Dispute Resolution

Tokyo Disputes Practice

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US Federal Prosecutors Actively Prosecute Electronic Trade Secret Theft

According to recent reports,[1] the theft of electronic data in the US overtook physical theft for the first time. Employers faced with this kind of employee theft often believe that their only remedy is to file a civil law suit based on a fiduciary or contractual relationship. But, in the US, an employer may also file a criminal complaint with the Department of Justice.

This article explains the legislative basis for federal prosecution of trade secret theft in the US, summarizes recent noteworthy federal prosecutions and explains the significance of these prosecutions for trade secret holders.

Legislative Background

The US federal government as well as some states have enacted statutes that specifically criminalize trade secret theft. The main Federal Legislation in this area is the Economic Espionage Act of 1996 (the "EEA"). Under the EEA, an individual who steals a trade secret for economic advantage can be imprisoned for up to ten years and fined up to $250,000 and an organization can be fined up to $5,000,000 (18 U.S.C. §§ 1832(a) and (b)). The receiver of a trade secret can also be criminally liable under the EEA if it knows that the trade secret was stolen (18 U.S.C. §§ 1832(a)(3)). A second federal statute is the Computer Fraud and Abuse Act (the "CFAA") that provides for criminal penalties where an individual gains unauthorized access to a computer to obtain something of value such as a trade secret.

1 The 2010/2011 global fraud report of Kroll, a risk consulting firm. The report is *available at* http://www.kroll.com/library/fraud/FraudReport_English-US_Oct10.pdf

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Recent Federal Prosecutions of Note[2]

High-frequency Trading Code Theft at Goldman Sachs

In December 2010, a federal jury convicted a former Goldman Sachs ("GS") computer programmer, Sergey Aleynikov, under the EEA for stealing software code related to GS' high-frequency trading operations. But Mr. Aleynikov was found not guilty of violating the CFAA because Mr. Aleynikov was authorized to access the code that he ultimately stole. The government's indictment alleged that although GS took significant measures to protect the confidentiality of its intellectual property assets, Mr. Aleynikov was able to transmit sensitive code to his home computers via email and other methods on multiple occasions. The indictment further stated that Mr. Aleynikov was planning to leave GS to join a start-up company called Teza where he would work on building a competing high-frequency trading system. Mr. Aleynikov's sentencing is scheduled for March, 2011.

High-frequency Trading Code Theft at Société Générale

In a similar case, Samarth Agrawal, a former trader at Société Générale ("SocGen"), was found guilty by a federal jury on November 19, 2010 of stealing proprietary computer code used in SocGen's high-frequency trading system. SocGen's security cameras caught Mr. Agrawal printing out hundreds of pages of code from his office at SocGen. Investigators later found the print-outs neatly organized at his home. Mr. Agrawal was negotiating with Tower Capital Research LLC ("Tower") to develop a competing high-frequency trading system for Tower along the lines of the system used at SocGen. Mr. Agrawal was arrested on the day he was supposed to start work at Tower.

Theft of Bristol-Myers Squibb Trade Secrets

According to a Department of Justice press release, Shalin Jhaveri, a former employee of Bristol-Myers Squibb, pleaded guilty on November 5, 2010 to stealing trade secrets in electronic format of his former employer in violation of the EEA. Mr. Jhaveri holds a Ph.D. from a well known Ivy League University and was employed at the time of his arrest in February 2010 as a Technical Operations Associate at Bristol-Myers Squibb. Mr. Jhaveri allegedly downloaded gigabytes of confidential data to his personal hard drive and took the data out of the company. At the time of his arrest by the FBI, Mr. Jhaveri was meeting in a Syracuse hotel room with an FBI informant he believed was an investor willing to finance a business venture that Mr. Jhaveri planned to start in his native India.

Theft of Ford Motor Company Trade Secrets

A Chinese citizen and former Ford employee, Xiang Dong Yu, pled guilty on November 17, 2010 to stealing Ford trade secrets. Mr. Yu was a Product Engineer for Ford from 1997 to 2007 and had access to Ford trade secrets during his employment. Before quitting Ford, Mr. Yu copied 4,000 Ford documents onto his external hard drive. Mr. Yu eventually became employed by Beijing Automotive Company, a competitor of Ford. The FBI arrested Mr. Yu when he returned to the US in 2009. When the FBI searched the Beijing Automotive Company laptop computer in Mr. Yu's possession, they found forty-one Ford design specifications. Under Mr. Yu's plea agreement, Mr. Yu faces a sentence of between 63-78 months' imprisonment, a fine of up to $150,000, and deportation.

Conclusion

When a company realizes that it has been the victim of trade secret theft in the US, in addition to considering a civil law suit, the company should consider the merits of contacting the Department of Justice about prosecuting the thief and possibly the company that hired the thief. A successful criminal prosecution sends a strong message to unethical employees and competing companies that there are serious consequences to stealing trade secrets. Conversely, to avoid accusations of trade secret theft, it is important for companies hiring laterally to conduct due diligence on their potential hires and require new hires to sign a statement that they are not bringing on board any trade secrets from their former employers.[3]

Making "Sealed Offers" in International Arbitration to Cap Liability for Costs

The costs of international arbitration can be considerable. The "sealed offer" provides a potential mechanism for capping those costs. This article briefly outlines some tips to consider in making a "sealed offer."

The Award of Costs in International Arbitration

An award of costs in international arbitration will be at the discretion of the arbitral tribunal, regulated only by the specific language of the arbitration clause and any applicable institutional arbitration rules. However, the most commonly used institutional arbitration rules impose a positive obligation on the tribunal to make an award on costs. Further, there is a general expectation that the legal and other costs of the successful party

2 Press releases from the Justice Department can be found at the following link http://www.justice.gov/criminal/cybercrime/ipnews.html

3 In 2008, HP was faced with this very problem when a lateral hire from IBM circulated IBM pricing data inside HP. HP avoided possible criminal liability by cooperating with IBM and the Department of Justice. On the other hand, the employee was prosecuted for trade secret theft.

will form part of the award on costs, with the unsuccessful party being ordered to compensate the successful party for its reasonable legal and other costs.

Three approaches to awarding costs have been observed in ICC arbitration: first, to order the losing party to bear all of the costs; second, to allocate costs in proportion to the outcome of the case, taking into account the relative success of each claim; and third, to require that the costs be shared equally by the parties or that each party bears its own costs. Nevertheless, several international arbitration practitioners have observed an emerging trend in favor of the first approach.

In light of this, parties to international arbitration who are at risk of receiving an unfavorable award must look for a means by which they can cap their potential costs liability. One potential solution is the "sealed offer."

The "Sealed Offer"

A "sealed offer" (often referred to as a "Calderbank letter" or "Calderbank offer") is a written offer to settle a dispute which has been referred to arbitration, made "without prejudice save as to costs." What distinguishes the sealed offer from an ordinary offer to settle a dispute, is the cost penalty (in respect of which see below) which the arbitral tribunal is expected to attach to it, against the offeree who does not accept the offer and fails subsequently to achieve a more favorable award by continuing the proceedings (i.e., "to beat the offer").

The offer is "sealed" and "without prejudice" because it is not to be brought to the attention of the arbitral tribunal before the determination of the substantive dispute, in case it influences the decision of the tribunal with regard to the merits of the substantive case. However, in order that the offer can be taken into account in assessing liability for costs, it must be brought to the attention of the arbitral tribunal before the tribunal makes a determination on costs, hence the words "save as to costs."

The Use of a Sealed Offer in International Arbitration

The sealed offer derives from English law and the practice of the English courts and arbitral tribunals in allocating costs whereby, as a general rule, the party considered to be the overall loser is ordered to pay the costs of the proceedings and the reasonable legal and other costs of the overall winner, as well as any sum awarded on the merits. This has been described as the "loser pays all" or "costs follow the event" principle and is generally followed even where the loser has defeated the winner on a number of points and the recovery of the latter is significantly less than the amount originally claimed, so long as the recovery is for more than a nominal amount.

The sealed offer alleviates the general rule on costs in England by displacing the "loser pays all" principle when the winner has failed to beat the offer (in other words, where it would have recovered the same or more by accepting the offer). In such an eventuality, the winner will generally be held liable for the loser's costs incurred after the time when the offer could have been accepted. Accordingly, the offeror can seek to place a ceiling on its potential costs liability in respect of the period following the offer, by offering to settle the offeree's claims (or certain of them) for such amounts as it sensibly believes the tribunal would award in respect of those claims, if the proceedings were not settled.

Common law jurisdictions which follow the English approach towards allocating costs, most notably Hong Kong, Australia and Canada, also give cognizance to the use of sealed offers to counterbalance the potentially unfair effect of their approach towards awarding costs. It is submitted that such a mechanism is crucial in any forum where costs are awarded in accordance with the English principle that "costs follow the event"; international arbitration, where this principle is increasingly followed, is one such forum. Anyone conducting international arbitration that has some connection with England, Hong Kong, Australia or Canada, should certainly use the sealed offer procedure where appropriate to contend with the potential application of the general rule on costs normally followed in those jurisdictions.

This is the first part of an article written by Poupak Anjomshoaa in *International Disputes Quarterly* (Winter 2008), *available at* http://www.whitecase.com/idq/winter_2008_tips/. The second part, on tips for making the sealed offer, will be published in the next issue of this newsletter.

Provisional Attachment Orders in Japan

Introduction

Civil procedure in Japan permits litigants to petition courts for various forms of provisional relief. Under certain circumstances, the courts will grant provisional attachment orders to litigants. A provisional attachment order prevents the target recipient (e.g., bank account, accounts receivable, etc.) of the order from transferring or disposing of assets belonging to the respondent pending resolution of the petitioner's claims by settlement or final judgment.

Purpose

The purpose of provisional attachment is to prevent a defendant from hiding or disposing of assets to avoid satisfying a future court judgment.[1] The attachment secures execution of a future judgment on a monetary claim. A petition for provisional attachment is typically filed before the plaintiff's law suit, but a petition may also be filed after the lawsuit is filed.

The Petition

To petition for provisional attachment, the petitioner must submit to the court (1) a written petition and (2) sufficient evidence supporting the petitioner's claim. These documents should be written in a simple persuasive manner and all assertions should be clearly linked to the evidence that the petitioner submits. The courts typically require Japanese translations of foreign language documents submitted in the proceeding.

Burden of Proof and Persuasion

A provisional attachment order is an extraordinary measure. In making a determination on whether to issue a provisional attachment order, the court carefully scrutinizes the petition. In reviewing a petition, the court demands convincing evidence supporting the claimed damages. While the burden can be difficult to carry, especially in complex cases, the required showing to obtain a provisional attachment order is lower than the show required to prevail at trial on the merits.

An application for provisional attachment must be based upon a reasonable apprehension that a favorable judgment for the applicant would lose its practical effect unless provisional attachment is ordered. In other words, the petitioner must convince the judge (1) that there is a high probability that the petitioner has a valid claim against the respondent, and (2) that freezing the respondent's assets is necessary to ensure that the respondent will be able to satisfy a potential damages award in the future.

Procedure

A petition for provisional attachment is heard ex parte by the court. The hearing is generally scheduled to take place during the court's next available slot for hearings on provisional matters. The evidence supporting the petitioner's claim must be available for immediate review. The court interviews counsel for the petitioner to determine whether the petitioner has met the burden required to obtain a provisional attachment order. The respondent is not present to defend itself. But the court often requires the petitioner to anticipate defenses that the respondent could raise (e.g., the claim has been satisfied, is subject to setoff, is legally deficient, etc.) and explain why such defenses fail.

Security Bond

If the court is satisfied that sufficient grounds for granting the petition exist, the court will issue a writ of provisional attachment to the specified recipient targets. As a condition to issuing the writ, the court will require the applicant to furnish a security bond. In our experience, the amount of the bond is typically based on a percentage of the value of the target of the attachment. The amount of the bond may also be based on a sliding scale such that the greater the likelihood of success on the merits the petitioner demonstrates, the assessed amount of the required bond decreases. Based on our experience, the amount of the bond could equal twenty to thirty percent of the target asset.

Effect

Once the bond is posted, the clerk of court will serve the writ on the recipient targets of the provisional attachment. Since the clerk serves the writ, the petitioner is not capable of controlling the exact timing of service. The writ prohibits the recipient targets from transferring assets (covered by the provisional attachment order) to the respondent.

At the request of the petitioner, the recipient targets are required to provide to the petitioner an acknowledgment of the existence of assets belonging to the respondent, within two (2) weeks of the date of service of the order. As a practical matter, the Tokyo District Court generally requires petitioners to request such acknowledgments from the recipient targets. The acknowledgement must also identify the assets and state whether the recipient intends to encumber the assets and, if not, to state the reason why. The court notifies the respondent after the writ has been served on the recipient targets. The applicant may execute on the writ only after obtaining a final judgment in the main action.

Irrespective of whether the recipient targets are in possession of any assets belonging to the respondent, receipt of an attachment order likely will negatively impact the respondent's relationships with the recipient targets and potentially disrupt the respondent's business by casting doubt on the respondent's financial stability. At minimum, the respondent will be forced to explain the facts and circumstances surrounding the attachment order to the recipient targets. Moreover, under most commercial agreements, receipt of an attachment order is an event of default.

Conclusion

Respondents are generally eager to disencumber assets subject to provisional attachment and to avoid the time and expense of litigating a subsequent lawsuit which would likely follow absent settlement. Hence, this strategy aims to achieve a relatively quick resolution through settlement.

1 Provisional remedies, including provisional attachment, are regulated by the Civil Provisional Remedies Law of 1989 and the Civil Provisional Rules of 1990.

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