

IN THIS ISSUE

Supreme Court Abolishes Federal Circuit's Test for Willfulness

Page 1

Brexit and Your European Trademarks

Page 2

Show Me the Money—*Kirtseng* and Supreme Court Guidance on Attorneys' Fees Awards in Copyright Cases

Page 3

The Crumbling of Collaborative Copyright Authorship Under *16 Casa Duse* and *Garcia*

Page 5

Harmonization of Trade Secrets in Europe and New U.S. Trade Secrets Law Gets the Green Light—What Do These Changes Mean for Companies in Germany, the UK, and the U.S.?

Page 6

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Supreme Court Abolishes Federal Circuit's Test for Willfulness

By [Bitra Rahebi](#) and [Esther Kim Chang](#)



On June 13, 2016, in *Halo Electronics, Inc. v. Pulse Electronics, Inc.*, 579 U.S. ____ (2016), the Supreme Court unanimously abrogated the Federal Circuit's 2007 decision in *In re Seagate Tech., LLC*, 497 F.3d 1360 (Fed. Cir. 2007). That decision

had established the standard for finding willful infringement, which is the predicate for awarding enhanced damages in patent infringement cases.

Seagate held that a plaintiff seeking enhanced damages must show that the infringement was willful under a two-pronged inquiry. *Id.* at 1371. First, the patent owner had to "show by clear and convincing evidence that the infringer acted despite an objectively high likelihood that its actions constituted infringement of a valid patent." *Id.* Objective recklessness would not be found if the accused infringer "raise[d] a substantial question as to the validity or noninfringement of the patent" during the infringement proceedings. *Halo Elecs.*, 579 U.S. ____ (slip op., at 5). Second, if it could establish objective recklessness, the patent owner then had to show, again by clear and convincing evidence, that the risk of infringement "was either known or so obvious that it should have been known to the accused infringer." *Seagate*, 497 F.3d at 1371.

The Supreme Court concluded that the Federal Circuit's willfulness test was "unduly rigid" and "impermissibly encumber[ed] the statutory grant of discretion to district courts." *Halo Elecs.*, 579 U.S. ____ (slip op., at 9). The problem with the prior test, according to the high court, was that it "require[d] a finding of objective recklessness in every case" before a court could award enhanced damages. *Id.* The Court reasoned that the language of the statute contained no such explicit limit or condition on when judges could make such awards. *Id.* at 8. Rather, 35 U.S.C. § 284 states only that a "court may increase the damages up to three times the amount found or assessed" and thus gives district courts discretion in awarding enhanced damages.

The Supreme Court also reasoned that the previous test allowed defendants to escape enhanced damages by pointing to a reasonable

continued on page 2

defense developed only during litigation. Under *Seagate*, the objective recklessness inquiry could be based on the “record developed in the infringement proceeding[s].” 497 F.3d at 1371. According to the Supreme Court, this allowed a person who willfully infringed a patent to escape enhanced damages as long as he could “muster a reasonable (even though unsuccessful) defense at the infringement trial” — “even if he did not act on the basis of the defense or was even aware of it.” *Halo Elecs.*, 579 U.S. ____ (slip op., at 10). The proper focus of the inquiry, the Court noted, should be on what the accused infringer knew at the time of the infringement, rather than on defenses later presented at trial. *Id.*

Accordingly, the Supreme Court concluded that, in certain cases, the subjective willfulness of a patent infringer could warrant enhanced damages — without regard to whether his or her infringement was objectively reckless. *Id.* This change allows an award of enhanced damages in certain cases involving deliberate infringement, even though an “independent showing of objective recklessness” may be unavailable or difficult to prove.

Although the decision whether to award enhanced damages is within the district court’s discretion, the Supreme Court cabined that discretion by holding that enhanced damages should be limited “to egregious cases of misconduct beyond typical infringement” and should not be awarded in “garden-variety cases.” *Id.* at 15.

AMENDED BURDEN OF PROOF

In addition to abandoning the prior test, the Supreme Court rejected the clear and convincing evidence standard required by *Seagate*. The Supreme Court held that enhanced damages need be proven by a preponderance of the evidence. *Id.* at 12.

AMENDED STANDARD OF APPELLATE REVIEW

The Supreme Court also addressed the standard for appellate review. Under Federal Circuit precedent, an award of enhanced damages was subject to trifurcated appellate review. *Id.* at 5. The first prong of the willfulness test, *i.e.*, objective recklessness, was reviewed *de novo*. *Id.* at 5-6. The second prong, *i.e.*, subjective knowledge, however, was reviewed for substantial evidence. *Id.* at 6. And the ultimate decision to award enhanced damages was reviewed for an abuse of discretion. *Id.*

The Supreme Court rejected the Federal Circuit’s three-part framework for appellate review and held that enhanced damages awards should be reviewed on appeal for an abuse of discretion. *Id.* at 12-13.

CONCLUSION

The Supreme Court’s decision in *Halo* allows for an award of enhanced damages in certain cases without establishing objective recklessness, amends the burden of proof for establishing willfulness from a clear and convincing evidence standard to a preponderance of the evidence standard, and makes clear that the district court’s decision whether to award enhanced damages is reviewed for abuse of discretion.

BREXIT AND YOUR EUROPEAN TRADEMARKS

By [Amanda Phillips](#), [Joyce Liou](#), and [Jennifer Lee Taylor](#)



The United Kingdom has voted by a narrow majority to leave the European Union (“Brexit”). But the process of Brexit will take time, and the implications for our clients’ businesses will also unfold over time. Our MoFo Brexit Task Force is coordinating across all of our offices and working with clients on their key concerns and issues, now and in the coming weeks and months. We will also be providing MoFo Brexit Briefings on a range of key issues. We are here to support you in any and every way that we can.

The European Union Trademark (“EUTM”) is possibly the most widely used vehicle worldwide to protect trademark rights. A single application filed in the European Union Intellectual Property Office (“EUIPO”) in Alicante, Spain provides protection in the 28 member countries of the European Union (“EU”). In view of the UK Brexit vote on June 23, 2016, you might be wondering what this means for trademarks that you have protected via an EUTM.

First and foremost, you should know that, as of now, your trademark rights are secure. Last week’s vote was only the first step in a multi-stage process which would culminate with the United Kingdom withdrawing as an EU member state. Your EUTM will protect your trademark rights in the United Kingdom until the United Kingdom formally exits the EU.

As for the long term, EU trademark practitioners currently think that it is highly likely that the final terms of the United Kingdom’s exit from the EU will include

some mechanism to address the protection of EUTMs in the United Kingdom. The simplest solution would be for the United Kingdom Trademark Office to register as United Kingdom national registrations any marks that were previously registered as EUTMs, while preserving their priority dates. But this could create conflicts within the United Kingdom trademark registry and may not be feasible. Further, the costs, procedures, and timeline for such a transition have not been worked out, and the scope of such an administrative undertaking would be enormous.

Because of these uncertainties, and in order to minimize any risks associated with this changeover, anyone who owns EUTMs and views the United Kingdom as an important market may want to consider filing for United Kingdom trademark registrations now, rather than waiting to see what happens when the United Kingdom formally exits the EU. And for new trademarks, we recommend filing in both the EU and the United Kingdom if the United Kingdom will be an important market for you. This increases costs only slightly and clearly secures a priority date for the United Kingdom.

We encourage you to reach out to us with any questions on your filing strategies.

SHOW ME THE MONEY— KIRTSAENG AND SUPREME COURT GUIDANCE ON ATTORNEYS' FEES AWARDS IN COPYRIGHT CASES

By [Michael Jacobs](#), [Eric Acker](#), and [Dean Atyia](#)



WHAT'S NEW

In June, the Supreme Court provided substantial guidance in an unsettled area of law by holding that, in deciding whether to award attorneys' fees under the Copyright Act's fee-shifting provision, 17 U.S.C. § 505, a court should give substantial weight to the objective reasonableness of the losing party's position, while still taking into account all other circumstances relevant to granting fees. *Kirtsaeng v. John Wiley & Sons, Inc.*, No. 15-375 (U.S. Jun. 16, 2016).

COMING IN HOT!

We'd like to extend our congratulations to our colleagues on recent awards and recognitions:

- *The National Law Journal* named MoFo to its fifth annual Intellectual Property Hot List.
- *Chambers USA* ranked MoFo's IP Practice as Band 1 in California and recommended 14 attorneys from the practice.
- *Legal 500 US 2015* named 20 MoFo attorneys as recommended in copyright, patent prosecution: utility and design, patent licensing and transactional, trademarks: litigation, patent litigation: full coverage, technology: outsourcing, patent litigation: International Trade Commission, and technology: transactions.
- MoFo has three partners ranked gold for patent litigation in California in the IAM Patent 1000 2016 - a feat matched by only one other firm. **Michael Jacobs**, **Rachel Krevans**, and **Harold McElhinny** complete the golden trio. MoFo also has the joint highest number of recommended individuals in the IAM Patent 1000 listings in California. The list includes 19 attorneys in the Intellectual Property group from around the world.
- *The Daily Journal* named San Francisco partner **Diana Kruze** to its list of "Top 40 Under 40" lawyers in California for 2016.

BACKGROUND

This story begins with an enterprising college student buying foreign textbooks on the cheap to sell in the United States for a profit. Petitioner Supap Kirtsaeng came to the United States from Thailand to study math at Cornell University. Respondent John Wiley & Sons (“Wiley”), an academic publishing company, sells textbooks to students in U.S. and foreign markets. Kirtsaeng noticed an arbitrage opportunity: Wiley’s textbooks sold in Thailand were virtually identical to their American counterparts, but much cheaper. Kirtsaeng asked family and friends to buy the foreign editions so that he could sell them to his fellow students for a profit.

Wiley discovered what Kirtsaeng was doing and sued him for copyright infringement, claiming that his activities violated Wiley’s exclusive right to distribute its copyrighted textbooks. Kirtsaeng invoked the first-sale doctrine as a defense. Under that doctrine, the lawful owner of a book or other copyrighted work is able to resell or otherwise dispose of the work as he sees fit. In short, Kirtsaeng argued that if he bought the book lawfully, he could sell it to whomever he wished.

But at the time Kirtsaeng raised the defense, lower courts were conflicted as to whether the first-sale doctrine applied to foreign-made books, and the Supreme Court ultimately divided four to four the first time it addressed the issue in *Costco Wholesale Corp. v. Omega, S.A.*, 562 U.S. 40 (2010). To settle the continuing conflict, the Court granted Kirtsaeng’s petition for certiorari on the issue and established that the first-sale doctrine allows the resale of foreign-made books, just as it does domestic ones. Kirtsaeng thus prevailed in defending against Wiley’s infringement claim.

TO THE VICTOR GOES THE SPOILS?

Returning victorious to the district court, Kirtsaeng invoked section 505 to seek more than \$2 million in attorneys’ fees from Wiley. The district court denied his motion, and the Second Circuit affirmed. The Supreme Court granted certiorari because lower federal courts had followed a variety of different approaches when determining whether to award attorneys’ fees. Section 505 states that a district court “may . . . award a reasonable attorney’s fee to the prevailing party.” It authorizes attorney fee-shifting, but without specifying standards that courts should adopt, or guideposts they should use, in determining when such awards are appropriate. The Court explained that the statutory language “connotes discretion” and lacks any “precise rule

or formula” for awarding fees. *Kirtsaeng*, No. 15-375 at 4 (quoting *Fogerty v. Fantasy, Inc.*, 510 U.S. 517 (1994)).

Yet the Court had previously recognized that there are limits on a court’s discretion. A district court may not award attorneys’ fees as a matter of course but must instead make a case-by-case determination. *Id.* A court also may not treat prevailing plaintiffs and prevailing defendants differently; litigants should be encouraged to litigate to the same extent whether they are plaintiffs or defendants. *Id.* Additionally, several nonexclusive factors should inform a court’s decision: “frivolousness, motivation, objective unreasonableness[,] and the need in particular circumstances to advance considerations of compensation and deterrence.” *Id.* But the Court recognized that there was “a need for some additional guidance” for lower courts.

The Supreme Court agreed with Wiley that, in deciding whether to award fees, a district court should give “substantial weight to the objective (un)reasonableness of a losing party’s litigating position.” *Id.* at 6. In so ruling, the Court rejected Kirtsaeng’s argument that district courts should give special consideration to whether a lawsuit resolved an important and close legal issue and thus meaningfully clarified copyright law.

The Court reasoned that the objective-reasonableness approach advances the Copyright Act’s goals because it both encourages parties with strong legal positions to stand on their rights and deters ones from weak legal positions from proceeding with litigation. According to the Court, when a litigant is clearly correct, the likelihood that he or she will recover fees gives him or her an incentive to litigate all the way, even if the damages at stake are small.

The Court also explained that the objective-reasonableness approach is more administrable than the “important and close legal issue” approach supported by Kirtsaeng because it would be difficult for a court to know at the end of a case whether a newly decided issue will have critical, broad legal significance.

The Court made clear, however, that objective reasonableness, while an important factor, is not always controlling. In any given case, even when a party’s position is objectively reasonable, a court may still award attorneys’ fees based on other relevant factors, and it may deny fees even though the losing party made unreasonable arguments. “Although objective reasonableness carries significant weight, courts must view all the circumstances of a case on their own terms, in light of the Copyright Act’s essential goals.”

WILEY SEEMS REASONABLE

Lower courts had concluded that Wiley’s position on the first sale doctrine was objectively reasonable, especially considering that several courts of appeals and four Justices of the Supreme Court had agreed that the first-sale doctrine did not apply to foreign-made works. The Court nevertheless remanded the case so the district court could again review Kirstaeng’s fee application—giving substantial weight to the reasonableness of Wiley’s litigating position, but also taking into account all relevant factors.

THE CRUMBLING OF COLLABORATIVE COPYRIGHT AUTHORSHIP UNDER *16 CASA DUSE* AND *GARCIA*

By [Paul Goldstein](#) and [Joyce Liou](#)



When is an author not an author? In *16 Casa Duse, LLC v. Merkin*, the Second Circuit Court of Appeals held that a film director’s

contributions, which the parties conceded did not qualify as a work for hire or a joint work, also failed to qualify as an independently copyrightable work of authorship.¹ While the court noted that the director “exercised a significant degree of control” over many of his film’s creative decisions respecting “camera work, lighting, blocking, and actors’ wardrobe, makeup, and dialogue delivery,” these contributions did not constitute “a ‘work of authorship’ amenable to copyright protection” because “non-freestanding contributions to works of authorship are not ordinarily themselves works of authorship.”²

The legal problem at the heart of *16 Casa Duse* is that the Copyright Act nowhere sanctions the denial of protection to copyrightable expression on the ground that it is “non-freestanding.” The practical problem created by the decision is that it throws into doubt the copyright status of the countless expressive contributions to collaborative works—computer code is a notable example—that for one reason or another fall outside the work for hire and joint work rubrics. The questionable status of these contributions can be partially, but never completely, repaired through the careful structuring of copyright assignments and licenses.

Ordinarily in the U.S., films fall into the work for hire category, with the director’s contributions assimilated to those of the actors, screenwriter, composer, and other participants. Because the film in *16 Casa Duse* failed to qualify under either of the Act’s two branches of work for hire—as “(1) a work prepared by an employee within the scope of his or her employment,” or as “(2) a work specially ordered or commissioned” for one of nine statutorily specified uses (of which a motion picture is one) “if the parties expressly agree in a written instrument signed by them that the work shall be considered a work made for hire”—the court was unable to assimilate the director’s rights to an employer’s.³

A collaborative work that fails to qualify as a work for hire will often nonetheless qualify as a joint work, defined by the Act as “a work prepared by two or more authors with the intention that their contributions be merged into inseparable or interdependent parts of a unitary whole.”⁴ The film in *16 Casa Duse* would presumably have met this test, and the director would have been a joint owner, but for an unusual twist that the Second Circuit had in *Childress v. Taylor* earlier added to the statutory definition: for a joint work to exist there must also be an “intent of both participants in the venture to regard themselves as joint authors.”⁵ Such intent was missing in *16 Casa Duse*.

The *Childress* gloss aimed to resolve a practical problem created by the statutory definition of joint work. Read literally, the statutory definition would give book editors and other secondary contributors to a work’s expression the (presumably unintended) status of joint owners. But, in removing this possibility by adding a requirement that they intend legally to be joint authors, *Childress* created

a greater practical problem than the one it resolved. If the editor’s contribution of expression does not make her a joint owner (or an employee), she must by default be an independent owner of the portion of the work that she contributed, with the power—that she would not have as a joint owner or employee—to prevent the work’s exploitation. This was the corner into which *Childress* painted the *16 Casa Duse* court, and the court escaped the corner by holding that the contribution was not a copyrightable work.

The Ninth Circuit followed *Childress* in *Aalmuhammed v. Lee*, holding that a consultant who had contributed copyrightable expression to a feature film, presumably intending that it become an inseparable part of the film, was nonetheless not a joint owner because there was no evidence of the *Childress*-required intent to be a co-author.⁶ To the *Childress* requirement, the Ninth

HARMONIZATION OF TRADE SECRETS IN EUROPE AND NEW US TRADE SECRETS LAW GETS THE GREEN LIGHT—WHAT DO THESE CHANGES MEAN FOR COMPANIES IN GERMANY, THE UK, AND THE U.S.?

By [Holger Kastler](#), [Sue McLean](#), [Wolfgang Schönig](#), and [Bryan Wilson](#)



Circuit then added one of its own: that the putative co-author have “superintendence” of the work or be its “inventive or master mind”—elements more traditionally associated with works for hire than with joint works.⁷ Subsequently, in *Garcia v. Google, Inc.*, a Ninth Circuit *en banc* panel held that an actress could not claim copyright ownership of her performance in a film.⁸ The court observed that the animating concern in *Aalmuhammed* had been that defining ownership differently would “fragment copyright protection” for a unitary work “into many little pieces.”⁹

Garcia v. Google and *16 Casa Duse*, and the circuit precedent on which they respectively rely, establish categorical rules of law. But, just as the motive behind these decisions is a practical concern over fragmenting ownership into “many little pieces,” so too does a practical solution exist for bridging the lacunae in ownership created by these rules. A producer of a film or other collaborative work, concerned that its product will legally qualify neither as a joint work nor as a work for hire, may nonetheless roughly emulate these legal categories by securing assignments of copyright ownership from all of the product’s contributors and then allocating rights and liabilities among them so that the resulting network of rights and liabilities resembles those that respectively attach to joint works and works for hire. (A contributor should readily agree to such an arrangement if the alternative, as in *16 Casa Duse* and *Garcia*, is to deprive him or her of any economic stake in the creative product.) The approximation will never be perfect—unlike a true work for hire, for example, the contractual arrangement will be subject to a statutory termination of transfer—but the approximation will often suffice to achieve the business goals of all the parties to the collaborative production.

A harmonized trade secrets protection regime is coming to Europe and the U.S. Until now, the approach to trade secrets across Europe has been fragmented, with some countries having specific trade secrets legislation and others relying on unfair competition, tort, or contract law. Trade secret protection

in the U.S. has been somewhat less fragmented, as almost every state (New York and Massachusetts being notable exceptions) has adopted some version of the Uniform Trade Secrets Act (“Uniform Act”). On May 11, 2016, President Obama signed into law the Defend Trade Secrets Act (“US DTSA”), which creates a federal cause of action with substantive elements that are very similar to the Uniform Act. For practical considerations regarding the US DTSA, see our [recent publication](#).

In November 2013, the European Commission proposed a new trade secrets directive with the aim of harmonizing the law in the EU and thereby encouraging European cross-border investment, competition, and innovation. Following much debate, the “[Directive \(EU\) 2016/943 of the European Parliament and of the Council of 8 June 2016 on the protection of undisclosed know-how and business information \(trade secrets\) against their unlawful acquisition, use and disclosure](#)” (the “EU Directive”) entered into force on 5 July 2016. EU Member States must implement the EU Directive into their national laws by 9 June 2018.

In this alert, we outline the EU Directive’s key provisions and discuss its potential impact on companies operating

1 *16 Casa Duse, LLC v. Merkin*, 791 F.3d 247, 255-56 (2d Cir. 2015).

2 *Id.* at 256, 257, 260.

3 *Id.* at 256.

4 See 17 U.S.C. § 101.

5 See *Childress v. Taylor*, 945 F.2d 500, 507 (2d Cir. 1991).

6 See *Aalmuhammed v. Lee*, 202 F.3d 1227, 1232, 1235 (9th Cir. 2000).

7 *Id.* at 1235.

8 *Garcia v. Google, Inc.*, 786 F.3d 733, 740 (9th Cir. 2015).

9 *Id.* at 742.

in Europe (with a particular focus on implications for Germany and the UK). We also provide recommendations for companies doing business in Europe and compare the EU Directive with the US DTSA.

SCOPE OF THE EU DIRECTIVE

The EU Directive sets out rules on the protection against the unlawful acquisition, use, and disclosure of trade secrets. But it specifies only a minimum harmonization of trade secrets protection in the EU. In other words, while the EU Directive generally provides for uniform protection, Member States can implement higher standards. The EU Directive does not address criminal sanctions, but does provide for civil rights and remedies. Member States remain free to maintain existing criminal sanctions.

WHAT IS A TRADE SECRET?

Under the EU Directive, a “trade secret” means any information that: (i) is secret in the sense that it is not, as a body or in the precise configuration and assembly of its components, generally known among or readily accessible to persons within the circles that normally deal with the kind of information in question; (ii) has commercial value because it is secret; and (iii) has been subject to reasonable steps under the circumstances, by the person lawfully in control of the information, to keep it secret. In short, a trade secret is information that is not generally known, has commercial value and is protected by the trade secret holder to keep it secret.

This is consistent with the definition used in the World Trade Organization’s Agreement on Trade-Related Aspects of Intellectual Property Rights (“TRIPS Agreement”). Nevertheless, the “reasonable steps” requirement appears to be novel for some EU Member States, which may not have incorporated the trade secrets definition in the TRIPS Agreement into their national laws. What constitutes “reasonable steps” may vary according to the trade secret’s value, the threats faced, and the cost of particular measures and likely will be the subject of future interpretation by the Court of Justice of the European Union (“CJEU”).

Although the rights in the EU Directive are similar to intellectual property (“IP”) rights, they are not considered IP rights. This is because the European lawmakers did not want to trigger provisions of other European laws relating to IP, such as the EU IPR Enforcement Directive (2004/48/EC) and the EU Customs Enforcement Regulation ([EC] No. 1383/2003).

LAWFUL ACTS

The acquisition of trade secrets will be lawful if obtained by: (i) independent discovery or creation, (ii) reverse

engineering or (iii) any other practice which conforms with honest commercial practices.

- **Reverse Engineering:** While independent creation or discovery appears to be a universally accepted concept, in certain parts of Europe at least reverse engineering can be a contentious practice. In this context, reverse engineering of trade secrets means “*the observation, study, disassembly or test of a product or object that has been made available to the public or that is lawfully in the possession of the acquirer free from any legally valid duty to limit the acquisition of the trade secret.*” While reverse engineering may be considered fair practice in the majority of Member States, it may be considered unfair competition and thus unlawful in other countries such as Germany (*e.g.*, according to German case law, reverse engineering may be unlawful if it requires a significant investment in workforce or technology to reverse engineer a product). So, despite the exception in the EU Directive, reverse engineering of trade secrets may still be contractually prohibited in Germany at least, and possibly in other countries that choose to follow that model.
- **Workers’ Representatives:** There is an exception for workers’ representatives (*e.g.*, trade union representatives) to exercise their rights to information and consultation in accordance with EU and national law or practices.
- **Honest Commercial Practices:** The term “*honest commercial practices*” is not defined or explained in the EU Directive. If and when the CJEU provides guidance on the term, its treatment by the TRIPS Agreement likely will be relevant. The TRIPS Agreement describes “*honest commercial practices*” as “*a manner contrary to honest commercial practices shall mean at least practices such as breach of contract, breach of confidence and inducement to breach, and includes the acquisition of undisclosed information by third parties who knew, or were grossly negligent in failing to know, that such practices were involved in the acquisition.*”

In addition, the acquisition, use, and disclosure of trade secrets shall be considered lawful to the extent that such acquisition, use, or disclosure is required or allowed by EU or national law.

Exceptions: The EU Directive also provides for various exceptions.

- **Freedom of Expression and Information:** Investigative journalism was a hotly contested topic, with the media sector raising significant concerns that trade secrets arguments could be used to prevent legitimate journalistic work that would be otherwise

in the public interest. The final draft of the exception refers explicitly to the Charter of Fundamental Rights of the EU and to respect for the freedom and pluralism of the media.

- **Whistleblowers:** Another exception that triggered much debate involved whistleblowers. Under the whistleblower exception, trade secret protection does not extend to cases in which information is disclosed for the purpose of revealing relevant misconduct, wrongdoing, or illegal activity. The discloser, however, must have acted to protect the general public interest. Critics of this exception argue that it may be misapplied to an unnecessarily broad publication of trade secrets. As with other language in the EU Directive, we will likely have to wait for the CJEU to clarify what constitutes “public interest” at some point in the future.
- **Workers:** Protection does not extend to trade secrets disclosures by workers to their representatives as part of the legitimate exercise of their functions in accordance with EU or national law. Guidance in the EU Directive makes clear that the EU Directive is not intended to affect or limit the use of collective agreements regarding duties not to disclose trade secrets, provided that such agreements do not restrict the scope of exceptions in the EU Directive.
- **Legitimate Interests:** There is also an exception for “legitimate interests” recognized by EU or national law. In the absence of guidance in the EU Directive, the CJEU likely will be asked to provide further guidance in due course.

EMPLOYEE MOBILITY

The EU Directive expressly responds to concerns that it may restrict employee mobility, stating that it shall not limit “employees’ experiences and skills honestly acquired in the normal course of employment.” The uncertain boundaries of this statement, however, make future interpretation by the CJEU inevitable.

This approach appears broadly consistent with the approach taken to “residual knowledge” of employees in certain Member States (*e.g.*, the UK, see below). It also reflects the approach often taken by parties to the use of “know-how” in outsourcing and other technology agreements, *i.e.*, to include a “residuals clause.” In any case, the EU Directive explicitly states that it will not prevent employers from concluding non-competition agreements with employees. Accordingly, restrictions and non-compete clauses concerning the use of trade secrets may continue to be used by employers, subject to national law.

UNLAWFUL ACTS

- **Unlawful Acquisition:** The acquisition of trade secrets is unlawful when carried out by: (i) unauthorized access to, appropriation of, or copying of items lawfully under the trade secret holder’s control; or (ii) any other conduct considered contrary to honest commercial practices. It also is unlawful for a person to acquire trade secrets from another party if that person knew or should have known that such party was using or disclosing trade secrets unlawfully.
- **Unlawful Use or Disclosure:** The use or disclosure of trade secrets is unlawful when it is carried out by a person who: (i) has acquired the trade secrets unlawfully or (ii) is in breach of a confidentiality agreement or any other duty not to disclose or to limit the use of the trade secrets. In addition, the use of trade secrets is unlawful if the user knew or should have known that the information was obtained from another person who was using or disclosing it unlawfully. The production, offering, or placing on the market of infringing goods also is unlawful, as well as the import or export of infringing goods for those purposes, if the person using the trade secrets knew or should have known that the trade secrets were used unlawfully. “Infringing goods” are goods with a design, characteristic, functioning, manufacturing process, or marketing that significantly benefits from trade secrets which were unlawfully acquired, used, or disclosed.
- The EU Directive makes clear that direct infringement should not require proof of willful intent or gross negligence. Such proof of willful intent or gross negligence should only be required in case of indirect infringement, *i.e.*, when obtaining the trade secret from another person who acquired, used, or disclosed the trade secret unlawfully.

RIGHTS AND REMEDIES

The EU Directive grants trade secret holders a broad range of remedies that are comparable (but not identical) to those available in intellectual property cases, *e.g.*, injunctive relief, corrective measures, and damages.

- **Injunctions and Corrective Measures**
 - In terms of provisional measures, a trade secret holder’s remedies may include an injunction and the seizure or delivery of suspected infringing goods. Permanent remedies may include an injunction, corrective measures such as the recall of infringing goods, and the destruction or delivery of items containing or implementing the trade secrets. Sanctions such as recurring penalty payments are also available for non-compliance with both provisional and permanent measures.

- An infringer may request financial compensation instead of the measures listed above, if: (i) the infringer neither knew nor had reason to know that the trade secret was obtained from another person who was using or disclosing it unlawfully, (ii) the execution of other measures would cause disproportionate harm to the infringer, and (iii) financial compensation appears to be reasonably satisfactory. If applied, compensation must not exceed the amount of royalties that would have been payable if the person had requested authorization to use the trade secret. In some Member States, *e.g.*, Germany, this possibility of compensation instead of an injunctive relief or corrective measures is new.
- **Damages:** Damages should be appropriate to the actual prejudice suffered due to the infringement. Appropriate factors are the negative economic consequences, including lost profits, that the injured party has suffered and any unfair profits made by the infringer. In appropriate cases, elements other than economic factors, such as the moral prejudice caused to the trade secret holder, may be considered. Damages may be set as a lump sum on the basis of elements such as, at a minimum, the amount of royalties or fees that would have been due if the infringer had requested authorization to use the trade secrets. With respect to employees, liability for damages may be limited if the employee acted without intent.

PROTECTION OF TRADE SECRETS DURING LITIGATION

The EU Directive provides for specific measures to protect trade secrets during litigation, including restricting access to documents and to hearings. Although the laws of a few Member States allows certain *in camera* proceedings, these proceedings tend to be rare in practice. The EU Directive therefore does not foresee the use of completely *in camera* proceedings. Instead, it allows a “limited number of persons,” consisting of at least one natural person and one attorney from each party, access to otherwise confidential documents and secret hearings. These individuals are subject to a confidentiality obligation that survives termination of the proceedings.

In addition, court judgments containing confidential information will be kept confidential by removing pages containing confidential information or redacting those parts. Trade secret holders may request the publication of such a court judgment, which keeps confidential information secret but still identifies the infringer and the infringing acts. Such a request for partial publication is subject to a strict proportionality test that considers the interests of both the trade secret holder and the infringer. It remains to be seen whether the courts of the Member States will grant

such requests. In Germany, for example, motions based on a similar provision in the German Patent Act (“PatG”) are rarely granted because applicants often fail to show the required legitimate interest.

LIMITATION PERIOD

Actions for trade secret infringement must be brought within a maximum of six years, but Member States can implement shorter time periods. The six year maximum limitation period is a welcome change for trade secret holders over prior draft versions of the EU Directive (*e.g.*, the 2013 draft version, which specified a much shorter two year limitation period).

WHAT THE EU DIRECTIVE DOES NOT DO

As mentioned above, trade secrets are not considered IP under the EU IPR Enforcement Directive and the EU Customs Enforcement Regulation. Consequently, trade secrets under the EU Directive do not benefit from the mechanisms that those regulations provide for IP rights, such as pre-litigation evidence collection under the EU IPR Enforcement Directive and border measures under the EU Customs Enforcement Regulation. The EU Directive does not provide specific rules on such measures for trade secrets either, leaving a gap in their protection.

Since Member States are free to implement or maintain higher standards of protection, such gaps may be filled by the laws of the Member States. As an example, the so-called “Düsseldorf procedure” in German patent cases permits obtaining and safeguarding evidence before filing a patent infringement complaint. This procedure, which was initially established by courts in Düsseldorf, could be extended to trade secrets.

Furthermore, due to lack of legislative power on the EU level, the EU Directive also does not cover criminal sanctions. Here, too, laws of the Member States may be used to fill this gap.

IMPLICATIONS OF THE EU DIRECTIVE FOR GERMANY

Although Germany has no specific statute that comprehensively regulates the law of trade secrets, the standard of trade secrets protection in Germany is generally high. As a result, the implementation of the EU Directive into German law will likely require only minimal changes.

Trade secrets are currently protected by the Act Against Unfair Competition (“UWG”), which renders unlawful all acts contrary to honest business practices and provides for civil remedies and criminal sanctions in cases of misappropriation of trade and business secrets (*Geschäfts- und Betriebsgeheimnisse*). Additional provisions dealing

with trade secret protection are found in other statutes, including the Civil Code (“BGB”), the Criminal Code (“StGB”), the Commercial Code (“HGB”), the Employee Inventions Act (“ArbnErfG”), as well as in the Works Constitution Act (“BetrVG”).

It remains to be seen whether the German courts will place greater emphasis on the precautionary “reasonable steps” undertaken to protect trade secrets, as discussed above. The current test under German law focuses on whether the need to keep certain information secret has become apparent under the circumstances, regardless of its financial value. Moreover, since reverse engineering generally is permissible under the EU Directive, German courts may be called to revisit their position that reverse engineering is considered unlawful if it requires “substantial investment.”

Companies in Germany likely will benefit from the enhanced protection accorded trade secrets in legal proceedings. While the German Civil Procedure (“ZPO”) provides certain mechanisms to protect trade secrets during litigation, the greater protections in the EU Directive are friendlier to the trade secret holder and thus may encourage more effective rights enforcement. Furthermore, the express implementation of the rights to recall and destroy infringing goods will further enhance the trade secret holder's position under German law.

While departing employees are traditionally well protected under German law (*e.g.*, where a post-contractual secrecy obligation would unreasonably impair the departing employee's professional development), whistleblowers likely will receive better protection in Germany after implementation of the EU Directive. Lastly, it remains to be seen whether pecuniary damages under the EU Directive will replace default injunctive relief, which is typically awarded in Germany.

IMPLICATIONS OF THE EU DIRECTIVE FOR THE UK

Current UK law protects trade secrets under contract law and the laws of equity. For this reason, the EU Directive's provision of statutory trade secret protection for the first time represents a significant change to UK law – at least in theory.

In practice, however, the EU Directive is unlikely to dramatically change the law. Arguably, the test for the existence of a trade secret under the EU Directive is stricter than existing UK law, because it requires that the information is commercially valuable and that the owner must have taken reasonable steps to keep it confidential. But existing UK law also protects information with the necessary quality of confidentiality that is disclosed in circumstances importing an obligation of confidentiality and that is used without the consent and to the detriment of the owner.

As for employees, current UK law requires them not to disclose confidential information accessed during their employment. When their employment ends, confidential information should be protected indefinitely, but any residual information that has become part of an employee's skill and experience cannot generally be protected unless specified by contract. Remedies under existing law are broadly similar to those in the EU Directive, *e.g.*, damages, account of profits and injunction. Current UK law provides no criminal penalties for trade secret infringement.

IMPACT OF BREXIT!

The UK voted to leave the EU on 23 June 2016. However, until the UK Government formally provides an Article 50 notice, the UK remains part of the EU and subject to EU law and regulation. Current indications are that the UK will not provide its Article 50 notice until 2017 at the earliest and, therefore, it seems likely that the UK will still be part of the EU on 9 June 2018. Therefore, according to EU law, the UK would be obliged to implement the EU Directive into UK law prior to its formal departure from the EU. Whether the UK will decide to do so is not yet clear.

Arguably, the UK may be happy to implement the new EU Directive given that, in practical terms, it does not significantly change the level of protection given to trade secrets under UK law, and adoption of the EU Directive will help to ensure a harmonized approach to trade secret protection for UK companies that operate across Europe. Moreover, even if the EU Directive is implemented into UK law, the UK could decide to repeal or change the law in the future.

OUTLOOK TO THE U.S.: HOW DOES THE EU DIRECTIVE COMPARE WITH THE US DTSA?

The US DTSA is modeled on the Uniform Trade Secrets Act, which in its substantive terms is very similar to the TRIPS Agreement and the EU Directive. The definition of trade secrets in the US DTSA uses different wording than the EU Directive, but the scope of coverage appears to be almost identical. The specific facts of a case will continue to be critical to determining what qualifies as a trade secret under either definition.

The remedies are similar as well, for the most part. The most significant difference is that the DTSA includes a specific provision for *ex parte* seizures of trade secret information. In appropriate circumstances, this allows a victim of trade secret theft to obtain a court order, quickly and without advance notice to the defendant, to seize misappropriated trade secret information. This seizure remedy is to be used only in extraordinary circumstances and requires a series of specific findings. As a result, it is unlikely to be used often.

Like the EU Directive, the US DTSA finesses the question of enforceability of employee non-competition agreements. The Act allows restrictions on employment relationships if they are “based on evidence of misappropriation and not merely on the information the person knows.” At the same time, the Act expressly forbids injunctions that “conflict with an applicable State law prohibiting restraints on the practice of a lawful profession, trade, or business.”

Also like the EU Directive, the US DTSA provides specific protections for whistleblowers. This differs from current state trade secrets laws, and it remains to be seen how broadly these protections will be construed.

Finally, the US DTSA requires the US Attorney General to prepare biannual reports detailing or providing, among other things: the scope of theft of American trade secrets occurring outside of the United States; the extent to which those thefts are sponsored by foreign governments; a breakdown of the trade secret protections by each of the United States’ trading partners; and specific recommendations to the executive and legislative branches for reducing trade secret theft and protecting American companies. The first report is due in one year. These provisions do not change any legal requirements, but illustrate the increasing concern among US lawmakers about international trade secrets issues.

CONCLUSIONS AND RECOMMENDATIONS

The EU Directive does not radically change trade secrets law in Europe, but does help to harmonize trade secrets law across Europe with the goal of bolstering investment, innovation, and competition and reducing costs. The new rights may be particularly helpful for small and medium-sized organizations that lack the budget and resources for extensive patent protection. Nonetheless, many organizations will still want to rely on intellectual property protection where appropriate, and the EU Directive will not mean that confidentiality agreements are no longer required. Contractual rights of confidentiality will

continue to be used to enhance statutory rights under the EU Directive. In addition, because the EU Directive is a minimum harmonization law, organizations will still need to be aware of any supplemental provisions under national laws implementing the EU Directive.

To benefit from the EU Directive’s protections, companies with valuable trade secrets should begin thinking about potential changes to their processes and procedures now, ahead of the implementation deadline. In particular, we recommend that organizations:

- Carry out an audit to identify information that falls within the definition of trade secrets;
- Check that they have appropriate and adequately-documented processes to protect their trade secrets, which preferably include:
 - Marking trade secrets as confidential;
 - Granting limited access to trade secrets to different users within the organization;
 - Checking template confidentiality agreements to ensure trade secrets are adequately protected including with respect to reverse engineering of trade secrets;
 - Checking whether existing agreements adequately protect trade secrets;
 - Putting in place technical measures to avoid reverse engineering of trade secrets;
 - Checking whether information security requirements are sufficient to protect trade secrets; and
 - Reviewing employment contracts and whistleblowing policies.

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