

Where We Are In The US Trade Secret Crackdown On China

By **David Laufman, Joseph Casino and Michael Kasdan** (May 29, 2020)

China is the world's second largest economy and one of the United States' largest trading partners. Successful collaboration between U.S. and Chinese companies on development and manufacturing has become the norm (look no further than the iPhone).[1]

At the same time, the theft of U.S. companies' trade secrets and other intellectual property by Chinese entities has increased dramatically.[2] The threat environment confronting U.S. industry consists of cyber intrusions, employee theft, and commercial collaborations, as well as economic espionage perpetrated by or on behalf of the Chinese government.[3]

Today, the crackdown by the U.S. Department of Justice on national security threats from China — launched in late 2018 and branded as the DOJ's China Initiative — continues at full throttle. Led by the DOJ's National Security Division, the China Initiative has multiple objectives, but its lead goal is to "[i]dentify priority trade secret theft cases, ensure that investigations are adequately resourced, and work to bring them to fruition in a timely manner." [4]

When it comes to the criminal prosecution of trade secret theft, the focus on China is understandable. According to a March 2020 DOJ report, "[a]bout 80 percent of all economic espionage prosecutions ... allege conduct that would benefit the Chinese state, and there is at least some nexus to China in around 60 percent of all trade secret theft cases." [5]

The technology road map for China's theft of intellectual property is hiding in plain sight in the "Made in China 2025 Notice," a 10-year advanced technology modernization plan issued by China's State Council in 2015. This government plan identifies 10 strategic manufacturing industries for promotion and development in China: (1) robotics and automated tools; (2) biotechnology; (3) next-generation information technology; (4) advanced rail equipment; (5) aircraft and aircraft components; (6) agricultural machinery and equipment; (7) clean energy vehicles; (8) maritime vessels and marine engineering equipment; (9) electrical generation and transmission equipment; and (10) so-called new materials, such as polymers.

Chinese companies are moving full steam ahead. The Nikkei Asian Review published an engaging interactive chart showing the shocking progression of China in patent filings over 20 years for nine out of 10 technical categories they reported on — consistent with the Chinese government's goals to be an owner and developer of technology rather than a cheap resource for non-Chinese companies.[6] The monumental efforts from China's industry to meet its government's dictate for advancement led China to be the source of the most patent applications in the world in 2019, ending a four-decade place at the top for the United States.[7]

But certain Chinese companies are also pursuing technological advances by nefarious means. Indeed, the increase in alleged trade secret misappropriation by Chinese companies likely stems from pressure from the Chinese to become a global technology leader. The



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mechanisms by which China purloins U.S. technology make it difficult, if not impossible, for American companies to protect their vital intellectual property.

According to the Office of the Director of National Intelligence, China uses every lever of national power to acquire technology and to accelerate the fulfillment of its strategic plan, including:

- Its civilian and military intelligence agencies;
- Front companies, designed to obscure the hand of the Chinese government;
- Nontraditional collectors, such as scientists and businessmen;
- Recruitment programs such as the Thousand Talents Program, an initiative to identify foreign experts to return to China and work on key strategic programs;
- Joint ventures, historically used as a vehicle to forcibly acquire technology and know-how;
- Mergers and acquisitions, in which China seeks to buy companies that have sought-after technologies, facilities, and people with relevant expertise;
- Research partnerships, where China actively seeks partnerships with government laboratories to learn about and acquire specific technology, and the skills necessary to run such facilities; and
- Academic collaborations where China exploits the openness of American academia through collaborations and relationships with universities to acquire specific research and gain access to high-end research equipment.

The threat vectors through which China predominantly has stolen U.S. intellectual property include cyber intrusions into the computer networks of American companies, as well as malicious insiders with access to proprietary information or data. Trade secret lawsuits concerning Chinese companies reflect the theft of U.S. intellectual property not only from economic espionage and computer hacking but also from joint ventures, movement of

employees, and other collaborations in business, research and academia.

Since the beginning of the China Initiative, the DOJ has brought eight federal prosecutions involving China for economic espionage (the theft or misappropriation of a trade secret for the benefit of a foreign government, instrumentality, or agent), trade secret theft, or conspiracy to commit economic espionage or trade secret theft. A ninth DOJ prosecution involving China did not allege the theft of a trade secret but charged the defendant with smuggling vials of biological research stolen from a medical laboratory in Boston.

The most recent federal criminal prosecution for economic espionage illustrates both the breadth of China's targets, as well as the challenges of defending against the state-sponsored theft of intellectual property.

In February 2020, the DOJ obtained the indictment of four members of the Chinese People's Liberation Army for hacking into the computer systems of the credit reporting agency Equifax and stealing Equifax's trade secrets, as well as the personal data nearly 150 million Americans. The government charged the defendants with conspiracy to commit economic espionage, as well as a substantive count of economic espionage, in addition to computer fraud, unauthorized access and intentional damage to a protected computer, and multiple counts of wire fraud. The trade secrets alleged to be stolen consisted of Equifax's data compilations and database designs.

U.S. companies are not relying completely on DOJ enforcement actions to protect their valuable trade secrets. They are also filing private civil lawsuits in U.S. federal courts, relying on both the Defend Trade Secrets Act and state trade secret laws to pursue international bad actors. The DTSA, which in 2016 established a civil remedy for the misappropriation of trade secrets, featured prominently in the recent case of *Austar International Limited v. Austarpharma LLC*.^[8]

In *Austar*, the plaintiff brought claims for breach of fiduciary duty, breach of operating agreement, conversion, violation of the DTSA, misappropriation of trade secrets, tortious interference with prospective economic advantage, and judicial expulsion against a U.S. company that the plaintiff was member of, a Chinese pharmaceutical company, and Rong Liu. Liu, a New Jersey resident, was alleged to have stolen the plaintiff's trade secrets for the benefit of his companies in China.

The U.S. District Court for the District of New Jersey refused to dismiss these claims, except the conversion claim, and declined to stay the action in favor of a similar lawsuit that had been brought in China, reasoning that the DTSA claims could not be brought in China..

The *Austar* complaint describes co-defendant Liu starting a Chinese company, poaching employees, filing patents on technology developed by the U.S. company, and misappropriating its trade secrets. This use of the DTSA by a private litigant in the United States illustrates how private civil actions can be utilized in trade secret theft. However, one advantage for the *Austar* plaintiff was easily obtained personal jurisdiction over the U.S.-based defendants.^[9]

Federal courts are also rendering favorable verdicts on behalf of private U.S. plaintiffs alleging the misappropriation of intellectual property to China under applicable state trade secrets laws. For example, on March 31 the U.S. District Court for the Western District of Pennsylvania denied the defendants' motion to set aside the entry of a default judgment under the Pennsylvania Uniform Trade Secrets Act in *PPG Industries Inc. v. Jiangsu Tie Mao Glass Co. Ltd.*^[10]

In PPG, the parties were competitors in the glass manufacturing industry. PPG alleged that defendants colluded with a former PPG employee to misappropriate its proprietary manufacturing processes. After learning of the scheme, PPG alerted the FBI, which arrested and charged the former employee. PPG sued Jaingsu Tie Mao Glass, as well as its CEO and purchasing agent, asserting claims under the Pennsylvania Uniform Trade Secrets Act, state tort and contract claims, as well as Racketeer Influenced and Corrupt Organizations Act claims. The defendants were served under the Hague Convention, but did not answer the complaint.

After third-party discovery, PPG moved for default judgment, which the court granted. The defendants then entered an appearance and opposed. The court, after finding it had personal jurisdiction over the defendants, found that the information that plaintiff's former employee gave to defendants clearly fell within the statutory definition of a trade secret and that defendants' conduct — including approving making a payment to PPG's former employee for the confidential information — constituted misappropriation. The court also granted PPG's request for maximum exemplary damages, permanent injunctive relief and attorney fees.

Companies have also sought to combat foreign trade secret misappropriation by bringing trade secret claims at the U.S. International Trade Commission. Even non-U.S. companies seeking to protect their trade secrets have used this procedural pathway.

For example, in a fight between two Korean goliaths, LG Chem Ltd. and its U.S. subsidiary, LG Chem Michigan Inc. filed a petition before the ITC seeking an investigation into an alleged massive misappropriation of LG Chem's trade secrets by SK Innovation Co Ltd., SK Battery America Inc. and SK Battery Hungary Kft. Based on SK Innovation allegedly improperly poaching LG Chem's employees and their subsequent disclosure of LG Chem's trade secrets to SK Innovation, LG Chem sought to stop importation of lithium ion batteries and specialized equipment to a plant being constructed by SK Innovation in Georgia.[11]

This shows that the ITC — with its fast-moving docket and broad remedial powers — may be an auspicious forum for enforcement against foreign entities who steal trade secrets and later try to exploit the U.S. market.

Companies are also serving as important sources of information for the DOJ. Indeed, Jay Bratt, Chief of DOJ's Counterintelligence and Export Control Section, recently told Global Investigations Review that the "vast majority" of investigations that resulted in recent trade secret theft prosecutions were triggered by on tipoffs from U.S. private sector companies:

They come from when industry notices anomalous behavior on its networks, when they see people sending what appeared to be proprietary information to personal email accounts or doing very large downloads right before they retire or leave the company. And it's through industry cooperation, that we're able to move forward and bring a case.

The DOJ attributes this, in part, to U.S. companies becoming better educated about the threat and methods of China-led economic espionage.

The January 2020 trade agreement with China reflects a U.S. effort to mitigate the problem of trade secret theft and the forced transfer of intellectual property. China agreed "to ensure effective protection for trade secrets and confidential business information and effective enforcement against the misappropriation of such information." [12] The agreement

prohibits every manner of trade secret misappropriation, including "electronic intrusions."

China also has agreed to end the practice of forcing or pressuring foreign companies to transfer their technology to Chinese companies as a condition for obtaining market access, administrative approvals or receiving advantages from the government. Given China's failure to abide by prior commitments to cease the theft of U.S. intellectual property, including the September 2015 agreement obtained by the Obama administration, there is reason for healthy skepticism regarding China's effective or sustained compliance with the new agreement.

U.S. companies therefore should ensure that they are maintaining robust computer network defenses and insider threat programs, alertness in their commercial collaborations with Chinese companies, and, if theft nonetheless occurs, be prepared to undertake civil or administrative litigation.

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[1] <https://www.cnbc.com/2019/09/23/chinese-theft-of-trade-secrets-is-on-the-rise-us-doj-warns.html>

[2] <https://www.justice.gov/opa/pr/chinese-national-sentenced-stealing-trade-secrets-worth-1-billion>

[3] <https://www.wsj.com/articles/an-after-hours-company-visit-spurs-espionage-charges-1505813401>

[4] <https://www.ipwatchdog.com/2020/02/09/china-initiative-combating-economic-espionage-trade-secret-exfiltration/id=118646/>

[5] <https://www.justice.gov/opa/page/file/1223496/download>

[6] <https://vdata.nikkei.com/en/newsgraphics/patent-wars/>

[7] <https://www.reuters.com/article/us-usa-china-patents/in-a-first-china-knocks-u-s-from-top-spot-in-global-patent-race-idUSKBN21P1P9>

[8] *Austar International Limited v. AustarPharma LLC et al.*, 2019 WL 6339848 (D.N.J. Nov. 27, 2019).

[9] *Compare Celgard, LLC v. Shenzhen Senior Technology Material Co. Ltd.* (US) Research, 2020 WL 1548513 (N.D. Calif. Mar. 5, 2020) (finding Chinese company not subject to personal jurisdiction even though it was alleged trade secrets were obtained from U.S.-based former employee of plaintiff).

[10] *PPG Industries, Inc. v. Jiangsu Tie Mao Glass Co., Ltd.*, PICS Case No. 20-0392

[11] <https://www.wiggin.com/publication/wiggin-and-dana-partners-kenneth-cho-and-michael-kasdan-co-author-article-for-iam/>

[12] <https://ustr.gov/countries-regions/china-mongolia-taiwan/peoples-republic-china/phase-one-trade-agreement/text>