Winter 2012

Beneficiaries of Misconduct: A Direct Approach to IT Theft

Andrew Popper, *American University, Washington College of Law*

Forthcoming: Marquette Intellectual Property Law Review
Winter 2012

Beneficiaries of Misconduct: A Direct Approach to IT Theft

Andrew F. Popper[1]

Professor of Law
American University, Washington College of Law
4801 Massachusetts Ave., NW
Washington, DC 20016
apoper@wcl.american.edu

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[1] Professor of Law, American University, Washington College of Law. Thanks are due Dean Claudio Grossman for his support and to law students Lucia Rich Miras, Melissa Kim, Jana Pariser, and Jonathan R.K. Stroud for their hard work and dedication in the preparation of this piece. Thanks are due also to Microsoft Corporation for support and assistance.

Summary

Stolen information technology (IT) is a domestic and global problem. Theft of IT by upstream producers has a pernicious effect on the competitive market and violates fundamental policies designed to protect those who create and invent such assets. Companies profiting from stolen IT are not just free-riding on the successes of those who design and produce the products and ideas that are a driving force in the U.S. economy – they are destabilizing rational pricing and distorting lawful competition by virtue of outright theft. Current legal recourse is insufficient to address such misconduct; new approaches are needed at the state and federal level. The Federal Trade Commission has, and should exercise, its authority to sanction IT theft. At the state level, legislation along the lines of the recently passed Washington statute holds out the promise of accountability for significant misconduct, fairness in pricing, a level and vibrant

competitive playing field, and the hope for the production of better and more efficient goods and services.

I. Introduction: The Impact of Stolen IT on Competition

Almost a century ago, the Supreme Court declared that the prohibition against unfair competition serves to protect fundamental values and important rights. "[T]he right to acquire property by honest labor or the conduct of a lawful business is as much entitled to protection as the right to guard property already acquired. . . . It is this right that furnishes the basis of the jurisdiction . . . of unfair competition."[2] The idea is simple: it is unfair to competitors and inconsistent with basic notions of market competition to allow market actors to steal the work or property of another and use that asset to obtain a competitive advantage over companies that play by the rules.[3] There are a number of settings, however, where current legal recourse is insufficient to address such misconduct, particularly when the item taken is information technology (IT).[4]

The idea that a competitor can steal and benefit from the property of a rival or other company for commercial gain is at odds with basic notions of efficiency and fair play.[5] Professor Glen Robinson states the matter precisely: "Our concept of competition is based on a regime of

[2] *Int'l News Serv. v. Associated Press*, 248 U.S. 215, 236-37, 240 (1918) (stealing information from the bulletin postings of a competitor is an act of unfair competition).

[3] RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 38 cmt. b (1995) (endorsing a remedy against an "unethical" competitor who profits from the highly valuable initial labor and investment of another but does not pay for that benefit).

[4] *See Intermountain Broad. & Television Corp v. Idaho Microwave, Inc.*, 196 F. Supp. 315, 322-24 (D. Idaho 1961) (plaintiffs should "make a case for protection under copyright law, statutory or common law," instead of common law misappropriation).

[5] Glen O. Robinson, *On Refusing to Deal with Rivals*, 87 Cornell L. Rev. 1177, 1191 (2002).

exclusive property rights. . . . Competitors are supposed to compete with their own property, not with the assets of their competitors. . ."[6] Robinson cites the "common law doctrine of 'unfair competition,' which prohibits firms from helping themselves to a competitor's property."[7] Although Robinson focuses on a company's theft of a *competitor's* property, the competitive harm is similar even where the stolen property belongs to a third party, since the recipient of the stolen property still obtains an advantage over its competitors to which it is not entitled and by means of an illegal act. This is as true with IT as it is with any other valuable asset and raises the basic question that is the focus of the research: What is the best way to address the enormous problems associated with theft of IT?

One approach to the theft of IT might, in appropriate circumstances, be to consider the misconduct a form of unfair competition or an unfair trade practice.[8] In the common sense understanding of the phrase, such practices are misappropriations[9] that might not always be actionable under conventional intellectual property regimes, particularly when the misappropriation occurs outside the territory of the regulating jurisdiction.[10] Moreover, intellectual property laws are designed to protect intellectual property *owners*; for the most part, no redress is provided for third parties suffering an independent competitive harm. To be blunt,

[6] Id. at 1191.

[7] Id.

[8] Paul B. Stephan, *American Hegemony and International Law: Sheriff or Prisoner? The United States and the World Trade Organization*, 1 Chi. J. Int'l L. 49, 59 (2000) ("The government needs to know about misbehavior by importers, such as theft of intellectual property or other unfair trade practices. . . .").

[9] *See Intermountain Broad. & Television Corp v. Idaho Microwave, Inc.*, supra note 4 (the remedy for such theft may lie in copyright or other common law claims but not in the common law of misappropriation.).

[10] On common law misappropriation, see Edmund J. Sease, *Misappropriation is Seventy-Five Years Old; Should We Bury It or Revive It?*, 70 N. DAK. L. REV. 781 (1994); Note, *Nothing But Internet*, 110 HARV. L. REV. 1143 (1997); Leo J. Raskind, *The Misappropriation Doctrine as a Competitive Norm of Intellectual Property Law*, 75 MINN. L. REV. 875, 882 (1991).

beneficiaries of the theft of IT secure an unjustified cost savings over their law-abiding competitors and are unjustly enriched.[11]

If a manufacturer steals software or other IT instead of paying for it, its input costs are reduced as compared to its competitors that pay for their IT. In cases where the company using stolen IT is a contract manufacturer, that cost advantage may accrue at least in part to the firm that hired the company to manufacture the goods on its behalf (i.e., the "hiring firm"). The result is an uneven playing field, rewarding thieves and their customers and penalizing those who respect the rule of law and follow best practices in terms of paying for their information technology and other key inputs.

These indirect yet undoubtedly damaging effects of IT theft have recently been the target of attention by numerous state Attorneys General and state legislatures. Over the past two years, Washington State and Louisiana have enacted laws designed to address the competitive harms arising from the use of stolen IT by manufacturers. These statutes, discussed in the body of the paper, authorize the state Attorney General (and, in the case of Washington State, injured manufacturers) to obtain redress for these competitive harms.[12] More recently, Attorneys General from 36 states and three U.S. territories issued a letter urging the Federal Trade Commission to attack this problem under Section 5 of the FTC Act and committing to exploring their ability to seek remedies under their respective state laws.[13] These and related developments

[11] For a discussion of unjust enrichment, see Peter Birks, *Unjust Enrichment and Wrongful Enrichment*, 79 Tex. L. Rev. 1769 (2001).

[12] 2011 Wash. Leg. Serv. Ch. 98 (codified at Wash. Rev. Code §§ 19.330.010-.100); 2010 La. Sess. Law Serv. Act 74 (codified at La. Rev. Stat. § 51:1427).

[13] Letter from the National Association of Attorneys General to the Federal Trade Commission (Nov. 4, 2011), http://www.naag.org/assets/files/pdf/signons/FTCA%20Enforcement%20Final.PDF.

signify a heightened awareness among lawmakers and law enforcement authorities of the close linkage between respect for property rights, fair competition, innovation, and economic growth in the global economy.

The values at stake are significant. In recent years, the reduction of tariffs and dismantling of trade barriers created opportunities for businesses, but pressured manufacturers to become more productive, in part by investing in sophisticated IT systems to increase profitability, with the hope that these expenditures will pay off through increased efficiencies.

Where, however, firms steal IT in order to gain a cost advantage, merit-based success in the marketplace is at risk and the motivation to create better and more efficient goods and services is in jeopardy. As Professor Robinson notes, "[a]n incentives problem is created any time one firm is permitted to free-ride on a competitor's investments, whether those investments are represented by tangible assets or intellectual property."[14] That formulation captures succinctly the set of legal, competitive, and ethical problems under review in this article.[15]

Stolen IT is a global problem that results in massive costs and has a severe economic impact. The estimated value of stolen software around the world in 2009 was $51.4 billion.[16] In 2010, it

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[14] Robinson, supra note 5, at 1210.

[15] Michael Deutch, *Unfair Competition and the "Misappropriation Doctrine" – A Renewed Analysis*, 48 St. Louis L.J. 503, 512 (2004) ("It is almost a tautology to state that unfair competition is morally improper. "Unfair" means valueless."); See 19 U.S.C. § 1677(b) (1988), ("antidumping" legislation addressing when a foreign competitor's domestic price was "fair" or if the competitor was "dumping" the item in the U.S. market and thus securing an undue competitive advantage).

[16] Seventh Annual BSA/IDC Global Software 09 Piracy Study 2 (May 2010); see also Stephen E. Siwek, *The True Cost of Copyright Industry Piracy to the U.S. Economy, Inst. for Pol'y Innovation* (Oct. 3, 2007), http://www.ipi.org/ipi/IPIPublications.nsf/PublicationLookupFul llText/23F5FF3E9D8AA7 9786257369005B0C79 (studies show a $ 58 billion loss from IP piracy).

was $58.8 billion, a 14% increase.[17] Moreover, "the global PC software piracy rate rose in 2009 to 43%, up two percentage points over the previous year. This means that for every $100 worth of legitimate software sold in 2009, an additional $75 worth of unlicensed software also made its way into the market."[18]

Although some IT theft is the result of criminal enterprize, most is conventional unauthorized copying -- piracy -- by individuals and commercial entities.[19] In a survey conducted in emerging markets, 51% of the respondents (individuals and business) stated that they thought it was *lawful* to pirate or copy software.[20] Further compounding the problem is the fact that the rate of IT theft is highest in some of the same countries that today account for a large share of global manufacturing.[21] The National Association of Attorneys General notes that software piracy rates in some of America's largest trading partners exceed 80-90%.[22]

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[17] Eighth Annual BSA/IDC Global Software 2010 Piracy Study 2 (May 2011).

[18] Seventh Annual BSA/IDC Global Software 09 Piracy Study 2 (May 2010). For comparison, a 2004 study showed the value of all counterfeited and pirated goods, internationally, to be $500 billion. *Commission on Intellectual Property, International Chamber of Commerce*, Doc. No. 450/986, The Fight Against Piracy and Counterfeiting of Intellectual Property (June 7, 2004); see generally *Organization for Economic Co-operation and Development, 2007. The Economic Impact of Counterfeiting and Piracy (Executive Summary*), http://www.oecd.org/dataoecd/13/12/38707619.pdf.

[19] Chun-Hsien Chen, Explaining Different Enforcement Rates of Intellectual Property Protection in the United States, Taiwan, and the People's Republic of China, 10 TUL. J. TECH. & INTELL. PROP. 211, 215-16 (2007) (discussing comparatively the culture of copying in the U.S. and Asia); Daniel C.K. Chow, Why China Does Not Take Commercial Piracy Seriously, 32 Ohio N.U.L. Rev. 203, 213 (2006) ("It is no exaggeration to say that many in China believe that they can engage in the theft of intellectual property with impunity. . . . This creates a widespread business culture that tolerates, or even encourages, unauthorized copying and theft of intellectual property. The culture of copying is so pervasive that even many of China's most successful legitimate companies treat it as a part of doing business.");

[20] Id., Eighth Annual BSA/IDC Study, supra note17, at 2.

[21] Id.

[22] Letter from the National Association of Attorneys General to the Federal Trade Commission (Nov. 4, 2011), http://www.naag.org/assets/files/pdf/signons/FTCA%20Enforcement%20Final.PDF.

It has become evident that "[c]ompanies that do not pay for the [software] programs they use to run their operations have an unfair cost advantage over companies that do, which skews competition."[23] As an OECD report notes:

> Counterfeiting and piracy have economy-wide effects: (i) innovation is undermined, (ii) criminal networks gain financially, (iii) the environment is negatively affected, (iv) workers are worse off. Moreover, in countries where counterfeiting and piracy is widespread, (v) foreign direct investment may be lower and (vi) the structure of trade may be affected.[24] . . . Rights holders experience: (i) lower sales volume and prices; (ii) damaged brand value and firm reputation; (iii) lower royalties, (iv) less incentive to invest in new products and processes, (v) higher costs, because of spending on efforts to combat counterfeiting and piracy, and (vi) potential reduction in the scope of their operations.[25]. . . Consumers acquiring counterfeit or pirated products, whether knowingly or unknowingly, (i) may be exposed to elevated health and safety risks, and (ii) could experience lower consumer utility due to generally lower quality of infringing products.[26]. . . Effects of counterfeiting and piracy on government come in the form of (i) lower tax revenues, (ii) the cost of anti-counterfeiting activities, including responding to public health and safety consequences and (iii) corruption.[27]

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[23] Eighth Annual BSA/IDC Study, supra note_17, at 4.

[24] OECD, supra note 18, at 17.

[25] Id. at 18.

[26] Id. at 19.

[27] Id. at 20.

While most studies on IT theft have focused on the direct harms to IT owners and to governments due to reduced private-sector investment and lower tax revenues, little attention has been paid to the indirect harms that IT theft may impose on competitors who incur the full costs of any IT they use. Often, these competitive harms are "hidden" by the fact that the victims have no idea that their competitors are breaking the law in order to gain a competitive edge.

II. Addressing IT Theft Under Existing Legal Regimes

Given the economic impact of IT theft including its potential impact on competition, it is worth exploring whether this problem can be addressed under existing legal regimes such as the Federal Trade Commission Act (FTCA), state unfair competition laws, and international trade law.

A. Federal Trade Commission Act

Section 5 of the FTCA gives the agency power to issue rules, publish guidelines, and initiate enforcement proceedings to address "unfair methods of competition" and "unfair or deceptive acts or practices".[28] The Federal Trade Commission (FTC) should exercise that power to address IT theft.

In empowering the FTC to act against "unfair methods of competition," Congress gave the agency broad and flexible authority to ensure the fairness of the competitive process.[29] In

[28] 15 U.S.C. § 45 (2006), referred to as Section 5 of the Federal Trade Commission Act and embodies both consumer protection and unfair competition authority.

[29] The Senate report explains that Congress left it to the FTC "to determine what practices were unfair" because "there were too many unfair practices to define, and after 20 of them into law it would be quite possible to invent

recognition of the expanse of this authority, the Supreme Court held that the FTC is authorized to "consider[] public values beyond simply those enshrined in the letter or encompassed in the spirit of the antitrust laws."[30] In 1989, senior FTC attorney James F. Mongoven described the expanse of Section 5 of the FTCA as follows:

> Section 5 reaches some classes of behavior beyond those prohibited by the Sherman and Clayton Acts. Section 5 also condemns business torts -- that is, actions that injure a competitor through reasons other than competition on the merits, or a superior ability to satisfy consumer demands. The legislative history of the FTC Act contains specific references to false disparagement, stock manipulation, industrial espionage, and "the hiring of detectives" as among the practices that the new commission would halt. It seems reasonable to treat the theft of intellectual property as having a familial resemblance to these other torts.[31]

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others." S. Rep. No. 63-567, at 13 (1914); see also H.R. Rep. No. 63-1142, at 19 (1914) ("There is no limit to human inventiveness in this field. . . . If Congress were to adopt the method of definition, it would undertake an endless task."); Senate Consideration of H.R. 15613, S. 4160 (Remarks of Sen. Newlands) (noting "it would be utterly impossible for Congress to define the numerous practices which constitute unfair competition and which are against good morals in trade"); id. (noting that unfair competition "covers every practice and method between competitors upon the part of one against the other that is against public morals . . . or is an offense for which a remedy lies either at law or in equity").

[30] See FTC v. Sperry & Hutchinson, 405 U.S. 233, 244 (1972) ("[T]he Federal Trade Commission does not arrogate excessive power to itself if, in measuring a practice against the elusive, but congressionally mandated standard of fairness it, like a court of equity, considers public values beyond simply those enshrined in the letter or encompassed in the spirit of the antitrust laws."); FTC v. Indiana Fed. of Dentists, 476 U.S. 447, 454-55 (1986) ("The standard of 'unfairness' under the FTC Act is, by necessity, an elusive one, encompassing not only practices that violate the Sherman Act and the other antitrust laws, but also practices that the Commission determines are against public policy for other reasons.").

[31] James F. Mongoven, The International Theft of Intellectual Property as a Violation of Section 5 of the Federal Trade Commission Act, 19 J. Reprints for Antitrust L. & Econ. 471, 503 (1989).

The FTC can use its substantial regulatory power if an unfair act or practice "causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or competition."[32] For example, in *In re C&D Electronics,* the Commission used its unfairness authority to address the sale of devices that permitted unauthorized viewing of cable TV signals.[33] In a separate statement, Chairman Daniel Oliver noted that consumers were harmed because "the activity here may provide disincentives that will result in services not being available to consumers at all."[34] Chairman Oliver was concerned that the respondents' actions would "undermine the competitive process that encourages innovation or maintenance of [cable] facilities" and raise the prices paid by law-abiding cable subscribers.[35]

Both the FTC's competition jurisdiction and its consumer protection jurisdiction serve the same end: namely, protecting consumer welfare.[36] Manufacturers' use of stolen IT distorts the marketplace and ultimately harms consumers. The FTCA anticipates agency action directed at "ethical notions of fairness and marketplace morality . . . [as well as] enforcement [based on] economic criteria [defining] unscrupulous acts in terms of consumer injury."[37] The theft of IT by

[32] 15 U.S.C. § 45(n).

[33] In re C&D Electronics, 109 F.T.C. 72 (1987).

[34] *Id.* at 80.

[35] *Id.* ("There is little or no reason for businesses to establish cable services, or expand and improve existing ones, unless sufficient revenue can be generated to warrant expenditures. Widespread or unchecked free riding could discourage ventures that would offer such services or could result in raising the prices for cable subscriptions in existing networks beyond optimal levels.").

[36] See, e.g., Timothy J. Muris, Chairman, Fed. Trade Comm'n, The Interface of Competition and Consumer Protection (Oct. 31, 2002), http://www.ftc.gov/speeches/muris/021031fordham.pdf ("[W]ell-conceived competition policy and consumer protection policy take complementary paths to the destination of promoting consumer welfare.").

[37] Marc A. Rodwin, *Consumer Protection and Managed Care: Issues, Reform Proposals, and Trade-Offs*, 32 HOUS. L. REV. 1321, 1364 (1996).

manufacturers certainly raises questions of fairness, marketplace morality, and unscrupulous acts that have a demonstrable and, in the long run, negative effect on the marketplace.[38]

Large-scale theft of information technology, particularly by manufacturers in countries with weak rule of law and where IT theft is rampant, [39] will, over any extended period of time, erode the ability of U.S. manufacturers to compete and undermine their incentives to produce better and more efficient goods in the United States. "Consumers may not be immediately harmed by such thefts. Indeed, the immediate impact is that consumers might see more firms supplying goods to certain markets. But if these thefts stifle incentives to invest in new technology, then consumers will inevitably suffer in the long run as economic growth rates decline."[40] The end result of IT theft is the potential loss of countless jobs,[41] lost billions in revenues, and, importantly, long-term market disincentives for U.S. manufacturers, creators and inventors.

Also, if consumer and other market actors believe reasonably a product was manufactured by a company that respects property rights and otherwise follows applicable law -- whether based on a company's code of conduct, its participation in a trade association that demands lawful conduct

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[38] See November 4, 2011 letter from the National Association of Attorneys General to the Federal Trade Commission ("Competition is unfairly distorted . . . when a manufacturer gains a cost advantage by using stolen information technology, whether in its business operations or manufacturing processes. It offends our sense of fairness when such wrongdoers reap a commercial advantage from their illegal acts."). Impact is discussed throughout Section One of this paper.

[39] The jurisdictional difficulties associated with IT theft outside the United States is not unlike the issues associated with the domestic sale of defective goods produced by foreign manufacturers. Popper, "The Two Trillion Dollar Carve-Out: Foreign Manufacturers of Defective Goods and the Death of H.R. 4678 in the 111th Congress," 26 TOXIC LAW REPORTER 105 (2011) (all too often, foreign manufacturers who produce defective goods are outside the reach of US courts and can inflict significant harms on US citizens and businesses with limited or no consequences).

[40] Mongoven, supra note 30, at 499.

[41] November 4, 2011 letter from the National Association of Attorneys General to the Federal Trade Commission (noting that 2.1 million U.S. jobs have been replaced by manufacturing in China, India, Mexico and Russia).

by participants and suppliers, or other public statements by a manufacturer or its representatives -- yet the company knowingly uses stolen IT, a deception has occurred that might violate the FTCA. For deceptive practices, the agency is authorized to take action if it can "establish that (1) there was a representation; (2) the representation was likely to mislead customers acting reasonably under the circumstances, and (3) the representation was material."[42]

The FTC may seek sanctions (either through agency proceedings or, in some instances in federal court) against "persons, partnerships, or corporations . . . using unfair methods of competition or unfair or deceptive acts or practices in or affecting commerce."[43] Under its competition jurisdiction, it may take steps to address "commerce with foreign nations" if the activity has "a direct, substantial, and reasonably foreseeable effect" on U.S. commerce.[44] Under its consumer protection jurisdiction, the Commission is authorized to address acts or practices involving foreign commerce that "cause or are likely to cause reasonably foreseeable injury within the United States."[45] The FTC has broad remedial powers "including restitution to domestic or foreign victims"[46] and injunctive relief in the form of "cease and desist orders"[47].

[42] FTC v. Tashman, 318 F.3d 1273, 1277 (11th Cir. 2003) (citations omitted); see FTC v. Direct Mktg Concepts, Inc., 569 F. Supp. 2d 285, 297 (D. Mass. 2008).

[43] Andrew Serwin, The Federal Trade Commission and Privacy: Defining Enforcement and Encouraging the Adoption of Best Practices, 48 San Diego L. Rev. 809, 821 (2011).

[44] 15 U.S.C. § 45(a)(3)(A).

[45] 15 U.S.C. § 45(a)(4)(A). For example, the FTC has taken action against U.S. companies for misrepresenting that their overseas manufacturers used environmentally friendly processes. In one case, the defendants' website claimed, "Jonano creats ecoKashmere in Asia in accordance with ISO 1400 environmental standards" and touted Jonano's use of organic bamboo, the testing conducted by authorized labs and professional certification groups, and certification to ISO and OKO-TEK standards. According to the FTC, these statements were deceptive because the process used to manufacture rayon actually involves hazardous chemicals and releases air pollutants. See Complaint and Exhibits, In re Sami Designs, LLC d/b/a/ Jonano, No. 082 3194 (Aug. 11, 2009), http://www.ftc.gov/os/caselist/0823194/090811samicmpt.pdf.

[46] 15 U.S.C. § 45(a)(4)(B).

[47] Elbert L. Robertson, *A Corrective Justice Theory of Antitrust Regulation*, 49 Cath. U.L. Rev. 741, 750 (2000).

When it comes to the theft of IT or other non-tangible assets, the power of the FTC to act to address anticompetitive, unfair, and deceptive practices is present. Recognizing that the exercise of sanction power is vested generally to the discretion of an agency,[48] the consumer deception and market distortion that occur as a result of the theft of IT justify consideration of agency action in this area.

B. State Unfair Competition Laws

Many states have unfair trade practices or consumer protection statutes modeled roughly after the FTCA. For example, the North Carolina statute tracks the FTCA by declaring unlawful "[u]nfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce."[49] Chapter 93A of the Massachusetts laws similarly prohibits "[u]nfair methods of competition and unfair or deceptive acts or practices in the conduct of any trade or commerce."[50] California creates a cause of action against anyone who engages in "unfair competition," broadly defined to include "any unlawful, unfair or fraudulent business act or practice."[51] Iowa and Missouri both prohibit "unfair practices" along with a variety of deceptive acts.[52]

[48] Heckler v. Chaney, 470 U.S. 821, 826 (1985) (in most instances, agency enforcement decisions are "committed to agency discretion by law").

[49] N.C. Gen. Stat. § 75-1.1(a).

[50] Mass. Gen. Laws ch. 93A, § 2.

[51] Cal. Bus. & Prof. Code §§ 17200, 17203.

[52] Iowa Code § 714.16(2)(a) (declaring unlawful "[t]he act, use or employment by a person of an unfair practice, deception, fraud, false pretense, false promise, or misrepresentation, or the concealment, suppression, or omission of a material fact with intent that others rely upon the concealment, suppression, or omission, in connection with the lease, sale, or advertisement of any merchandise"); Mo. Rev. Stat. § 407.020(1) (declaring unlawful "[t]he act, use

State unfair trade laws protect consumers and competitors[53] and level the playing field giving competitors who play by the rules an equal shot at benefitting from their labor and investment as opposed to those who "cream-skim" or "free-ride" on the efforts of others. These laws are predicated, *inter alia*, on the overriding importance in any marketplace of merit, efficiency, creativity, and competitive rigor. "One who has used his intellectual, physical, or financial powers to create a commercial product should be afforded judicial relief from a competitor who seeks to 'reap what he has not sown'."[54] The idea of such laws is to achieve a fair and robust competitive market in which similarly situated participants compete based on optimal efficiency and proficiency.[55]

The key feature of most of these laws is that anyone who engages in an "unfair" act can be penalized. The type of claim that can be initiated, however, is determined by each state's definition of *unfair act*. States often do not define clearly the scope of unfair acts, leaving courts to decide which acts confer an unfair advantage in business relations.[56]

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or employment by any person of any deception, fraud, false pretense, false promise, misrepresentation, unfair practice or the concealment, suppression, or omission of any material fact in connection with the sale or advertisement of any merchandise in trade or commerce").

[53] Johnson v. City of Pleasanton, 982 F.2d 350 (9th Cir. 1992).

[54] Rudolf Callmann, He Who Reaps Where He Has Not Sown: Unjust Enrichment in the Law of Unfair Competition, 55 Harv. L. Rev. 595, 612 (1942).

[55] Miguel Deutch, Unfair Competition and the "Misappropriation Doctrine" - A Renewed Analysis, 48 St. Louis U. L.J. 503, 545 (2004) (raising the "free-rider" problem in the context of economic efficiency and misappropriation).

[56] See, e.g., United Labs., Inc. v. Kuykendall, 403 S.E.2d 104, 109 (N.C. Ct. App. 1991) ("No precise definition of 'unfair methods of competition' as used in [§ 75-1.1] exists. . . . 'Rather, the fair or unfair nature of particular conduct is to be judged by viewing it against the background of actual human experience and by determining its intended and actual effects upon others.'" (quoting McDonald v. Scarboro, 370 S.E.2d 680, 684 (N.C. Ct. App. 1988))); see also JUDICIARY COMM., WASHINGTON STATE HOUSE OF REP., H.B. 1495 BILL ANALYSIS (2011), *available at* http://apps.leg.wa.gov/documents/billdocs/2011-12/Pdf/Bill%20Reports/House/1495%20HBA%20JUDI%2011.pdf (reasoning that "The state's Consumer Protection Act (CPA) prohibits unfair or deceptive acts or practices and unfair methods of competition in the conduct of trade or commerce that directly or indirectly affect the people of Washington. Several statutes specify practices that constitute unfair acts, but they do not provide an exhaustive list. A court may find that conduct not specifically enumerated in statute may constitute an unfair or deceptive act.").

Because the case law has developed differently in each state, attempts to bring claims based on manufacturers' unfair use of stolen IT face considerable legal uncertainty. For example, in Massachusetts, Chapter 93A claims can arise from a competitor's theft and misappropriation that resulted in an unfair business advantage.[57] In Iowa, by contrast, the existing precedent is thin and does not provide any examples of actions arising out of distortions to the competitive process. Because Iowa courts have recognized that the prohibition on "unfair practices" should be interpreted in a broad and flexible way, there is a legal basis to argue that a manufacturer's use of stolen IT should be actionable as an unfair practice.[58] The sparseness of the case law means that this would be a novel argument under the Iowa statute.

The state unfair trade practices laws are also subject to certain limitations, such as jurisdiction-specific restrictions on who has standing to enforce a violation of the law. In Iowa, only the state attorney general (AG) may bring a case; the Iowa Consumer Fraud Act does not include a private right of action.[59] Texas limits private plaintiffs to a narrow set of claims: private plaintiffs can bring claims based only on the specific acts enumerated in the statute, whereas the Texas AG is authorized to take action against all "false, misleading, or deceptive acts or practices."[60] To satisfy the standing requirements under California's unfair competition law, a private plaintiff "must now (1) establish a loss or deprivation of money or property sufficient to qualify as injury

[57] See Datacomm Interface, Inc. v. Computerworld, Inc., 396 Mass. 760, 778 (1986) (competitor's misrepresentation regarding its possession of a conversion copy of a circulation list purchased by plaintiff's parent in foreclosure violated Chapter 93A); Lee v. Mt. Ivy Press, L.P., 63 Mass App. Ct. 538 (2005) (upholding judgment for plaintiff's Chapter 93A claims predicated upon defendant fraudulently inducing plaintiff to sign away her copyright and profits from book).

[58] See State ex rel. Miller v. Cutty's Des Moines Camping Club, Inc., 694 N.W.2d 518, 526 (Iowa 2005) ("What is an 'unfair practice'? On its face the term is dizzying in its generality. Guidance can be found, however, in the decisions of other courts . . . . These courts have determined statutes that prohibit 'unfair practices' are designed to infuse flexible equitable principles into consumer protection law so that it may respond to the myriad of unscrupulous business practices modern consumers face.").

[59] See generally Iowa Code § 714.16.

[60] See Tex. Bus. & Com. Code Ann. § 17.46(b), (d).

in fact, i.e., *economic injury*, and (2) show that that economic injury was the result of, i.e., *caused by*, the unfair business practice or false advertising that is the gravamen of the claim."[61]

There may also be state-specific limitations on the relief afforded under the statute. For example, there is a wide range in civil penalties that can be assessed against entities found to have engaged in unfair acts. Missouri caps civil penalties at $1,000 per violation.[62] In Iowa, courts can impose a penalty of up to $40,000 per violation.[63] Similarly, although almost all states' unfair trade statutes authorize equitable relief, the territorial scope of any injunction could vary. Naturally, once a court has obtained personal jurisdiction over a defendant, the court has power to enjoin activities outside the state.[64] However, courts may decline to exercise this power for comity reasons or for fear of offending the policy of other states, particularly if it is unclear whether the conduct would be illegal under the other states' laws.[65] Because not all states prohibit "unfair" acts,[66] courts may decide to limit the scope of the injunction so that it only applies within the state.

[61] Kwikset Corp. v. Superior Court, 246 P.3d 877, 885 (Cal. 2011).

[62] Mo. Rev. Stat. § 407.100(6).

[63] Iowa Code § 714.16(7).

[64] See Restatement (Second) of Conflict of Laws § 53 (1971) ("A state has power to exercise judicial jurisdiction to order a person, who is subject to its judicial jurisdiction, to do an act, or to refrain from doing an act, in another state.").

[65] Cf. Restatement (Third) of Unfair Competition § 48, cmt. c (1995) ("The issuance of an injunction under state law prohibiting otherwise lawful conduct in another state raises serious concerns. Thus, although a court may have jurisdiction to grant broader relief, an injunction protecting the right of publicity should ordinarily be limited to conduct in jurisdictions that provide protection comparable to the forum state.").

[66] A number of the state statutes prohibit deception but not unfairness. For example, Section 349 of New York's General Business Law prohibits "[d]eceptive acts or practices in the conduct of any business, trade or commerce." N.Y. Gen. Bus. Law § 349. The New York legislature chose not to import the FTCA's prohibition on "[u]nfair methods of competition" and "unfair ... acts or practices," an omission that one federal court has found significant. See Leider v. Ralfe, 387 F. Supp. 2d 283, 295 (S.D.N.Y. 2005) ("[T]his omission indicates that anticompetitive conduct that is not premised on consumer deception is not within the ambit of the statute.").

Independent of the unfair trade statutes, some states recognize a separate common law tort of unfair competition. However, what constitutes an act of "unfair competition" varies from jurisdiction to jurisdiction. For example, a few states confine "unfair competition" to its historical roots in claims involving the "palming off" of goods or the misappropriation of a competitor's labor or expenditures.[67] In other states, the concept of unfair competition has evolved to include "all statutory and non-statutory causes of action arising out of business conduct which is contrary to honest practice in industrial or commercial matters."[68] In states that recognize a broader concept of unfair competition, a wide range of commercial torts may fall under that general designation. These include the torts of business defamation, trade secret misappropriation, tortious interference with commercial relationships, and similar illegal or unethical conduct that harms competitors. Because the scope of the doctrine varies so much between states, it may be difficult for manufacturers to obtain effective relief under this tort doctrine.[69]

[67] See, e.g., Kenney v. Hanger Prosthetics & Orthotics, Inc., 269 S.W.3d 866, 871 (Ky. Ct. App. 2007).

[68] Am. Heritage Life Ins. Co. v. Heritage Life Ins. Co., 494 F.2d 3, 14 (5th Cir. 1974); see also Rehabilitation Specialists, Inc. v. Koering, 404 N.W.2d 301, 305–06 (Minn. Ct. App. 1987) ("Unfair competition is not a tort with specific elements; it describes a general category of torts which courts recognize for the protection of commercial interests.").

[69] There are causes of action in tort that, at first blush, could be used to address the harms caused by IT theft: conversion, tortious interference with contact, or misappropriation. See, e.g., C. Owen Paepke, *An Economic Interpretation of the Misappropriation Doctrine: Common Law Protection for Investments in Innovation*, 2 High Tech. L.J. 55, 63 (1987); Courtney W. Franks, Comment, *Analyzing the Urge to Merge: Conversion of Intangible Property and the Merger Doctrine in the Wake of* Kremen v. Cohen, 42 HOUS. L. REV. 489, 522 (2005) (explaining that Oklahoma, Nevada and Tennessee do not recognize conversion of intangible property). However, their remedial potential is limited to direct harms to owners and not to the market or competitive injuries that are the focus of this paper. Moreover, misappropriation applies only in those situations where the plaintiff made a significant investment to develop its own content. It is at best unclear whether misappropriation could be stretched to include situations where the rival is not directly copying or exploiting the plaintiff's own content. Similarly, while conversion might be available for the IT owner to seek relief, it does not address the independent harm suffered by a competitor. Finally, for tortious interference with business relationship, the plaintiff would need to prove that the defendant interfered with a specific current or future business relationship, an extraordinarily difficult task – if not impossible – when it comes to the harms a competitor sustains. See, *e.g.*, *Kaufmann, Inc. v. Americraft Fabrics, Inc*., 232 F. Supp. 2d 220, 225, (S.D. N.Y. 2002); *Republic Tobacco, L.P. v. North Atlantic Trading Co.*, 254 F. Supp. 2d 1007, 1011 (N.D. Ill. 2003) (noting that New York, Kentucky, and Illinois law regarding interference claims have similar requirements).

C. **National Trade Laws**

National trade laws provide additional possible remedies against the use of stolen IT by manufacturers, at least where those products are manufactured abroad and then imported into the United States.[70]

Section 337 of the US Tariff Act of 1930 allows the U.S. government to exclude any item that violates U.S. patent, copyright, or trademark laws from entry into the United States.[71] Additionally, an action can be brought for a broad variety of "unfair acts," interpreted to include misappropriation of trade secrets,[72] false advertising, breach of nondisclosure agreements, and violations of antitrust laws.[73] Congress has stated that the language of section 337 is "designed to cover a broad range of unfair acts."[74] Thus, although it would be an issue of first impression, there is a basis to believe that the importation of products into the United States from a foreign manufacturer using stolen IT would constitute an unfair act within the meaning of section 337.[75]

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[70] See Lee Burgunder, Legal Aspects of Managing Technology, 3d ed. (2004).

[71] 19 U.S.C. 1337(a)(1)(B)-(C); (d).

[72] In the Matter of Certain Coamoxiclav Products, Potassium Clavulanate Products, and Other Products Derived from Clavulanic Acid. (The Coamoxiclav Products Case), *Certain Coamoxiclav Prods*., No. 337-TA-479, 2003 WL 1793272 (U.S. Int'l Trade Comm'n Mar. 6, 2003); Investigation 337-TA-479, before the ITC, April 16, 2003. http://www.usitc.gov/secretary/fed_reg_notices/337/I0416aa9.PDF.

[73] See Robert A. Caplen, Recent Trends Underscoring International Trade Commission Reviw of Initial Determinations and Federal Circuit Appeals from Final Commission Determinations under Section 337 of the Tariff Act of 1930, 17 Fordham Intellectual Property, Media and Entertainment L. J. 337 (2007) (tracking how Section 337 has been reinvigorated by rounds of amendments).

[74] S. Rep. 100-71, 100th Cong., 1st Sess., at 128.

[75] For instance, the Commission has held that the scope of section 337 is "broad enough to prevent *every type and form of unfair practice*." Certain Welded Stainless Steel Pipe and Tube, ITC Inv. No. 337-TA-29, USITC Pub. 863, Opinion of Commissioners Minchew, Moore and Alberger at 39 (1978) (emphasis added), quoting S. Rep. 595, 67th Cong., 2d Sess., at 3. The Court of Customs and Patent Appeals (the precursor to the Court of Appeals for the Federal Circuit) likewise has stated:

Pursuant to 19 U.S.C. 1337 (§ 337), the United States International Trade Commission (ITC)[76] has the authority to enforce a variety of U.S. international trade laws, including § 337. The ITC "is an independent, quasi-judicial Federal agency with broad investigative responsibilities on matters of trade."[77]

Section 337 actions are usually initiated by complainants, who must file a formal complaint.[78] Section 337(a)(1)(A) provides in relevant part:

> (1) [T]he following are unlawful . . .:
>
> (A) Unfair methods of competition and unfair acts in the importation of articles . . . into the United States, or in the sale of such articles by the owner, importer, or consignee, the threat or effect of which is—
>
> (i) to destroy or substantially injure an industry in the United States . . .

19 U.S.C. § 1337(a)(1)(A).

> [T]he quoted language is broad and inclusive and should not be held to be limited to acts coming within the technical definition of unfair methods of competition as applied in some decisions. . . . [I]t is evident from the language used that Congress intended to allow wide discretion in determining what practices are to be regarded as unfair.

In re Von Clemm, 229 F.2d 441, 443–44 (C.C.P.A. 1955).

[76] *See* 19 U.S.C. 1337.

[77] http://www.usitc.gov/press_room/about_usitc.htm

[78] See Robert A. Caplen, Recent Trends Underscoring International Trade Commission Reviw of Initial Determinations and Federal Circuit Appeals from Final Commission Determinations under Section 337 of the Tariff Act of 1930, 17 Fordham Intellectual Property, Media and Entertainment L. J. 337, 356 (2007) (explaining that sometimes the ITC may initiate an investigation "upon its initiative").

It does not matter where the respondent is domiciled. The overwhelming majority of respondents have been domiciled in Asia, but there have also been respondents from Europe, Africa, the Middle East, the Caribbean, Australia and Oceania, and the Americas.[79]

Upon receiving a complaint, the ITC begins an investigation of the alleged violation.[80] The ITC assigns the case to an administrative law judge (ALJ); however, section 337 actions resemble a civil litigation more than an administrative proceeding.[81] The ALJ files the initial determination (ID), which includes the findings of fact and conclusions of law. If the ITC does not order review of the ID, then the ID becomes the ITC's determination.[82] In its determination, the ITC may issue an exclusion order[83] or a cease and desist order.[84] U.S. Customs officials are charged with enforcing the exclusion order.

As scholars have noted, ITC enforcement is desirable over court litigation for at least four reasons: it offers injunctive-like relief, it is "drastic and swift," the forum is generally favorable

[79] See Robert A. Caplen, Recent Trends Underscoring International Trade Commission Review of Initial Determinations and Federal Circuit Appeals from Final Commission Determinations under Section 337 of the Tariff Act of 1930, 17 Fordham Intellectual Property, Media and Entertainment L. J. 337, 374 (2007).

[80] 19 U.S.C. 1337(b).

[81] See Robert A. Caplen, Recent Trends Underscoring International Trade Commission Reviw of Initial Determinations and Federal Circuit Appeals from Final Commission Determinations under Section 337 of the Tariff Act of 1930, 17 Fordham Intellectual Property, Media and Entertainment L. J. 337, 357 (2007) (listing section 337 proceedings' similarities to a civil litigation: full scale discovery, trial-type hearings with due process safeguards, a record, motions, depositions, interrogatories, requests for admission, applications for issuance of subpoenas).

[82] 19 U.S.C. 1337(j) ("If the Commission determines that there is a violation . . . it shall – (A) publish such determination in the Federal Register, and (b) transmit to the President a copy of such determination." The President may disapprove the ITC's action based on "policy reasons" within sixty days.)

[83] 19 U.S.C. 1337(e).

[84] 19 U.S.C. 1337(f).

to the U.S. industry, and there is no need to obtain personal jurisdiction over the foreign importers.[85]

However, ITC enforcement also has its drawbacks. For example, although the ITC is authorized to initiate proceedings, in practice it has rarely done so. This leaves the private complainant with the costly and time-consuming burden of proving the existence of the unfair act, a relationship between the unfair act and the imported article, a "domestic industry," and a showing that the domestic industry has been or is likely to be injured by the activity. These are onerous obligations guaranteeing an expensive process – and one where there are no money damages for successful plaintiffs. Considering these drawbacks – and given the volume IT theft referenced earlier in this article – it is safe to say that while the § 337 remedy is of value, this enforcement mechanism has not come close to addressing the core problems of piracy and economic harm. Finally, because the President has the authority to modify or reject any relief granted, the possibility of a presidential veto creates another level of uncertainty for potential plaintiffs.[86]

III. **The Washington and Louisiana Statutes**

In July 2011, a new unfair practices law came into effect in Washington State designed to promote a level playing field by targeting the problem discussed in this article--namely, the harms that arise when manufacturers steal software or other IT products and thereby gain an

[85] Jack Q. Lever, Jr., Unfair Methods of Competition in Import Trade: Actions Before the International Trade Commission, 41 BUS. LAW. 1165, 1167–68 (Aug. 1986).

[86] *Id.* at 1168.

unfair competitive advantage against manufacturers that pay for the IT they use.[87] The new law provides that:

> Any person *who manufactures an article or product while using stolen or misappropriated information technology in its business operations* after notice and opportunity to cure . . . , is deemed to engage in *an unfair act* where such an article or product is sold or offered for sale in this state, either separately or as a component of another article or product, and in competition with an article or product sold or offered for sale in this state.[88]

The Washington statute creates a new cause of action against manufacturers who illegally *use* (as opposed to pirate) software or other IT to reduce their costs and thus compete unfairly with honest manufacturers. In limited situations, the Washington statute also imposes responsibilities on firms that hire such manufacturers to produce products on their behalf (i.e., "hiring firms") as an ancillary way of avoiding the unfair competitive harm caused by the manufacturers' conduct.

In 2010, Louisiana also passed a bill to address situations where IT theft distorts the marketplace. Modifying the Louisiana Unfair Trade Practices and Consumer Protection Law (LUTPA), the Louisiana legislation declared that:

> It shall be unlawful for a person to develop or manufacture a product, or to develop or supply a service using stolen or misappropriated property, including

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[87] Wash. Rev. Code § 19.330.

[88] Wash. Rev. Code § 19.330.020.

> but not limited to computer software that does not have the necessary copyright licenses, where that product or service is sold or offered for sale in competition with those doing business in this state.[89]

A violation is deemed an unfair method of competition and an unfair practice or act, and is subject to the remedies and penalties provided for elsewhere in the LUTPA.

Although both statutes seek to remedy the harm that occurs when manufacturers use stolen IT to gain an unfair competitive advantage, the Washington statute has some additional notable features, discussed below.

A. **Notice and Opportunity to Cure**

Under the Washington statute, liability cannot be imposed on either a manufacturer using stolen IT or a hiring firm unless that manufacturer or hiring firm has been given advance notice of the problem and an opportunity to rectify the situation. For instance, Section 50 of the statute ensures that manufacturers are put on notice of the alleged stolen IT use and given at least 90 days to rectify the situation before a complaint may even be filed:

> No action may be brought under RCW 19.330.020 unless the person subject to RCW 19.330.020 received written notice of the alleged use of the stolen or misappropriated information technology from the owner or exclusive licensee of the information technology or the owner's agent and the person: (a) Failed to

[89] La. Rev. Stat. § 51:1427.

> establish that its use of the information technology in question did not violate RCW 19.330.020; or (b) failed, within ninety days after receiving such a notice, to cease use of the owner's stolen or misappropriated information technology. However, if the person commences and thereafter proceeds diligently to replace the information technology with information technology whose use would not violate RCW 19.330.020, such a period must be extended for an additional period of ninety days, not to exceed one hundred eighty days total. The information technology owner or the owner's agent may extend any period described in this section.[90]

Likewise, a hiring firm or other third party cannot be added to an action or subject to liability, respectively, unless it (1) was served with a copy of the Section 50 notice sent to the manufacturer at least 90 days prior to the entry of judgment against the manufacturer; and (2) failed, within 180 days of receiving the notice, to direct the manufacturer to cease its use of stolen IT.[91] Thus, the Washington statute ensures that any party potentially subject to liability is on notice of the putative action and has an opportunity to rectify the situation *before* liability may be imposed.

B. **Limited Monetary and Injunctive Relief**

If a manufacturer refuses to legalize its IT or establish that its use is legitimate after receiving the Section 50 notice, the State Attorney General may file suit for damages or injunctive relief. An

[90] Wash. Rev. Code § 19.330.050(1).

[91] *See* Wash. Rev. Code §§ 19.330.060(2)(a), 19.330.080(1)(c).

injured business whose products are sold in Washington State can also take action against competitors that use $20,000 or more of stolen IT in their business operations, provided that the plaintiff itself does not use stolen IT.[92]

If the court determines that a manufacturer violated the Washington statute, it may order the manufacturer either to pay actual damages or statutory damages (up to the retail price of the stolen or misappropriated IT), whichever is greater.[93] If the court determines that the manufacturer willfully violated the statute, it may increase damages by up to three times.[94]

The Washington statute authorizes courts, under limited circumstances, to enjoin a manufacturer from further violations, including enjoining the sale of products in Washington state made in violation of the statute.[95] The court may enjoin sales only if the manufacturer's violation resulted in at least a 3% difference in the product's retail price over a four-month period.[96] Preliminary injunctive relief is prohibited altogether.[97]

The Washington statute does not apply to companies providing services, medicines, or certain copyrightable end-products, or where the allegation that the IT is stolen is based on the violation of a patent, misappropriation of a trade secret, or violation of the terms of an open-source license.[98]

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[92] Wash. Rev. Code §§ 19.330.060(1), (5).

[93] Wash. Rev. Code § 19.330.060(1)(b).

[94] Wash. Rev. Code § 19.330.060(4)(a).

[95] Wash. Rev. Code § 19.330.060(1)(a).

[96] Wash. Rev. Code §§ 19.330.020, 19.330.010(5).

[97] Wash. Rev. Code § 19.330.060(6)(a).

[98] *See* Wash. Rev. Code § 19.330.030.

C. **Recourse Against Hiring Firms**

If a court finds a manufacturer in violation of section 20,[99] a claim can be added for "actual direct damages against a third party who sells or offers to sell in this state products made by that person."[100] Damages against a third party are capped at $250,000 and can only be imposed if, *inter alia*, the section 20 violator "did not make an appearance or does not have sufficient attachable assets to satisfy a judgment against the person," and "either manufactured the final product or produced a component equal to thirty percent or more of the value of the final product."[101] In addition, the third party must have a direct contractual relationship with the section 20 violator – i.e., the third party must be a hiring firm.[102] Other businesses or consumers in Washington State that purchase a section 20 violator's products are exempt altogether.

The Washington statute contains several safe harbors that allow hiring firms to avoid liability as well any disruption to their product supply chain.[103] For example, a hiring firm qualifies for a safe harbor if (1) the hiring firm requires its contract manufacturers to use legal IT and promptly

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[99] Section 20 states,

Any person who manufactures an article or product while using stolen or misappropriated information technology in its business operations after notice and opportunity to cure as provided in RCW 19.330.050 and, with respect to remedies sought under RCW 19.330.060(6) or 19.330.070, causes a material competitive injury as a result of such use of stolen or misappropriated information technology, is deemed to engage in an unfair act where such an article or product is sold or offered for sale in this state, either separately or as a component of another article or product, and in competition with an article or product sold or offered for sale in this state that was manufactured without violating this section. A person who engages in such an unfair act, and any articles or products manufactured by the person in violation of this section, is subject to the liabilities and remedial provisions of this chapter in an action by the attorney general or any person described in RCW 19.330.060(5), except as provided in RCW 19.330.030 through 19.330.090.

[100] Wash. Rev. Code § 19.330.060(2).

[101] Wash. Rev. Code § 19.330.060(2), (3).

[102] Wash. Rev. Code § 19.330.060(2)(d).

[103] Wash. Rev. Code §§ 19.330.060(1)(a), 19.330.060(2).

demands that its contractor manufacturers legalize if they are in violation of the Washington statute; or (2) the hiring firm employs responsible supply-chain practices related to the use of IT.[104]

D. **In Rem Proceedings**

When those who have stolen IT or other non-tangible assets are in-state and before a court, there are, as discussed above, a number of options for sanctions. Enforcement with out-of-state or foreign parties presents more challenging issues, particularly in light of the Court's refusal to resolve in *Nicastro*[105] and *Goodyear*[106] the *in personam* jurisdiction issues raised in *Asahi*.[107] This problem set arises any time a U.S. consumer or business is affected adversely by the sale or distribution of unsafe, defective, or otherwise flawed (e.g., made with or benefitting from stolen US IT or IP) foreign-made goods. Even when sales are substantial and part of a multi-state distribution program – and even when there is an aggregate of U.S. sales, if the conventional minimum contact requirements of *Asahi* are not met, jurisdiction over a foreign company can be extraordinarily difficult, if not impossible.[108] *Asahi* does invite Congress to address the jurisdictional void for federal court jurisdiction but thus far, Congress has failed to do so.[109] Accordingly, jurisdiction over the person (for foreign producers) cannot be the sole means of

[104] Wash. Rev. Code § 19.330.080(1)(c), (d).

[105] J. McIntyre Machinery, Ltd. v. Nicastro, 131 S. Ct. 2780 (2011).

[106] Goodyear Dunlop Tires Operations v. Brown, 131 S. Ct. 2846 (2011).

[107] Asahi Metal Industry Co. v. Superior Court, 480 U.S. 102 (1987).

[108] Andrew F. Popper, *The Two-Trillion Dollar Carve-Out: Foreign Manufacturers of Defective Goods and the Death of H.R. 4678 in the 111th Congress*, 26 BNA Insight, No. 4, (2011).

[109] Asahi Metal Industry Co. v. Superior Court, 480 U.S. at 116 ("We have no occasion here to determine whether Congress could, consistent with the Due Process Clause of the Fifth Amendment, authorize federal court personal jurisdiction over alien defendants based on the aggregate of national contacts, rather than on the contacts between the defendant and the State in which the federal court sits."[citations omitted]).

achieving the objectives of a level playing field, merit-based competition, and appropriate protection for those who create the technology that drives the American economy.

In Washington State, if a manufacturer is beyond the court's *in personam* jurisdiction, action may be initiated directly against *products* in which the manufacturer holds title (and are offered for sale in-state) if the seller is in violation of section 20.[110] As with injunctions against sales, in rem actions are limited to cases in which the manufacturer's violation resulted in at least a 3% difference in the product's retail price over a four-month period.[111]

Section 60 of the Washington statute authorizes the court, in certain situations, to enjoin sales in the state of products made with stolen IT, while Section 70 authorizes the court to proceed directly *in rem* against products made with stolen IT where the court is unable to obtain personal jurisdiction over the manufacturer.[112] These types of remedies are not unprecedented. In fact, seizing property to avoid the harms that flow inevitably from their entering the stream of commerce is very much part of U.S. legal history.

In her article, *International Courts and the U.S. Constitution: Reexamining the History*, Professor Jenny Martinez[113] discusses, *inter alia*, the early piracy and slave-ship seizure cases decided before the Civil War and subsequent adoption of the 13th Amendment. These decisions,

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[110] Wash. Rev. Code § 19.330.070.

[111] Wash. Rev. Code §§ 19.330.020, 19.330.010(5).

[112] Wash. Rev. Code §§ 19.330.060(1)(a), 19.330.070.

[113] Jenny S. Martinez, International Courts and the U.S. Constitution: Reexamining the History, 159 U. PA. L. REV. 1069, 1101 et. seq. (2011).

beginning in 1796, predate the formal national legal condemnation of slavery – and yet ships were seized even though slave traders were not prosecuted.[114]

United States v. La Vengeance[115] involved the seizure of a ship designed and outfitted for piracy. The Court considered whether denial of a jury trial required under the newly minted Judiciary Act violated the rights of the parties. The Court found that the seizure was not a criminal act but rather an action in admiralty. "It is a process of the nature of a libel in rem; and does not, in any degree, touch the person of the offender."[116] A decade later, *The Schooner Sally*[117] upheld property forfeiture without a personal prosecution.

The Palmyra[118] is another case in which an in rem seizure of a vessel was upheld, notwithstanding the absence of a charge (in that instance, for piracy) against any person. Unlike a case directed against a person,[119] an in rem action is focused on a "thing . . . here primarily considered as the offender. . . . Many cases exist[] where the forfeiture for acts done attaches solely in rem, and there is no accompanying penalty in personam. [Such] prosecutions [are not]

[114] The Slavers (Reindeer), 69 U.S. (2 Wall.) 383, 393, 403 (1864) ("libels in rem may be prosecuted in any district where the property is found"); The Slavers (Kate), 69 U.S. (2 Wall.) 350, 366 (1864) (an in rem proceeding could be used to seize a vessel designed to transport and sell slavese); The Josefa Segunda, 18 U.S. (5 Wheat.) 338, 343 (1820) (involving seizure and condemnation of property used in slave trade).

[115] 3 U.S. (3 Dall.) 297, 301 (1796).

[116] Id at 301.

[117] United States v. Schooner Sally, 6 U.S. (2 Cranch) 406 (1805).

[118] 206. 25 U.S. (12 Wheat.) 1, 12-13 (1827).

[119] See Harmoney v. United States (The Brig Malek Adhel), 43 U.S. (2 How.) 210, 233 (1844) ("The vessel which commits the aggression is treated as the offender, as the guilty instrument or thing to which the forfeiture attaches, without any reference whatsoever to the character or conduct of the owner.").

dependent upon each other. . . . [P]roceeding in rem stands independent of, and wholly unaffected by any criminal proceeding in personam."[120]

More recent cases have relied on *The Palmyra*. In *U.S. v. Ursery*,[121] the court continued the distinction between personal cases and in rem actions, citing *The Palmyra*. The Court, however, labeled this distinction a fiction if the forfeiture is a sanction against an individual who has committed an offense as opposed to a forfeiture designed to achieve general compliance with a set of clearly articulated legislative goals.[122] An in rem forfeiture of property that is exclusively an "instrumentality" of an offense is arguably permissible and not a punishment of the owner.[123] Civil forfeitures designed to limit or prevent unlawful action are, however, fairly common.[124]

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[120] In U.S. v. Bajakajian, 524 U.S, 328 n.5 (1998) the Court discussed the "'guilty property' theory behind in rem forfeiture [which] can be traced to the Bible, which describes property being sacrificed to God as a means of atoning for an offense. See Exodus 21:28. In medieval Europe and at common law, this concept evolved into the law of deodand, in which offending property was condemned and confiscated by the church or the Crown in remediation for the harm it had caused." See 1 M. Hale, Pleas of the Crown 420-424 (1st Am. ed. 1847); 1 W. Blackstone, Commentaries on the Law of England 290-292 (1765); O. Holmes, The Common Law 10-13, 23-27 (M. Howe ed. 1963)."

[121] 518 U.S. 267, 274 (1996) (distinguishing a civil in rem forfeiture action from a "personal penalty" (citing The Palmyra, 36 U.S. (12 Wheat.) at 14-15)).

[122] U.S. v. Bajakajian at 326;. United States v. Ursery, 518 U.S. 267 (1996) (KENNEDY, J., concurring) ("Civil in rem forfeiture is not punishment of the wrongdoer for his criminal offense").

[123] Austin v. United States, 509 U.S. at 627-628 (SCALIA, J., concurring in part and concurring in judgment, distinguishing property as the vehicle used to commit an offense); J. W. Goldsmith, Jr.-Grant Co. v. United States, 254 U.S. 505, 508-510 (1921).

[124] United States v. Nichols, 841 F.2d 1485, 1486-87 (10th Cir. 1988) ("Civil forfeiture has been widely used in the United States. Typically the government has been permitted to seek the forfeiture of contraband or harmful instrumentalities employed in an illegal activity. . . . [to] obtain 'virtually any type of property that might be used in the conduct of a criminal enterprise.'" citing Calero-Toledo, 416 U.S. at 683; See, e.g., United States v. Mandel, 408 F.Supp. 679, 682 (D. Md. 1976) (on the frequency of seizing automobiles or firearms).

An object can "evidence" a violation even if the current owner was not actively involved in the misconduct. When that happens, the "guilty object" can be seized and forfeited – and the forfeiture furthers enforcement of the underlying statute or regulation.[125]

IV. Precedents for the Washington Statute

Although the Washington statute embodies a novel approach to problems arising from IT theft, precedent for many aspects of the Washington statute can be found in other areas of law.

A. Enacting a State Statute to Address a Specific Method of Unfair Competition: Trade Secrets

State law on the misappropriation of trade secrets provides an interesting analogy to the type of conduct prohibited by the Washington statute. As courts have recognized, "[t]he law governing protection of trade secrets essentially is designed to regulate unfair business competition."[126] Both the tort of misappropriation of trade secrets and the Washington statute seek to provide a remedy for the unfair competition and market distortions that occur when companies acting in good faith compete with those that have gained a market advantage by stealing the inventions, property, or other intangible assets of another.

[125] "Traditionally, forfeiture actions have proceeded upon the fiction that inanimate objects themselves can be guilty of wrongdoing. Simply put, the theory has been that if the object is 'guilty,' it should be held to forfeit." United States v. United States Coin & Currency, 401 U.S. 715, 719 (1971) (citation omitted).

[126] Univ. Computing Co. v. Lykes-Youngstown Corp., 504 F.2d 518, 539 (5th Cir. 1974).

Trade secret law emanates from a provision of Roman law that sought to protect information Roman slaves might disclose to competitors.[127] Today, it is a patchwork of state trade secret protections, some statutory and some derived from common law claims. Trade secret litigation is particularly important to small companies.[128]

Although trade secrets were once a purely state matter, the United States, as a party to the World Trade Organization's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS),[129] also now provides national protection to trade secrets.[130] The U.S. has complied through the Economic Espionage Act of 1996 as well as state law protection of trade secrets.[131]

1. Restatement of Torts, section 39 and the Uniform Trade Secret Act

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[127] ROBERT P. MERGES, PETER S. MENELL, & MARK A. LEMLEY, INTELLECTUAL PROPERTY IN THE NEW TECHNOLOGICAL AGE 33–35 (5th ed. 2010) (discussing the Roman cause of action in *actio servi corrupti*, or literally, an action for corrupting the slave).

[128] *Id.* at 35.

[129] Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994, 1869 U.N.T.S. 299, 33 I.L.M. 1197 (1994) [hereinafter TRIPS Agreement], *available at* http://www.worldtradelaw.net/uragreements/tripsagreement.pdf.

[130] *Id.* at 16 (Article 39). Article 39 reads in relevant part:

1. In the course of *ensuring effective protection against unfair competition* as provided in Article 10*bis* of the Paris Convention (1967), Members shall protect undisclosed information in accordance with paragraph 2 and data submitted to governments or governmental agencies in accordance with paragraph 3.

2. Natural and legal persons shall have *the possibility of preventing* information lawfully within their control from being disclosed to, acquired by, or used by others without their consent in a manner contrary to honest commercial practices so long as such information:

(a) 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;

(b) has commercial value because it is secret; and

(c) has been subject to reasonable steps under the circumstances, by the person lawfully in control of the information, to keep it secret.

[131] See Robin J. Effron, Secrets and Spies: Extraterritorial Application of the Economic Espionage Act and the TRIPS Agreement, 78 N.Y.U. L. REV. 1475 (2003).

Until recently, the common law of the states was the only guiding law concerning trade secret protection. Today it is embodied in the Uniform Trade Secrets Act (UTSA). "[S]tate laws generally define a trade secret as consisting of three elements: (1) information (2) that has actual or potential economic value because it is secret and (3) is, in fact, a secret. [In addition,] the UTSA . . . requires that a potential rights holder make a reasonable effort to maintain the secrecy of the information."[132]

Currently, 46 states have adopted the USTA in some form, and two are currently considering it.[133] However, the laws have all been adopted with amendments, with differing statutes of limitations, criminal and civil penalties, and even causes of action one can bring. The goals underlying these laws, like the goals underlying the Washington statute, is protection and encouragement of creativity, invention, and innovation without hampering unduly the public access to information.

2. Federalizing Trade Secret Law

In an attempt to both comply with TRIPS and strengthen trade secret protection, in 1996 Congress passed the Economic Espionage Act[134] ("EEA") providing criminal and civil penalties for economic and industrial espionage.[135] In the legislative history of the EEA, one Senator

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[132] Id.

[133] *See State Should Adopt Protections for Trade Secrets,* NEWBURY PORT NEWS (Massachusetts), October 19, 2011, http://www.newburyportnews.com/opinion/x744038983/State-should-adopt-protections-for-trade-secrets.

[134] The Economic Espionage Act of 1996**,** Pub.L. 104-294, 110 Stat. 3488 (codified at 18 U.S.C § 1831–1839 (2006)) http://www.economicespionage.com/EEA.html.

[135] O'Hara, *supra* note 8, at 241 n.3 (defining the difference between industrial and economic espionage as the difference between benefactors: industrial espionage benefits anyone other than the owner, while the narrower economic espionage benefits "a foreign government, foreign instrumentality, or foreign agent").

stated there were "glaring gaps" in state trade secret law that only federal legislation could rectify.[136] Recently, some have argued that, particularly in light of the EEA and TRIPS, trade secret law should be further federalized.[137]

Senators Herb Kohl and Christopher Coons introduced an amendment to the Currency Exchange Rate Oversight Reform Act that would give a private federal right of action to trade secret owners for violations of section 1832(a), or trade secret theft.[138] This would amend the EEA to include a right of civil action for anyone "aggrieved by a violation of section 1832(a)." Section 1832(a) is one of the two types of conduct prohibited under the EEA, and it applies to misappropriating trade secrets related to or included in a product placed in interstate commerce knowing or intending that the misappropriation will injure the trade secret owner.

Like the unfair competition theories and state statutes discussed above, which seek to provide a remedy to businesses for the harms arising when a competitor obtains an unfair benefit from stolen IT, state and federal trade secret laws likewise seek to remedy the harms that businesses suffer when a competitor steals and benefits from a company's trade secret. While the theft in the former case involves the property of a third party (in this case, the IT owner), the harm to competitors, competition, and ultimately to consumers will often be quite similar -- namely, law-

[136] 142 Cong. Rec. S12,201, 12,208 (daily ed. Oct. 2, 1996) (statement of Sen. Specter). The legislative history of the EEA includes many examples of trade secret theft and misappropriation that state law cannot address. *See id.*

[137] David Almeling, *Guest Post: First Patent Reform, Now Trade Secret Reform?*, PATENTLY-O (Oct. 12, 2011, 3:08 PM) http://www.patentlyo.com/patent/2011/10/almeling-trade-secret.html.

[138] Id.; Press Release, Senator Kohl, "Kohl Offers Amendment to Protect American Businesses," http://www.kohl.senate.gov/newsroom/pressrelease.cfm?customel_dataPageID_1464=4775, October 5, 2011; Press Release, "Senator Coons introduces two amendments to currency bill to protect American intellectual property; Protecting American innovation is critical to protecting American jobs, http://coons.senate.gov/newsroom/releases/release/senator-coons-introduces-two-amendments-to-currency-bill-to-protect-american-intellectual-property, October 5, 2011.

abiding firms will be placed at a competitive disadvantage in the marketplace due to their competitor's theft of property.

B. Dual-Track Enforcement by State Regulators and Private Attorneys General

As noted above, the Washington statute provides a cause of action not only for the state's attorney general, but also for injured competitors. The notion of a combined effort that includes enforcement by state AGs and private parties (in this case, manufacturers that have been the victims of unfair competition by competitors using stolen IT) is not unusual and is well-suited to meet the challenge presented by stolen IT. In looking at problems with managed health care, Professor Marc Rodwin noted that when dealing with broadly defined "unfair or deceptive trade practices," enforcement can be shared by state "regulatory agencies, such as the Attorney General's Office of Consumer Protection, and private parties . . . [who can be awarded] treble damages and . . . plaintiff 's attorneys' fees." [139]

The Washington statute adopts just such a dual-track enforcement regime, and in doing so sends a powerful message. Professor Rodwin noted that the presence of fines or other sanctions "provide[s] an incentive for sellers to resolve private disputes out of court." Statutes of this type also create the potential that fines or penalties will cover litigation costs, helping consumers – or, in the case of the Washington statute, law-abiding manufacturers – "without funds to bring suits." Protection of the interests of those victimized by the market distortions caused by a manufacturer's theft of IT is consistent with current thinking on the role of private attorneys

[139] Marc A. Rodwin, *Consumer Protection and Managed Care: Issues, Reform Proposals, and Trade-Offs*, 32 HOUS. L. REV. 1321, 1364-5 (1996).

general.[140] This is particularly true where rights are violated and existing enforcement of those rights is lacking due to a lack of information, incentives, or other factors.[141]

C. **Gatekeeper Liability**

One of the primary challenges in protecting information technology and other non-tangible assets and property involves the ease of copying and the difficulty of detecting theft. IT is at once valuable and vulnerable. Unlike conventional physical property, once it moves beyond the dominion and control of its inventors and creators, the enforcement landscape becomes complex. Protection against IT theft or other forms of misappropriation of intangible assets must rely on contracts, license agreements, public (domestic and international) and private enforcement of patent, copyright, and trademark statutes, regulations, treaties, and similar regimes. While that level of protection may seem substantial,[142] as noted at the outset of this paper, it has been insufficient to prevent wholesale theft of billions of dollars of this property. Moreover, modest state legislation designed to discourage theft and piracy, with generous notice provisions, limited sanction potential, and limited scope (excluding from its coverage copyright and other conventional intellectual property) is hardly the stuff of suppression.

[140]William B. Rubenstein, *On What a "Private Attorney General" Is - and Why It Matters*, 57 VAND. L. REV. 2129, 2131 (2004) (defining broadly the role of private attorneys general who pursue public interests on behalf of private clients); see also Jeremy A. Rabkin, *The Secret Life of the Private Attorney General*, LAW & CONTEMP. PROBS., WINTER 1998, at 179, (exploring traditional role of [the] private attorney general model); See Abizer Zanzi, *The Constitutional Battle Over the Public Interest Litigant Exception to Rule 82*, 21 ALASKA L. REV. 329, 334 (2004) (describing a private attorney general as one who fights for a public interest on behalf of a non-governmental client). The Washington statute does not authorize true private AG actions, as a private party must prove competitive injury in order to have standing and can seek a remedy only for its own injury.

[141]Michael L. Rustad, *Smoke Signals from Private Attorneys General in Mega Social Policy Cases*, 51 DEPAUL L. REV. 511, 517 (2001) (those acting as private attorneys general advance the public interest).

[142] Gideon Parchomovsky & Alex Stein, *Originality*, 95 Va. L. Rev. 1505, 1509-12 (2009) (noting the perils of excessive copyright protection); Dorean M. Koenigfn, *Joe Camel and the First Amendment: The Dark Side of Copyright and Trademark-Protected Icons*, 11 Cooley L. Rev. 803 (1994) (intellectual property doctrines chills freedom of speech); Rosemary J. Coombe, *Objects of Property and Subjects of Politics: Intellectual Property Laws and Democratic Dialogue*, 69 TEX. L. REV. 1853 (1991) (intellectual property doctrine may limit political speech).

A culture of misappropriation has evolved around these assets here and abroad.[143] In many jurisdictions, including those that account for a significant share of global manufacturing, software and related products are copied without authorization and used at staggering levels.[144] There are two obvious effects of such theft. First, it undercuts the incentive to create the property by greatly diluting the value of these assets. Second, it provides an unfair advantage to those who sell products benefitting from such theft. Nonetheless, one could argue that as long as a lower consumer price results, the market has succeeded and legal interference is unwarranted. Similar arguments have been used in the past in an attempt to rationalize the use of child labor and environmentally hazardous practices by manufacturers, but are now uniformly rejected not only because they seek to condone immoral or illegal conduct, but because they risk driving a "race to the bottom" among manufacturers in terms of their labor practices, environmental practices, and other corporate conduct.

In some cases, it is not only the manufacturer who steals IT that enjoys an unfair competitive edge. Companies that hire manufacturers to produce products on their behalf and under their label, yet who turn a blind eye to the manufacturer's theft of IT or other illegal practices, may also be reaping an unfair cost advantage. Should these hiring firms be seen as third-party beneficiaries of the manufacturer's theft and assigned responsibility for the manufacturer's

[143] Chun-Hsien Chen, Explaining Different Enforcement Rates of Intellectual Property Protection in the United States, Taiwan, and the People's Republic of China, 10 TUL. J. TECH. & INTELL. PROP. 211, 215-16 (2007) (discussing comparatively the culture of copying in the U.S. and Asia); Daniel C.K. Chow, Why China Does Not Take Commercial Piracy Seriously, 32 Ohio N.U.L. Rev. 203, 213 (2006) ("It is no exaggeration to say that many in China believe that they can engage in the theft of intellectual property with impunity. . . . This creates a widespread business culture that tolerates, or even encourages, unauthorized copying and theft of intellectual property. The culture of copying is so pervasive that even many of China's most successful legitimate companies treat it as a part of doing business.").

[144] Id.

conduct? In the domain of the criminal justice system, scholars find this a complex matter.[145] The property and interests in question in this paper could be protected through criminal or civil mechanisms when it comes to a thief – but what about the third-party beneficiary?

Professor Reiner Kraackman posed the question succinctly: "[W]hen should we impose liability on parties who, although not the primary authors or beneficiaries of misconduct, might nonetheless be able to prevent it. . . .?"[146] Professor Kraackman used the term "gatekeeper" to describe those who benefit from misconduct and have the power or potential to lessen the probability of misconduct. He asks whether the following are present to assess whether a third-party beneficiary of misconduct should play a role or be the subject of some form of enforcement or sanction:

(1) "serious misconduct that practical penalties cannot deter;

(2) missing or inadequate private gatekeeping incentives;

(3) gatekeepers who can and will prevent misconduct reliably; and

(4) gatekeepers whom legal rules can induce to detect misconduct at reasonable cost."[147]

In the case of stolen IT used by manufacturers acting on behalf of hiring firms, Professor Kraackman's criteria are met. Currently, such hiring firms are not deterred by penalties, have few incentives to look upstream to discover misconduct by their contract manufacturers (at least

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[145] Ellen M. Bublick, Symposium: Upside Down? Terrorists, Proprietors, and Civil Responsibility for Crime Prevention in the Post-9/11 Tort Reform World, 41 Loy. L.A. L. Rev. 1483, 1521 (2008)(("Whether third parties should be fully liable for failure to protect against crime is a complex question. . . .")

[146] Reinier H. Kraakman, Gatekeepers: The Anatomy of a Third Party Enforcement Strategy, 2 J.L. Econ. & Org. 53, 53 (1986).

[147] Reinier H. Kraakman, Gatekeepers: The Anatomy of a Third Party Enforcement Strategy, 2 J.L. Econ. & Org. 53, 61 (1986).

with regard to IT theft), have the capacity to limit or prevent misconduct (as most hiring firms do today with regard to labor practices and the like), and can, with a minimum of effort, use reasonable care to detect misconduct at reasonable cost. Empowered to take action or face consequences, such hiring firms can play a central role in lessening theft of IT. "[W]here gatekeepers and enforcement targets transact, gatekeepers can disrupt misconduct either by refusing to transact with would be wrongdoers at all or by refusing requests by wrongdoers for illicit or substandard performance during the course of a broader transaction."[148]

In a *Harvard Law Review* piece a few years ago, [149] Professor Daryl J. Levinson explained that the means to efficient enforcement are not limited to direct prosecution. He observed that proceeding against the "primary or proximate causer of harm" may be less effective than directing enforcement efforts at those who have the most influence over the wrongdoer. "Courts (and even economic theorists) often fail to recognize that the optimal target of liability is not the wrongdoing injurer but rather some other individual, institution, or group . . . well-situated to monitor and control the wrongdoer's behavior. . . ." Compliance motivation[150] – in this case, creating incentives against theft and unauthorized copying – might best be achieved by the "threat of 'indirect' liability."[151]

[148] Id. at 62-63.

[149] Daryl J. Levinson , Aimster & Optimal Targeting, 120 Harv. L. Rev. 1148, (2007).

[150] Systems where a third party faces clear consequence for failing to act or report are not unusual. See Kraackman, supra note 142 at 65, n.40: "Tax preparers are subject to $100 and $500 fines for negligent disregard of the law and willful understatement of tax liability respectively (IRC § 6694, 1985)"; See also, *Herman & MacLean v. Huddleston*, 459 U.S. 375, 386 n.22, (1983) (no liability by implication for third parties who prepare securities registration statements; the duty must be express); Escott v. BarChris Constr. Corp., 283 F.Supp. 643, 683 (S.D.N.Y. 1968) (third party liability must be express).

[151] Levinson, supra note 142, at 1148.

Professor Levinson recognizes that indirect liability is not always workable. "[I]ndirect liability is appropriate only in the limited set of cases in which direct liability is clearly impractical and an alternative target capable of exercising formal control over the primary wrongdoer, through a contractual or otherwise profitable relationship, is readily available. . . ."[152] Those conditions (contract, profit, the capacity to apply compliance pressure) are evident in many settings where hiring firms indirectly "benefit" from theft of IT by their contract manufacturers (in the form of lower prices for manufactured goods). Moreover, there is good reason to think that hiring firms might be unusually effective in enforcing compliance by contract manufacturers. A well-written statute "taps the best focusing device of all: a community of legally sophisticated gatekeepers."[153]

Professor Levinson focuses on the *Aimster* litigation, in which Judge Posner approved the imposition of liability against the intermediaries of wrongful conduct.[154] Though *Aimster* focused on an intermediary who facilitated illegal copyright infringement, the concept of indirect liability (and Judge Posner's embrace of that idea) provides theoretical support for the ultimate practical effect of the Washington statute: holding third parties indirectly accountable for wrongful conduct committed by those "hired" to manufacture on their behalf. As Levinson explains, regardless of whether indirect liability is premised on the third party's wrongdoing—as in the case of knowingly assisting wrongdoers—or purely vicarious liability—as with respondent

[152] Id. at 1154.

[153] Kraackman, supra at 142 (on the general effect of a third-party regime and moral and legal suasion).

[154] *See* Daryl J. Levinson, Aimster & Optimal Targeting, 120 Harv. L. Rev. 1148 (2007); In re Aimster Copyright Litigation, 334 F.3d 643 (7th Cir. 2003). The Supreme Court followed, saying "[O]ne who distributes a device with the object of promoting its use to infringe copyright, as shown by clear expression or other affirmative steps taken to foster infringement, is liable for the resulting acts of infringement by third parties." Metro-Goldwyn-Mayer Studios, Inc. v. Grokster, Ltd., 545 U.S. 913, 919 (2005). According to Levinson, however, the case "is a telling indication of the very limited distance from the traditional model that most courts will be willing to stray." Nonetheless, neither *Aimster* nor *Grokster* involved an express statutory provision allowing indirect liability.

superior—indirect liability poses an opportunity for "motivating a well-situated third party to police and prevent wrongdoing."[155]

As discussed above, the Washington statute imposes limited secondary responsibility on hiring firms on the theory that such firms are causally responsible for the harms targeted by the statute insofar as they have ultimate decisionmaking authority regarding the sale of the goods in the state, and because they have a unique ability, given their commercial relationships, to discourage stolen IT use by their contract manufacturers.

V. **A Brief Look at Legal and Economic Objections to the Washington Statute**

Some have asserted that the Washington and Louisiana Statutes are unconstitutional because they interfere with the power to regulate copyright or international commerce – powers vested to Congress.[156] Others contend that theft or misappropriation of IT is more properly seen as an inconsequential cost of modern and vital information dissemination, an essential component of free speech with a resulting consumer gain in lower prices. These contentions are unconvincing.

A. **Preemption**

[155] Levinson, *supra* note 5, at 1149. Nevertheless, Levinson explains that there are two conditions for indirect liability to be efficient: 1) the third party "must be capable of controlling wrongdoing in some cost-effective way," and 2) "the subsidiary costs of indirect liability must not be too high." *Id.* at 1150-51.

[156] *Why is Microsoft Seeking New State Laws That Allow It to Sue Competitors For Piracy by Overseas Suppliers?* GROKLAW (March 24, 2011, 9:46 AM), http://www.groklaw.net/articlebasic.php?story=2011032316585825.

The Supremacy Clause,[157] the constitutional base of preemption, ostensibly prohibits state laws that duplicate or conflict with a federal law.[158] Thus, a tort claim that might penalize an individual or entity for complying with a federal statute would be preempted. In recent years the Supreme Court has found that the Food, Drug, and Cosmetic Act (FDCA)[159] and the Hatch-Waxman Act[160] preempt certain state tort claims.

"The purpose of Congress is the ultimate touchstone in every pre-emption case."[161] Thus, there must be a congressional intent to preempt.[162] If there is an explicit preemption clause, the court must ascertain the scope of that which is prempted. In *Goldstein v. California*,[163] discussed by scholar Viva R. Moffat,[164] the Court held that the enforcement of a state law would not stand as an obstacle to the achievement of a federal purpose where Congress had not indicated it wished to regulate the act in question.[165]

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[157] U.S. CONST. Art. IV, cl. 2. ("This Constitution, and the Laws of the United States which shall be made in Pursuance thereof ... shall be the supreme Law of the Land; ... any Thing in the Constitution or Laws of any state to the Contrary notwithstanding.").

[158] *See* Altria Group v. Good, 555 U.S. 70 (2008); Maryland v. Louisiana, 451 U. S. 725, 746 (1981); Gibbons v. Ogden, 22 U.S. 1 (1824).

[159] Food, Drug, & Cosmetic Act (FDCA), Pub. L. No. 75-717, ch. 675, 52 Stat. 1040 (1938) (codified as amended in scattered sections of 21 U.S.C.).

[160] Drug Price Competition and Patent Term Restoration (Hatch–Waxman) Act of 1984, Pub. L. No. 98-417, 98 Stat. 1585 (codified at 21 U.S.C. § 355(b), (j), (*l*); 35 U.S.C. §§ 156, 271, 282 (2006)).

[161] Medtronic, Inc. v. Lohr, 518 U. S. 470, 485 (1996) (internal quotation marks omitted) (quoting Retail Clerks v. Schermerhorn, 375 U. S. 96, 103 (1963)).

[162] *Altria Group*, 555 at 72 (citing Jones v. Rath Packing Co., 430 U. S. 519, 525 (1977).

[163] Goldstein v. California, 412 U.S. 546, 561 (1973).

[164] Viva R. Moffat, *Super-Copyright: Contracts, Preemption, and the Structure of Copyright Policymaking*, 41 U.C. DAVIS L. REV. 45, 82–83 (2007).

[165] The Court concluded that "[i]n regard to this category of 'Writings,' Congress has drawn no balance; rather it has left the area unattended, and no reason exists why the State should not be free to act."

Some commentators have questioned whether the Washington statute might be preempted by federal copyright law.[166] Section 301 of the U.S. Copyright Act preempts state law only if that law (1) protects legal rights that are "equivalent to" rights protected by the Copyright Act; <u>and</u> (2) regulates works that fall "within the subject matter of copyright."[167] In fact, the Washington statute does neither.

State laws are not subject to Copyright Act preemption "if an extra element is required instead of or in addition to the acts of reproduction, performance, distribution or display in order to constitute [the] state-created cause of action."[168] The Washington statute contains elements that are qualitatively different from, and in addition to, elements that must be satisfied in order to assert a copyright infringement claim. For example, no claim can be brought under the Statute unless the products from the manufacturer using stolen IT were sold or offered for sale in Washington State <u>*in competition with*</u> products made without violating the prohibition. Moreover, only competing manufacturers (not IT owners) have standing to sue under the statute (in addition to the State Attorney General), and the competing manufacturer must establish that it suffered economic harm. None of these elements is required to state a claim under the Copyright Act.

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[166] *See* Jan Teague, Guest Column: Microsoft Software-Piracy Bills Would Harm Businesses, SeattlePI.com's The Microsoft Blog (Mar. 11, 2011, 8:00 AM), http://blog.seattlepi.com/microsoft/2011/03/11/guest-column-microsoft-software-piracy-bills-would-harm-businesses/.

[167] 17 U.S.C. § 301(a).

[168] Wrench LLC v. Taco Bell Corp., 256 F.3d 446, 456 (6th Cir. 2001). As the author of a leading copyright treatise writes, "if qualitatively other elements are required instead of, or in addition to, the acts of reproduction, performance, distribution, or display, in order to constitute a state-created cause of action, then the right does not lie 'within the general scope of copyright' and there is no pre-emption." David Nimmer, *Nimmer on Copyright*, § 1.01[B][1] (2010) (footnotes and internal quotation marks omitted).

The Washington statute is not vulnerable to preemption for the additional reason that it does not regulate works that "come within the subject matter of copyright."[169] The Statute expressly excludes cases in which the article or product sold or offered for sale in the state "is a work within the subject matter of copyright as specified in section 102 of Title 17, United States Code."[170] Thus, if articles or products sold in Washington State fall within the scope of copyright, one seeking recourse from an alleged violation is limited to the Copyright Act, not the statute. If articles or products fall outside the scope of copyright, however, and their sale in the state constitutes an unfair trade practice, the Washington statute will provide a remedy to injured manufacturers.

There is nothing novel or inappropriate with a state pursuing a policy that furthers the purposes of federal law, so long as such actions are not preempted. Since the purpose of the Washington statute is complementary with clearly stated federal goals, and does not conflict with such goals, it is not preempted.

There are powerful federalism policies in play when a state exercises policy powers to protect the interests of its citizens. For example, "the U.S. system of antitrust federalism sometimes means that state sovereignty will defeat attempts to establish a uniform, national policy on how best to redress competitive harm."[171] Even in situations where the state statute has an arguably suppressive effect on unrestrained price competition, the Court has allowed states to engage in precisely such activity so long as the policy is "clearly articulated . . . affirmatively expressed . .

[169] 17 U.S.C. § 301(a).

[170] Wash. Rev. Code §§ 19.330.030, 19.330.010(2).

[171] Leon B. Greenfiled and William J. Kolasky, *Antitrust Modernization: Picking Up the European Gauntlet?*, 22 Antitrust ABA 56, 58 (2008).

. [and] actively supervised by the State. . . ."[172] The Washington statute falls squarely within those criteria.

B. Fairness in Price Competition Matters

In some cases, goods made by manufacturers using stolen IT will be cheaper in the short run because the manufacturer's cost basis is reduced by the theft. Why impose legal consequences when the consumer is getting a product at a reduced price? The answer lies, in part, with the fundamental values at stake.

Although hard-core Chicago-School economists might argue that consumers are benefiting from the lower price, the consequences of this kind of price myopia are problematic.[173] A narrow focus on reducing prices fails to take into account an array of values and incentives, not the least of which is stimulation of creativity and invention. The short-term benefits for consumers who pay less are more than offset by the longer-term adverse effects in terms of reduced competition and the adverse impact on creation and invention of better goods and services.

There is a long-term and real risk in the failure to provide a regime to insure the protection of revenue, income, or royalties for IT. Talking about economic regulation and antitrust

[172] *California Retail Liquor Dealers Assn. v. Midcal Aluminum, Inc.*, 445 U.S. 97, 105 (1980). See *FTC v. Ticor Title Insurance Co*., 504 U.S. 621, 633 (1992). ("Actual state involvement, not deference to private price-fixing arrangements under the general auspices of state law, is the precondition for immunity from federal law."); see also Parker v. Brown, 317 U.S. 341, 350-51 (1943) ("In a dual system of government in which, under the Constitution, the states are sovereign, save only as Congress may constitutionally subtract from their authority, an unexpressed purpose to nullify a state's control over its officers and agents is not lightly to be attributed to Congress. . . .").

[173] Thomas J. Horton, *The Coming Extinction of Homo Economicus and the Eclipse of the Chicago School of Antitrust: Applying Evolutionary Biology to Structural and Behavioral Antitrust Analyses*, 42 LOY. U. CHI. L.J. 469, 501 (2011) (fairness, economic morality, and broad values, more than efficiency based or Chicago School economics and a fixation on price, are fundamental to human beings and essential for survival).

enforcement, Professor Thomas Horton posits that "[i]t is time to stop accepting Judge Bork's ANTITRUST PARADOX thesis. . . . [W]e should focus on fair and ethical competition, which will enhance, rather than sacrifice, our economic system's overall dynamic and adaptive efficiency."[174]

Professor Horton's argument is consistent with the notion of rendering level the playing field. He relies on Alfred Kahn as support for the value of fairness in the competitive market. "[F]air competition is an "end in itself." . . . linked with the noneconomic values of free enterprise – equality of opportunity, the channeling of the profit motive into social constructive channels. . . ."[175]

The notion that the legal system must tolerate an evolving segment of the culture that accepts theft is nonsensical. "[M]oral behavior is necessary for exchange in moderately regulated markets . . . to reduce cheating without exorbitant transaction costs."[176] Professor Horton's very recent scholarship on these points also relies on Adam Smith for the proposition that competitive regimes and antitrust enforcement, "should not be based solely on economic measurements but also on moral and political judgment."[177] Turning a blind eye to IT theft ignores essential

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[174] Id.

[175] ALFRED E. KAHN, STANDARDS FOR ANTITRUST POLICY, IN MONOPOLY POWER AND ECONOMIC PERFORMANCE: THE PROBLEM OF INDUSTRIAL CONCENTRATION 151-52

[176] Id.

[177] Horton, supra note 168at 512, citing RICHARD HOFSTADTER, WHAT HAPPENED TO THE ANTITRUST MOVEMENT, IN THE BUSINESS ESTABLISHMENT 113, 149 (Earl Frank Cheit ed., 1964) (on the importance of moral force in antitrust enforcement).

morality issues and fosters the notion, immortalized in our cinematic culture, that "greed is good, greed simplifies, greed clarifies, greed in all of its forms makes the marketplace work."[178]

The idea of morality in the competitive market, including taking steps to level the playing field, may be at odds with the Chicago School, but it is squarely in line with deep-seated and fundamental values that transcend the simplistic notion of allocative efficiency. A morally sound market is dynamic; in fact, it is the foundation of not just efficient market theory but is the "glue that holds our societies together."[179]

VI. **Conclusion**

The theft of IT or other non-tangible assets by upstream producers has a pernicious effect on fair market pricing, violates a most fundamental public policy (protection of those who create and invent such property), and violates ethical norms regarding the retail sale of goods that benefitted from stolen IT.[180] Thus, it makes solid economic sense to develop a plan to address such theft with multiple enforcement mechanisms.

Much of this paper is focused on manufacturers and hiring firms benefitting from theft or misappropriation of property. These companies are not just free-riding on the successes of those who produce the products and ideas that are a driving force in the U.S. economy, they are destabilizing the pricing market and distorting lawful competition by virtue of outright theft.

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[178] WALL STREET (20th Century Fox 1987).

[179] Horton, supra note 168 at 511.

[180] EICC (Electronic Industry Citizenship Coalition) Code of Conduct , http://www.eicc.info/EICC%20CODE.htm; for OECD information on theft or piracy of IT, see http://www.oecd.org/document/23/0,3746,en_2649_37461_44088983_1_1_1_37461,00.html.

Market misconduct of this nature generates disincentives to creativity and distorts pricing and manufacturing costs.

The harm to competition and consumers is documented and substantial, the laws violated are clear (and, as to foreign producers, nearly impossible to enforce), public policy is implicated (in terms of both the letter and spirit of the laws regarding the use of IT), fairness issues abound (regarding the injury suffered by those who produce the ideas and inventions that drive the economy), and unethical behavior (overt theft of IT) is rampant.

Legislation is needed not just to stimulate creation and invention; state legislation, along the lines of the Washington statute discussed in this paper, holds out the promise of fairness in pricing, a level and vibrant competitive playing field, and some modicum of justice for those whose work has been stolen.