** “The phrase *differential level of income* simply means the difference in the amount of income. That is, these methods compare the owner/operator using the intangible asset to a benchmark income measure. The benchmark income measure would be (a) the owner/operator income without the intangible asset, (b) the owner/operator income using a prior generator of the intangible asset, (c) an industry average level of profitability, (d) a level of profitability earned by identified guideline companies, or (e) some other benchmark income measure. The differential income measure does not necessarily have to be owner/operator operating income, net income, or net cash flow. Rather, the differential income could be measured by the difference in just about any owner/operator financial fundamental.”<sup>lxxxvi</sup>
4. **Residual income methods that typically start with the owner/operator’s total business income.** “In applying these methods, the analyst identifies all of the owner/operator contributory assets. Contributory assets are all of the other assets—other than the actual intangible asset—that are used to produce the owner/operator income. Next, the analyst applies a fair rate of return on investment to each of the contributory asset categories. Typical contributory asset categories include net working capital assets, real estate and tangible personal property assets, and routine intangible assets (like, intangible assets other than the subject intangible asset). The analyst multiplies the fair rate of return by the value of each contributory asset category to conclude a contributory asset charge. The total business income less than the total contributory asset charge equals the residual (sometimes called *excess*) return. The residual income is the amount of owner/operator’s income associated with the intangible asset.”<sup>lxxxvii</sup> This method is generally used in situations in which the trade secret is the primary driver of cash flow.

Another important test for the damages expert to consider is the value of the trade secret(s) in relation to the overall enterprise value of the company. This can be especially relevant in situations when there are multiple trade secrets held by the plaintiff.

## **Reasonable Royalty**

In situations in which the damages cannot be calculated based on plaintiff’s actual loss or defendant’s unjust enrichment, a reasonable royalty can be used to calculate damages caused by the misappropriation of trade secrets. As discussed earlier, a reasonable royalty damages calculation is used relatively less frequently than the plaintiff’s actual loss or defendant’s unjust enrichment in misappropriation of trade secrets cases.

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The reasonable royalty is generally based on the royalty income that the plaintiff would have earned had it entered into an agreement to license the misappropriated trade secrets to the defendant. There is a relatively small amount of case law on quantifying reasonable royalty in trade secrets cases. Some experts may look at case law for reasonable royalty on patent infringement legal cases, which is far more developed.

The reasonable royalty rate method generally calculates what a third-party licensor would pay to a third-party licensee for an arm's length use license related to the misappropriated trade secret(s). Additionally, the royalty rate may be based on documentation between the parties (which shows the value that the parties placed on the misappropriated trade secrets) or other existing licensing agreements with other third parties for the trade secrets.

The AICPA Guide to Intangible Asset Valuation states that "The reasonable royalty rate method models the scenario in which the respondent approaches the owner/operator in good faith and negotiates an arm's-length license for the lawful use of the intangible asset [trade secret]. The principle supporting this method is that the licensee would be willing to pay a fair royalty rate for the inbound license of the claimant's intangible asset and the licensor would be willing to accept a fair royalty rate for the outbound license of the claimant's intangible asset."<sup>lxxxviii</sup>

In comparison to other types of intellectual property (patents, copyrights, and trademarks), there are significantly fewer licensing agreements pertaining to trade secrets. Additionally, damages experts may consider the factors used to determine reasonable royalty from patent infringement case law (such as Georgia-Pacific factors and apportionment), which are well-developed; however, this is not a requirement.

A reasonable royalty considers the royalty base and the royalty rate. A royalty rate can generally be based as a percentage of gross revenue, percentage of net revenue, percentage of cost savings, per unit, lump sum, or some other basis agreed to by the parties. Trade secrets are generally licensed either on an individual stand-alone basis, or as a component of a patent or a broader IP license agreement.

There are several sources of royalty rate data, which include.<sup>lxxxix</sup>

- ktMINE ([www.ktmine.com](http://www.ktmine.com))
- RoyaltySource ([www.royaltysource.com](http://www.royaltysource.com))
- RoyaltyStat ([www.royaltystat.com](http://www.royaltystat.com))
- Consor ([www.consor.com](http://www.consor.com))
- MARKABLES ([www.markables.net](http://www.markables.net))
- *Licensing Economic Review*
- Licensing Royalty Rates published by Wolters Kluwer and authored by Gregory J. Battersby and Charles W. Grimes

Below is a summary of royalty rate methods used to calculate a reasonable royalty rate in misappropriation of trade secrets matters:

1. **Incremental profit method.** "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. This profits measure (in other words, as if not 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.”<sup>xc</sup>

2. **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 discounted cash flow 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.”<sup>xci</sup>
3. **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:
  - the relevant time period of the third-party licenses;
  - the financial condition of both licensor and licensee parties;
  - the exclusivity of the license;
  - any relevant government regulations;
  - any nonmonetary compensation included in the license; and
  - the [remaining useful life] RUL of the licensed intangible asset.”<sup>xcii</sup>
4. **Comparable profit margin method** (also known as 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).”<sup>xciii</sup>

Cost savings may be another consideration in analyzing reasonable royalty.

The Supreme Court of Texas in *Southwest Energy Product Company v. Toby Berry-Helfand and Gery Muncey*, No. 13-0986, Oct. 2015, stated the jury was instructed to analyze both value-to-the-defendant and reasonable royalty measures. The jury determined the value of the trade secret to be \$11,455,000. This value was based on the “value to the defendant in the past was equivalent to the ‘value of the trade secret,’ which was defined in the charge as:

an estimate of the amount that a person desiring to use the trade secret would be willing to pay for its use and a trade secret owner desiring to license the trade secret would be willing to accept, if neither party were completed to do so. In determining the value of a trade secret, you may consider such factors as:

- (i) the resulting and foreseeable change in the parties’ competitive posture as a result of the misappropriation of the trade secret;
- (ii) the prices past purchasers or licensees of the trade secret may have paid;



- (iii) the total value of the trade secret to the owner, including their development costs and the importance of the secret to the owner's business;
- (iv) the nature and extent of the use the defendant intended for the secret; and
- (v) whatever other unique factors in the particular case might have affected the parties' agreement, had they negotiated and agreed on a reasonable value, such as the ready availability of alternative processes.<sup>xciv</sup>

In the matter of *Sabatino Bianco, M.D. v. Globus Medical, Inc.*, 53 F.Supp3d 929 (E.D. Tex. 2014), the Court set (an ongoing royalty rate of 5% on Defendant's future sales for a maximum of 15 years. Despite Defendant's argument that any "head start" it received had dissipated before trial so an ongoing royalty should not apply, the Court reasoned that Defendant failed to present evidence regarding its "head start" theory at trial so this was no basis to dispute the ongoing royalties. The Court noted that this was a proceeding to set the ongoing royalty rate so the jury's verdict was the proper starting point for making the determination of ongoing royalties." This decision was affirmed by the federal circuit. This case involved a doctor who was awarded \$4.3 million and future royalties in connection with three misappropriated trade secrets involving the company's top-selling spinal fusion devices.<sup>xcv,xcvi</sup>

## Defendant's Rebuttal Strategies to Plaintiff's Damages Expert's Opinions

Below is a list of certain defendant's rebuttal strategies to plaintiff's damages expert's opinions that a damages expert should generally consider:

- The plaintiff has not proved that its damages were caused by defendant's misappropriation of trade secrets and there is no nexus between the misappropriation of trade secrets and actual loss<sup>xcvii</sup>
- The plaintiff's damages amounts claimed or portions thereof, are unrelated to the alleged trade secret misappropriation<sup>xcviii</sup>
- The plaintiff's damages expert's opinions are deemed to be speculative and do not meet the reasonable certainty threshold
- The plaintiff's loss period for damages for the time it would have taken to independently develop the trade secret or reverse engineer the trade secret should be reduced<sup>xcix</sup>
- Some portion of the plaintiff's damages is comprised of an impermissible double-recovery<sup>c</sup>
- The defendant did not use the trade secret information – (example may include the doctrine of inevitable disclosure – inevitable disclosure is an inference that the former employee will inevitably use former employer's trade secrets in carrying out the same duties for new employer – state laws vary significantly on this issues)<sup>ci</sup>
- The plaintiff has not adequately defined / identified its trade secrets<sup>cii</sup>
- The plaintiff only included a damages model based on misappropriation of all of the trade secrets and failed to disaggregate damages among trade secrets or other legal claims<sup>ciii</sup>
- The alleged trade secret information is already in public domain and knowledge through public disclosure is not due to any act of the defendant<sup>civ</sup>
- The alleged trade secret information was independently developed by defendant without access to the trade secret information<sup>cv</sup>
- The alleged trade secret information was not kept secret in confidence and treated as confidential<sup>cvi</sup>
- The alleged trade secret information can be easily reversed engineered, independently derived, or acquired through other lawful means of acquisition<sup>cvii</sup>
- The alleged trade secret information does not provide a competitive advantage
- The plaintiff's losses to the business were caused by changes in consumer demand for a product or service incorporating the trade secret or alternative products
- Plaintiff's damages do not meet the test of reasonable certainty for recovery of damages
- The plaintiff did not indicate to employees, vendors, suppliers, consultants, etc. that certain information and/or know-how was considered to be a trade secret
- The remaining economic useful life of the trade secret is lower than the period asserted by the plaintiff's damages expert
- The plaintiff's damages expert does not have the requisite qualifications
- The plaintiff's damages expert relied upon unreliable data
- The plaintiff's damages expert employed unreliable methodology or procedures
- The plaintiff's damage expert's damages opinions included errors and omissions
- The plaintiff's damages expert used invalid assumptions
- The plaintiff's damages expert had unreliable results
- The plaintiff's damages expert's opinions were based on legal theories not available in the jurisdiction

## **Challenges in Quantifying Damages for Early Stage Companies or Technology – Observations from *Waymo v. Uber***

### **Uber**

Waymo has alleged that Uber stole its trade secrets and intellectual property and of infringing on patents related to its LiDAR systems. This matter dealt with self-driving car technology. It was alleged that Waymo's engineer took 14,000 files with him to Uber in January 2016. Waymo was the driverless car unit of Google until it was spun off Google's business in December 2016. Uber Technologies Inc. paid \$680 million for the self-driving technology in its acquisition of OttoMotto LLC in August 2016.

Waymo was initially seeking billions in damages including both unjust enrichment and reasonable royalty.<sup>cviii</sup>

- Waymo's unjust enrichment was based on incremental future profits or saved development.
  - \$3.242 billion incremental profits for unjust enrichment for eight trade secrets based on baseline coverage.
  - \$5.553 billion incremental profits for unjust enrichment for eight trade secrets based on optimistic coverage.
  - \$0.926 billion saved development costs for unjust enrichment for eight trade secrets
- Waymo's reasonable royalty damages were \$3.566 billion for eight trade secrets.

Below are selected excerpts from the *Daubert* ruling on the plaintiff's damage expert.

- “[Plaintiff’s Expert] offered opinions labeled as both unjust enrichment and reasonable royalty. Other than grade-school arithmetic, however, he did not apply any coherent principle, methodology, theory, or technique, much less one possessing any discernible indicia of reliability. Instead, he made the same arguments that the lawyers can make based on other evidence in the case that can speak for itself. As this order now explains, [Plaintiff’s Expert’s] opinions will be excluded both because they do not qualify as expert testimony under FRE 702 and because they are substantially more prejudicial than probative under FRE 403.”
- “[Plaintiff’s Expert’s] emphasis on his supposed ‘conservatism,’ both in the aforementioned paragraph and throughout his report, was an effort to appear reasonable despite the astronomical valuations assigned to each of Waymo’s asserted trade secrets. Put different, it was a transparent attempt to skew the damages horizon and desensitize the jury to the enormity of what Waymo is seeking by contrast with what it supposedly could have sought. In short, [Plaintiff’s Expert’s] phony cloak of conservatism was a mere trial gimmick – a fact that undercuts the reliability of his opinion.”
- “A separate problem is that [Plaintiff’s Expert] brings no specialized knowledge to the table. To repeat, he is not an economist but merely an inactive CPA and inactive lawyer. Here, for example, [Plaintiff’s Expert] simply adopted the opinions of others and performed grade-school arithmetic counsel can do on an easel. Where is any specialized knowledge? There is none. The absence of any real expertise is a pervasive problem in [Plaintiff’s Expert’s] incremental future profits ‘analysis.’”
- “[Plaintiff’s Expert’s] pseudo-‘analysis’ [is] nothing more than lawyer argument dressed up as expert opinion.”

## NAVIGATING THE CHALLENGES IN MEASURING DAMAGES IN MISAPPROPRIATION OF TRADE SECRETS MATTERS

- “Mind you, this comes to a total royalty more than ten times greater than a ‘ten percent’ royalty. [Plaintiff’s Expert] calls it “ten percent,” evidently to masquerade as more reasonable.”

Waymo and Uber agreed to a settlement of this matter during the first week of trial in February 2018 for payment of \$245 million in Uber stock (approximately 0.34 percent interest in Uber based on its stock price as of the date of settlement) and an agreement not to use the Waymo confidential information in the Uber technology.

Even though Waymo was seeking significantly more in damages, the settlement in *Waymo v. Uber* is still significant from a historical perspective and would be in the top ten for historical disclosed settlements in trade secrets cases.

### **Conclusion**

Trade secrets litigation is on the rise and will continue to increase in the future. There are a lot of approaches to measuring damages in a misappropriation of trade secrets litigation matter. It is important that counsel retains an experienced damage expert who can tie the damages remedies to the unique facts and circumstances of the case and be flexible in his/her approach to calculating damages. Quantifying damages in a trade secrets case is significantly different from other types of litigation matters. Additionally, there are significant differences in state and federal laws and case law covering misappropriation of trade secrets and counsel should work closely with an experienced damages expert in this area.

If you have any questions regarding measuring damages in misappropriation of trade secrets cases, please contact us below.

All the best,

Sikich LLP



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## **Curriculum Vitae of Shawn Fox, CPA, ABV, CFA, ASA**

Shawn Fox is a managing director in the dispute resolution practice of Sikich LLP (“Sikich”) and is based in the Chicago office. He has 22 years of experience providing forensic accounting and dispute advisory services to the business and legal community. As a certified public accountant, Shawn provides dispute advisory services, fraud and forensic accounting investigative services, financial analysis services, and valuation services to organizations and their counsel.

With significant experience in the preparation of expert reports, Shawn assists clients in all phases of complex litigation, including case assessments, discovery, document review, damages analysis, complex modeling, and demonstrative exhibits. He has testified in 46 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. Shawn is also retained as a consultant to quantify the potential damages or exposures in disputed matters.

Shawn directs forensic investigations and analysis across a wide range of areas, including high-stakes litigation, complex damages, lost profits, unjust enrichment, economic damages, diminution of value, reasonable royalty, intellectual property infringement, bad faith, breach of contract, breach of fiduciary duty, misappropriation of trade secrets, tortious interference, securities, fraud, purchase price disputes/post-acquisition disputes, class action, and bankruptcy litigation, as well as valuation and insurance claims recoveries.

Shawn also leads investigations on financial restatements and financial reporting fraud, regulatory investigations, assessing fraud risk, corporate investigations, employee misconduct, whistleblower, and construction cost overrun matters.

Prior to joining Sikich, he was the Partner-in-Charge of RSM’s litigation and investigation consulting services practices for the Central Region in Kansas City, a Managing Director of BDO’s litigation and dispute resolution practice in Chicago, and a Managing Director and national leader of economic damages practice at Willamette Management Associates in Chicago.

### **LICENSES AND CERTIFICATIONS**

Shawn holds the following certifications:

- Certified Public Accountant (“CPA”) licensed in Illinois, Missouri, Kansas, and Iowa
- Accredited in Business Valuation (“ABV”) with the American Institute of Certified Public Accountants (“AICPA”)
- Chartered Financial Analyst (“CFA”) with the CFA Institute (“CFAI”)
- Accredited Senior Appraiser (“ASA”) with the American Society of Appraisers in the business valuation discipline

### **PROFESSIONAL AFFILIATIONS**

His professional affiliations include:

- American Institute of Certified Public Accountants (“AICPA”)
- National Association of Forensic Economics (“NAFE”)
- American Bankruptcy Institute (“ABI”)

## NAVIGATING THE CHALLENGES IN MEASURING DAMAGES IN MISAPPROPRIATION OF TRADE SECRETS MATTERS

- Turnaround Management Association (“TMA”)
- American Society of Appraisers (“ASA”)
- Chicago Bar Association (“CBA”)
- Kansas City Metropolitan Bar Association (“KCMBA”)
- Missouri Society of Certified Public Accountants (“MOCPA”)

### EDUCATION

Bachelors of Business Administration, accounting, University of Iowa

### INTELLECTUAL PROPERTY LITIGATION EXPERIENCE

Shawn has worked on intellectual property litigation matters involving patent infringement, false patent marking, trademark and trade dress infringement, misappropriation of trade secrets, copyright infringement, false advertising, unjust enrichment, and transfer pricing. His intellectual property litigation expertise includes lost profits, reasonable royalty, incremental profits, fixed and variable costs, product line profitability, valuation, diminution in value, unjust enrichment, and apportionment.

#### *Patent Infringement and False Patent Marking*

- Prepared rebuttal analysis of plaintiff’s damages expert on legal claims for patent infringement and false patent marking related to hammermill hammers and grinder hammers.
- Prepare rebuttal analysis of plaintiff’s damages report asserted by non-practicing entity against national online retailer related to search technology (narrow by, narrow by).
- Prepared damages report on behalf of the plaintiff in a matter related to sorting and collating technology for pharmaceutical automation technology.
- Prepared damages report on behalf of the plaintiff in a matter related to technology that treats arthritis and other inflammatory conditions in animals.
- Prepared rebuttal analysis to lost profits and reasonable royalty damages assessment related to infant care products (bathroom safety).
- Prepared rebuttal analysis to lost profits and reasonable royalty damages assessment related to pet grooming tools.
- Prepared lost profits and reasonable royalty damages assessment related to alleged breach of contract, patent infringement, tortious interference, and misappropriation of trade secrets related to dog treats.
- Evaluated reasonable royalty for patented technology related to spill proof cups.
- Evaluated patent infringement damages and reasonable royalty related to online medical billing software.
- Evaluated patent infringement damages and reasonable royalty related to Voice-Over Internet Protocol (VoIP) technology.
- Evaluated patent infringement damages and reasonable royalty related to retractable syringes.
- Evaluated patent infringement damages related to magnetic induction heating technology applied to food delivery systems.
- Evaluated patent infringement damages and reasonable royalty with regard to coating machinery technology.

Trademark and Trade Dress Infringement

- Profit rate construction, including analysis of the expenses related to the production, distribution, and sale of the alleged infringing units, and apportionment analysis related to word and logo marks for footwear products.
- Analyzed revenues related to word marks and damages methodologies.

Misappropriation of Trade Secrets

- Prepare analysis of damages alleged by plaintiff. The plaintiff's legal claims include misappropriation of trade secrets, breach of contract, breach of implied covenant of good faith and fair dealing, unjust enrichment, fraudulent inducement, accounting, and unfair competition. The technology is related to video streaming technology. The defendant allegedly took the confidential information during due diligence of plaintiff.
- Prepared rebuttal analysis of damages calculated by the plaintiff's damages expert. The plaintiff's legal claims include violation of Copyright Act, misappropriation of trade secrets, unfair trade practices, fraud and fraudulent misrepresentation, conversion, intentional interference with contractual relations, tortious interference with prospective business relations, negligence, breach of contract, and unjust enrichment. The technology is related to software used by the gaming industry.
- Prepared analysis of damages alleged by plaintiff and rebuttal analysis of counterclaim plaintiff. The plaintiff's legal claims include declaratory judgment, misappropriation of trade secrets, civil theft of trade secrets, civil theft, conversion, intentional interference with contractual relations, breach of contract, and unjust enrichment. The defendant allegedly took confidential information and documents to his new investment banking firm.
- Prepared analysis of damages alleged by claimant and counterclaimant. The claimant was asserting breach of contract and the counterclaimant was asserting breach of contract; declaratory judgment; misappropriation of trade secrets; fraudulent inducement to enter a contract; tortious interference with a contract; and alter ego liability. Testified as an expert witness at deposition and at arbitration hearing for respondents and counterclaimant.
- Prepared analysis of damages alleged by the Plaintiff in a misappropriation of trade secrets, tortious interference with contractual relationships, and breach on non-compete agreement. Testified as an expert witness at deposition.
- Calculated unjust enrichment and reasonable royalty damages in connection with misappropriation of trade secrets and unjust enrichment claims related to pool safety technology.
- Analyzed unjust enrichment and misappropriation of trade secrets damages asserted by the plaintiff as a result of the plaintiff's head of research and development providing all of the plaintiff's trade secrets to one of its top competitors in its industry. Our work included analyzing the plaintiff's research and development costs, assisting with the determination of reasonable royalty the defendant would have paid to license the plaintiff's trade secrets, as well as helping to calculate the value of the specific benefits received by the defendant from the misappropriation of trade secrets.

Copyright Infringement

- Calculated plaintiffs' lost profits on sales of products, which would have been released "but for" the actions of the defendant, and defendant's profits from the sale of allegedly infringing products (related to model train accessory products).
- Analyzed revenues related to an alleged copyright infringement of a guitar used by a musician.

False Advertising

- Prepared rebuttal analysis of damages claims asserted by the plaintiff related to alleged false and misleading marketing activities of the defendants, alleged breach of the settlement agreement, and alleged fraudulent inducement of the settlement agreement. The key issue in this case related to private label versus on-label marketing activities of surgical swab applicators.
- Evaluated damages related to false advertisements in connection with cable modem and DSL service providers.

Unjust Enrichment

- Prepared analysis of defendant's profits derived from e-commerce activities related to legal claims of breach of fiduciary duty; beach of the implied duty of good faith and fair dealing; conspiracy in restraint of trade; and fraudulent misrepresentation, inducement, and omission.

Transfer Pricing

- Prepared comparable uncontrolled transaction (CUT) method analysis for transfer pricing litigation matter. This case involved analysis of license agreements between U.S. parent company and subsidiaries and foreign licensees (supply points).



## **Curriculum Vitae of David Wharton, CPA, CFE, CFF**

David is a senior manager in Sikich's dispute advisory services practice. He has thirteen years of experience providing forensic accounting, litigation support and financial consulting services covering a wide array of complex matters including: commercial litigation, fraud investigations, determination of lost profits, insurance claims such as business interruption and fidelity bonds, financial institution related matters, class actions and intellectual property disputes. David has significant experience developing dynamic yet easy to understand damages models for complex litigation matters, investigating known or alleged instances of financial fraud as well as managing and analyzing large volumes of financial data using database tools.

David is also experienced in assisting counsel with discovery requests, document review, opposing expert report critiques, the preparation of deposition questions for both fact and opposing expert witnesses and trial demonstratives preparation.

Prior to joining Sikich, David worked in the Litigation and Investigative Services practice at two of the six largest international accounting firm providing forensic accounting, litigation support, financial consulting and investigative services.

David's experience includes the following types of matters:

- Lost profits damages calculations
- Breach of contract damages
- Business interruption claims
- Earn-out / purchase price disputes
- Partnership disputes
- Statutory violations
- Patent and trademark infringement
- Construction related matters
- Class action matters
- Fraud investigations
- Employee theft / misuse of corp. assets
- Complex funds tracing
- Marital dissolutions
- Personal injury / wrongful death
- Investigation and substantiation of claims for insurance carriers
- Insurance claim preparation for insureds
- Residential mortgage lending matters

### **Representative Case Experience**

#### **Breach of Contract / Lost Profits**

- Analyzed all capital asset and charity care expenditures over numerous years of a Midwestern hospital group on behalf of a healthcare foundation for compliance with terms of an asset purchase agreement when the former not-for-profit hospitals were purchased by a large for-profit hospital corporation.
- Calculated the lost profits incurred by a pharmacy buying group as a result of the termination of the buying group's contract with a pharmaceutical drug wholesaler.
- Analyzed the business records of a Midwest trucking firm on behalf of the firm's truck leasing company. The trucking firm had sued the leasing company over the poor condition of the trucks which the trucking firm claimed forced it out of business. The analysis of the relevant records showed that the trucking firm was significantly less profitable than the opposing expert claimed in his report.

### **Class Action Matters**

- Managed the development of a complex database of mortgage origination and payment data for a large class action case for a bank in Ohio. Performed analyses and queries of the data to determine potential damages. Analyzed the opposing expert's damages database and discovered a large error which significantly reduced the amount of claimed damages. Case involved the bank's improper calculation of interest on residential mortgage loans.
- Assisted in the creation of a large database of mortgage loan origination data and performed numerous queries and analyses of the data at counsel's request to ascertain loan information and potential settlement amounts for individual borrowers in a large residential mortgage class action case. Case involved a claimed violation of Missouri's usury statute.
- Reviewed a large propane company's commercial propane contracts to assist in the determination of class member inclusion and exclusion for a class action matter which alleged that commercial propane customers had been charged improper rates for propane gas in excess of their contracted amounts.

### **Trademark Infringement**

- Analyzed two decades of financial statements of several dozen foreign subsidiaries of a large multi-level marketing beauty products company as part of the development of a complex damages model for use in the expert damages analysis of a trademark infringement dispute.
- Managed a complicated financial model in a trademark infringement case involving an apparel manufacturer and a chain of shoe stores. Helped prepare expert witness for deposition and trial testimony.
- Prepared a damages model and expert report in a trademark infringement dispute between a motorcycle manufacturer and an apparel manufacturer.

### **Patent Infringement**

- Prepared a damages model and expert report in a patent infringement dispute between two manufacturers of sound dampening materials in the automotive industry.
- Assisted with the preparation of a lost profits damages and reasonable royalty analysis in a patent infringement, breach of contract, tortious interference and misappropriation of trade secrets dispute between a pet treat manufacturer/retailer and the previous owner of the intellectual property.

### **Other Litigation Matters**

- Reviewed several hundred boxes of financial records of a bankrupt airline for relevancy in a dispute between the airline and an engine manufacturer over downtime caused by engine repairs and maintenance. From the documents reviewed, developed a preliminary damage model for counsel which was used to settle the case.
- Prepared a damages model for a matter involving a general contractor, the general contractor's insurance company and a county government which arose during the construction of the county's correctional facility.

## NAVIGATING THE CHALLENGES IN MEASURING DAMAGES IN MISAPPROPRIATION OF TRADE SECRETS MATTERS

- Served on a consulting team which worked directly with counsel and the testifying expert witness to analyze the work papers and audit reports of a Big Four accounting firm which was accused of failing to follow professional standards in the performance of its audit of an international trucking firm.
- Helped investigate claims of auditor malpractice involving its audit of a large financial services client. The accounting firm was under threat of lawsuit from the shareholders of the financial services firm.

### **Professional Accreditations and Affiliations**

- Certified Public Accountant (“CPA”) licensed in Missouri with reciprocity in most other states
- Certified Fraud Examiner (“CFE”) from the Association of Certified Fraud Examiners
- Certified in Financial Forensics (“CFF”) from the American Institute of Certified Public Accountants
- Member of the American Institute of Certified Public Accountants (“AICPA”)
- Member of the Association of Certified Fraud Examiners (“ACFE”)

### **Education**

- Bachelor of Science in Accounting with distinction, University of Missouri, Kansas City

## **Curriculum Vitae of Alex Brandon, ASA**

Alex Brandon is a senior manager in Sikich's Forensic and Valuation Services practice. He has 10 years of experience in providing valuation and dispute advisory services to the business and legal community.

Alex manages engagements across a range of service lines, including:

- Damages analyses related to complex commercial, intellectual property infringement, and bankruptcy litigation matters;
- Valuations for financial and tax reporting purposes;
- Valuations for estate and gift tax planning purposes.

Additionally, Alex has served as an expert witness regarding the valuation of an entity for an arbitration matter and has extensive experience assisting clients in all phases of litigation, including early case assessment, discovery, document review, damages analysis, and trial preparation. He has performed analyses related to lost profits, diminution of value, economic loss, reasonable royalty, and unjust enrichment. He also has experience in researching economic and industry data, building financial models, applying forensic accounting techniques, and writing expert reports.

Prior to joining Sikich, Alex worked as an experienced manager in Grant Thornton's corporate finance practice and as a manager in RSM's litigation and investigative services practice, where he provided business valuation, forensic accounting and litigation support services to middle and upper middle market clients.

### **LICENSES AND CERTIFICATIONS**

Alex holds the following certification:

- Accredited Senior Appraiser ("ASA") with the American Society of Appraisers in the business valuation discipline

### **PROFESSIONAL AFFILIATIONS**

Alex's professional affiliations include:

- American Society of Appraisers ("ASA")
- Bar Association of Metropolitan St. Louis ("BAMSL")
- Association of Certified Fraud Examiners ("ACFE")

### **EDUCATION**

Bachelor of Science in Business Administration, Finance, University of Missouri  
Master of Business Administration, Management, University of Missouri

## NAVIGATING THE CHALLENGES IN MEASURING DAMAGES IN MISAPPROPRIATION OF TRADE SECRETS MATTERS

### PRESENTATIONS

- 6/18 “Quantifying Damages in Breach of Contract Cases,” Live Presentation at Greensfelder, Hemker & Gale, P.C.
- 4/18 “Calculating Damages in Tortious Interference Matters,” Live Webinar Hosted by Sikich Forensics Academy
- 1/18 “Lost Profits and Other Damage Calculations,” Live Webinar Hosted by *The Knowledge Group*
- 4/14 “Daubert Challenges: Key Issues, Recent Trends and Preparing Damages Experts,” Live Presentation at Thompson Coburn LLP
- 4/12 “Common Mistakes to Avoid in Calculating Lost Profits in Breach of Contract Matters,” Live Presentation at Sandberg Phoenix & von Gontard P.C.

### EXPERT TESTIMONY

- 2013 *John Riordan, M.D., Plaintiff/Claimant v. Phoenix Urology of St. Joseph, Inc., Mercury Investors, Inc., Mercury Equipment Co., Inc., and Mercury Surgery Center, LLC, Defendants/Respondents*  
Case No. 12BU-CV00447. Hollis Hanover Arbitrator  
Engaged by the plaintiff to opine on the value of a 25% ownership interest in Phoenix Urology of St. Joseph, Inc. in connection with the termination of a minority shareholder

### NOTABLE ENGAGEMENTS

- ASC 805 and tax allocation analyses for a publicly traded consumer products company
- ASC 805, 350 and 718 analyses for a \$900 million healthcare technology company
- ASC 805 analysis in connection with change of ownership of a National Hockey League club
- Rebuttal analysis of a valuation expert in connection with a legal malpractice matter with alleged damages of approximately \$260 million
- Solvency (valuation) analyses of 37 entities in connection with the bankruptcy of a large boat manufacturer
- Evaluation and rebuttal valuation analysis of an aerospace company in connection with a breach of contract claim
- FDIC mandated examination of community bank to investigate potential fraudulent financial reporting
- Investigation of claimed asset purchases in relation to a multi-hospital purchase agreement
- Calculation of damages (lost profits and increased expenses) for a breach of contract claim in connection with a Department of Veterans Affairs project
- Calculation of damages (construction cost overruns, liquidated delay damages, and additional financing costs) for a breach of contract claim between owner and contractor

## NAVIGATING THE CHALLENGES IN MEASURING DAMAGES IN MISAPPROPRIATION OF TRADE SECRETS MATTERS

- Evaluation and rebuttal of damages claim associated with the termination of an employment contract
- Evaluation and rebuttal of damages claims asserted by the plaintiff related to alleged false and misleading marketing activities of the defendants, alleged breach of settlement agreement, and alleged fraudulent inducement of settlement agreement and prepared counter damages claim related to alleged false and misleading marketing activities of the plaintiff
- Evaluation and rebuttal of damages claim asserted by the plaintiff in an inverse condemnation litigation matter involving a dairy farm

<sup>i</sup> “Time to Modernize and Strengthen Trade Secret Law,” *Corporate Counsel*, December 1, 2015.

<sup>ii</sup> “Protection of Trade Secrets: Overview of Current Law and Legislations,” Congressional Research Service Report, Brian T. Yeh, September 5, 2014.

<sup>iii</sup> *Am. Sales Corp. v. Adventure Travel, Inc.*, 862 F. Supp. 1476, 1479 (E.D. Va. 1994).

<sup>iv</sup> *Sw. Energy Prod. Co. v. Berry-Helfand*, 491 S.W. 3d 699, 711-711 (Tex. 2016).

<sup>v</sup> *University Computing Co. v. Like’s-Youngstown Corp.*, 504 F.2d 518 (5<sup>th</sup> Cir. 1974).

<sup>vi</sup> Protection of Trade Secrets: Overview of Current Law and Legislations,” Congressional Research Service Report, Brian T. Yeh, September 5, 2014, p. 13.

<sup>vii</sup> “The Case for Enhanced Protection of Trade Secrets in the Trans-Pacific Partnership Agreement,” U.S. Chamber of Commerce, p. 11.

<sup>viii</sup> <https://www.fbi.gov/news/testimony/combating-economic-espionage-and-trade-secret-theft>.

<sup>ix</sup> Lex Machina Trade Secret Litigation Report 2018, July 2018.

<sup>x</sup> [http://ipcommission.org/report/IP\\_Commission\\_Report\\_Update\\_2017.pdf](http://ipcommission.org/report/IP_Commission_Report_Update_2017.pdf).

<sup>xi</sup> “Seven Reasons Why Trade Secrets Are Increasingly Important,” Berkeley Technology Law Journal, September 1, 2012.

<sup>xii</sup> <https://www.law.com/corpcounsel/2018/06/12/what-you-need-to-know-about-the-european-trade-secrets-directive/>.

<sup>xiii</sup> <https://www.law.kuleuven.be/citip/blog/will-eu-member-states-implement-the-eu-directive-on-trade-secrets-on-time/>.

<sup>xiv</sup> “Update: A New Top 10 Disclosed Trade Secret Settlement,” Orrick, Herrington & Sutcliffe LLP, Monte Cooper and Cam Phan, July 18, 2014.

<sup>xv</sup> “DuPont Settles Trade-Secrets Case Against Kolon Industries,” *The Wall Street Journal*, April 30, 2015.

<sup>xvi</sup> <https://www.law.cornell.edu/uscode/text/18/1839>.

<sup>xvii</sup> Uniform Trade Act with 1985 Amendments, § 1.4.

<sup>xviii</sup> “Best Practices & Legal Requirements For Protecting Your Company’s Trade Secrets, Kilpatrick Townsend, May 4, 2015.

<sup>xix</sup> <http://www.uniformlaws.org/LegislativeFactSheet.aspx?title=Trade%20Secrets%20Act>.

<sup>xx</sup> Professors’ Letter in Opposition to the Defend Trade Secrets Act of 2015 (S. 1890, H.R. 3326), November 17, 2015, p. 7.

<sup>xxi</sup> <http://www.beckreedriden.com/trade-secrets-laws-and-the-utsa-a-50-state-and-federal-law-survey-chart/>.

<sup>xxii</sup> “Anything but Uniform: A State-By-State Comparison of the Key Differences of the Uniform Trade Secrets Act, Snell & Wilmer L.L.P., Sid Leach.

<sup>xxiii</sup> 18 U.S. Code Chapter 90 – Protection of Trade Secrets, §1839, para. 3.

<sup>xxiv</sup> New York First Restatement of Torts, §757.

<sup>xxv</sup> <https://www.law.cornell.edu/uscode/text/18/1839>.

<sup>xxvi</sup> *Ibid*, §1.2.

<sup>xxvii</sup> Uniform Trade Act with 1985 Amendments, p. 2.

<sup>xxviii</sup> <https://www.law.cornell.edu/uscode/text/18/1839>.

<sup>xxix</sup> <https://www.law.cornell.edu/uscode/text/18/1839>.

- <sup>xxx</sup> *Ibid*, §2(a).
- <sup>xxxi</sup> *Ibid*, p. 8.
- <sup>xxxii</sup> *Ibid*, 2(b).
- <sup>xxxiii</sup> *Ibid*, §3(a).
- <sup>xxxiv</sup> *Ibid*, p. 11.
- <sup>xxxv</sup> Uniform Trade Act with 1985 Amendments, §3(b).
- <sup>xxxvi</sup> <https://www.law.cornell.edu/uscode/text/18/1839>.
- <sup>xxxvii</sup> Uniform Trade Act with 1985 Amendments, §4.
- <sup>xxxviii</sup> *Ibid*, §6.
- <sup>xxxix</sup> <https://law.justia.com/codes/alabama/2006/4653/8-27-4.html>.
- <sup>xl</sup> <https://www.law.com/newyorklawjournal/2018/05/11/recoverable-damages-in-trade-secret-and-unfair-competition-claims/>.
- <sup>xli</sup>
- [https://leginfo.legislature.ca.gov/faces/codes\\_displayText.xhtml?lawCode=CIV&division=4.&title=5.&part=1.&chapter=&article=](https://leginfo.legislature.ca.gov/faces/codes_displayText.xhtml?lawCode=CIV&division=4.&title=5.&part=1.&chapter=&article=)
- <sup>xlii</sup> <https://www.law.cornell.edu/uscode/text/18/2701>.
- <sup>xliiii</sup> <https://www.law.cornell.edu/uscode/text/18/2707>.
- <sup>xliiv</sup> <https://www.law.cornell.edu/uscode/text/18/1030>.
- <sup>xliv</sup> <https://www.law.cornell.edu/uscode/text/18/1030>.
- <sup>xlvi</sup> <https://www.law.cornell.edu/uscode/text/18/1030>.
- <sup>xlvii</sup> 18 U.S. Code Chapter 90 – Protection of Trade Secrets, §1831.
- <sup>xlviii</sup> Lex Machina Trade Secret Litigation Report 2018.
- <sup>xlix</sup> <http://www.txcourts.gov/media/1386415/130986.pdf>.
- <sup>l</sup> <https://www.casemine.com/judgement/us/5914b0d7add7b049347554a7>.
- <sup>li</sup> Guide to Intangible Asset Valuation, American Institute of Certified Public Accountants, Robert F. Reilly and Robert P. Schweihs, 2014, p. 117.
- <sup>lii</sup> Gross revenue is generally the money a company earning through its normal business operations (such as selling a product or service); whereas, net revenue is generally defined to be gross revenue less sales returns and allowances and sales discounts.
- <sup>liii</sup> “Calculating Lost Profits,” AICPA Practice Aid 06-4, p. 3.
- <sup>liiv</sup> <https://www.leagle.com/decision/infdc020150824577>.
- <sup>liv</sup> “Calculating Lost Profits,” AICPA Practice Aid 06-4, p. 25.
- <sup>lvi</sup> *Ibid.*, p. 26.
- <sup>lvii</sup> “Current Trends in Trade Secret Valuation and Damages, Business Valuation Resources, LLC, Barry Werbin and Craig Jacobson, July 28, 2015, slide 47.
- <sup>lviii</sup> “Calculating Lost Profits,” AICPA Practice Aid 06-4, p. 26.
- <sup>lix</sup> *Ibid*, p. 29.
- <sup>lx</sup> *Ibid*, pp. 29-30.
- <sup>lxi</sup> Guide to Intangible Asset Valuation, American Institute of Certified Public Accountants, Robert F. Reilly and Robert P. Schweihs, 2014, p. 188.
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