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The DTSA: The Litigator's Full-Employment Act

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The DTSA: The Litigator's Full-Employment Act

Sharon K. Sandeen*

Abstract

Civil litigation is expensive, both for the party bringing suit and the party that must defend against such claims. For a variety of reasons, not the least of which are the usual requests for preliminary relief and protective orders, trade secret litigation is particularly expensive. These costs can have a crippling effect on small businesses and start-up companies that are accused of trade secret misappropriation, often resulting in litigation expenses that exceed the alleged harm to the plaintiff. Such litigation is particularly costly and unjust in cases where the plaintiff asserts rights that, due to common misunderstandings about the limited scope of trade secret rights, they do not have.

While no body of law can perfectly distinguish right from wrong, and, thus, there are bound to be civil judgments that are both under- and over-inclusive, due to the possible anticompetitive effects of trade secret claims, the predominate law that currently governs trade secret law in the United States, the Uniform Trade Secret Act, includes numerous provisions that are designed to strike a balance between the putative trade secret owner and the alleged misappropriator, frequently erring on the side of competition, information diffusion, and employee mobility. Unfortunately, the proposed legislation to create a civil cause of action for trade secret misappropriation, the Defend Trade Secrets

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THE DTSA: THE LITIGATOR’S FULL-EMPLOYMENT ACT 309

Act (DTSA), threatens to upset this balance by, among other things, significantly increasing the costs of trade secret litigation.

This Essay details how various provisions of the DTSA are bound to be highly litigated and, as a result, will greatly increase costs for litigants and the federal judiciary, making the DTSA not worth its costs.

Table of Contents

I. Introduction.....	309
II. The Asserted Benefits of the DTSA	311
III. The Costs of the DTSA	313
A. More Trade Secret Cases Will Be Filed in Federal Court.....	313
B. The Constitutional Basis for the DTSA Will Be Challenged Frequently	314
C. The Proposed Seizure Remedy Is New and Untested and Is Likely To Be Highly Contested	317
D. There Is No Federal Jurisprudence of Trade Secret Law to Fill the Gaps of the DTSA	319
IV. Conclusion	321

I. Introduction

When individual citizens sue U.S. businesses, policymakers often lament the litigious nature of U.S. society and call for tort reform as a means to limit lawsuits and reduce litigation costs. Thus, it is surprising that U.S. lawmakers have recently proposed the adoption of a new federal tort that will enable more federal lawsuits to be brought against U.S. businesses, particularly small businesses and start-up companies. Titled the “Defend Trade Secrets Act” (DTSA),¹ the proposed new law would amend the federal Economic Espionage Act of 1996 (EEA)² to create a

1. Defend Trade Secrets Act of 2015, H.R. 3326, 114th Cong. (2015).

2. 18 U.S.C. §§ 1831–39 (2012).

private federal right of action for trade secret misappropriation when similar state causes of action already exist to protect U.S. trade secrets.

For nearly two hundred years, the body of state law that currently enables trade secret owners to enforce their rights, in either state or federal court (the latter based upon diversity jurisdiction), has served trade secret owners in the U.S. well, particularly as it evolved and was later codified in the Uniform Trade Secrets Act (UTSA) to include clearer definitions and broader remedies.³ Many trade secret cases are unsuccessful, however, not because of deficiencies in existing state laws, but because of the non-existence of legitimate trade secrets or the absence of evidence of misappropriation. Even worse, weak or non-existent trade secret rights are often asserted against start-up companies that, in “the American Way,” simply want a chance to start a business that they believe will provide benefits to consumers.

Although touted as essential legislation for the protection of U.S. trade secrets, no evidence has been presented to demonstrate that the existing system of uniform state laws—particularly when coupled with existing federal laws—is insufficient to protect the interests of legitimate trade secret owners.⁴ In fact, the current system was recently ranked the best

3. See Sharon K. Sandeen, *The Evolution of Trade Secret Law and Why Courts Commit Error When They Do Not Follow the Uniform Trade Secrets Act*, 33 *HAMLIN L. REV.* 493, 501 (2010)

By the time of the adoption of the UTSA in 1979, forty years had passed since the publication of the Restatement First [of Torts] and the drafters of the UTSA had the benefit of the further common law development of trade secret law. Also by then, the courts of law and equity in the United States had merged and there was a much greater reliance on and reception of statutory law. . . . [B]ecause the UTSA is a code rather than a restatement of existing law, it was used to fill gaps in the law that had not been filled by common law courts and to refine or change common law principles that were considered ill-advised.

4. To date, forty-seven of the fifty states, plus Puerto Rico and the U.S. Virgin Islands, have adopted the Uniform Trade Secrets Act, making it one of the most widely adopted uniform laws in the United States. *Legislative Facts Sheet—Trade Secrets Act*, UNIF. LAW COMM’N, <http://www.uniformlaws.org/LegislativeFactSheet.aspx?title=Trade%20Secrets%20Act> (last visited Oct. 21, 2015) (on file with the Washington and Lee Law

system for the protection of trade secrets in the world.⁵ Rather, the principal arguments in favor of the legislation are the preference of many large companies to litigate in federal courts and unsubstantiated claims that cyber-espionage cannot be stopped without an additional federal law. Against these asserted benefits, little attempt has been made to weigh the costs of the DTSA, both in terms of the burdens that it will place on U.S. businesses—who will be the targets of federal lawsuits—and the federal judiciary.

This Essay aims to rectify this deficiency by considering what, if anything, the DTSA will add to trade secret enforcement that state laws do not already provide and at what costs. After considering these questions, this Essay concludes that the marginal benefits of the DTSA do not outweigh its costs, principally because the creation of a new federal civil cause of action will significantly increase the incidence and magnitude of federal trade secret litigation, at both the district court and appellate court levels, thereby making the DTSA the “Litigator’s Full-Employment Act.”

II. The Asserted Benefits of the DTSA

A number of arguments have been made to support the passage of the DTSA, but the fundamental question is: Will the DTSA be an improvement over the existing system of state laws and, if so, at what costs? Simply arguing that “more is better,” or that federal law somehow has more deterrent effects than state law, is not a compelling basis for new federal legislation, especially when a well-developed body of state law already exists. While a more convincing policy argument in favor of the DTSA is that trade secret misappropriation is “wrong” and that U.S. businesses are “harmed” when their trade secrets are taken,

Review).

5. See Mark F. Schultz & Douglas C. Lippoldt, *Approaches to Protection of Undisclosed Information (Trade Secrets): Background Paper* 30–32 (OECD Trade Policy Papers, Working Paper No. 162, 2014) (providing a trade secrets protection index and component scores by country), <http://dx.doi.org/10.1787/5jz9z43w0jnw-en>.

those arguments are already addressed by the existing body of state and federal laws that provide civil remedies and criminal penalties for trade secret misappropriation.

The rhetoric surrounding the proposed legislation speaks to threats of cyber-espionage and the problem of foreign spies, but the DTSA does not directly address those concerns by defining new or different wrongs. Rather, it merely adopts the UTSA definition of wrongful acquisition of trade secrets through “improper means,” which has long been defined to include “espionage through electronic or other means.”⁶ Such behavior is not only already prohibited by the UTSA⁷ but is also a federal crime according to the existing language of the EEA,⁸ and the Computer Fraud and Abuse Act (CFAA) already exists to directly address the problem of computer hacking.⁹

Some argue that a federal law that amends the EEA is needed to take advantage of its extra-territorial provision so that U.S. companies might be more successful in pursuing actions against individuals who are located in, or move to, foreign countries.¹⁰ The extra-territorial provision of the EEA is weak, however, particularly with respect to individuals who reside in foreign countries. Significantly, § 1837 of the EEA does not apply to non-U.S. citizens and non-permanent resident aliens of the U.S. who are alleged to have misappropriated trade secrets located outside the United States. Although the extra-territorial provision of the EEA might apply to foreigners who commit an act within the U.S. “in furtherance of the offense,” it does not solve the related issues of whether U.S. courts can obtain personal jurisdiction over such individuals and whether any resulting judgment can be enforced.

6. H.R. 3326 § 2(b).

7. UNIF. TRADE SECRETS ACT § 1(1) (UNIF. LAW COMM'N 1985).

8. 18 U.S.C. §§ 1831–39 (2012).

9. *Id.* § 1030.

10. See R. Mark Halligan, *Protection of U.S. Trade Secret Assets: Critical Amendments to the Economic Espionage Act of 1996*, 7 J. MARSHALL REV. INTELL. PROP. L. 656, 669 (2008) (“The proposed amendments to the EEA would extend the benefits of extraterritorial jurisdiction to EEA civil actions which, in turn, will provide significant new protection against the rampant economic espionage attacks directed toward U.S. companies.”).

Whittling away the substantive arguments in favor of the DTSA, one is left with the impression that the principal reason behind the proposed legislation is the preference of large U.S. companies to pursue litigation in federal, instead of state, courts. One reason for this preference is undoubtedly the fear that the proverbial “federal case” instills in some litigants and their lawyers (thereby often leading to quick capitulation of even weak cases), but there is also the perception that federal court procedures and federal judges are simply better at handling business litigation.

III. The Costs of the DTSA

Against the asserted benefits of the DTSA, Congress should consider its costs. As further explained below, these costs include the anticipated increase in the number of trade secret cases that will be filed in federal court, plus the increased complexity of federal litigation, particularly in the early stages of trade secret litigation.

A. More Trade Secret Cases Will Be Filed in Federal Court

Currently, a significant number of trade secret cases are filed in federal court based upon diversity jurisdiction. With the passage of the DTSA, this number will increase to include cases where the factual predicates for federal subject matter under the DTSA (discussed below) can be shown. While this number is unlikely to be 100% of all trade secret cases filed in the U.S., it can be anticipated that a large percentage of all cases currently filed in state courts will, in the future, be filed in federal courts. This will increase the case load of the federal judiciary.

As noted previously, one of the asserted justifications for the DTSA is that federal courts are better at handling complex business litigation, but then why not transfer other state court business cases to federal court? For instance, why not grant federal subject matter jurisdiction to breach of contract claims that, to use the jurisdictional language of the DTSA, “relate to a

product or service used in or intended for use in, interstate commerce”¹¹ More importantly, does such an argument justify the adoption of a federal law that essentially mirrors state law?

One reason we have state courts and state litigation, including for complex business litigation, is because federal court jurisdiction is limited by the U.S. Constitution and because we have historically had faith in the ability of state court judges to handle such matters. Another reason is that there are significant costs associated with the creation of new federal causes of action. These reasons alone counsel against adoption of the DTSA.

B. The Constitutional Basis for the DTSA Will Be Challenged Frequently

Because the jurisdiction of the federal courts is limited by the U.S. Constitution,¹² a federal court is precluded from making a decision on the merits of a case unless it is first determined that the court has proper jurisdiction.¹³ In the case of alleged subject matter jurisdiction, this means that it must first be shown that the lawsuit “arises under the laws of the United States.” While the DTSA will be the law that provides subject matter jurisdiction for federal courts to hear trade secret misappropriation claims, whether the factual predicates for such jurisdiction can be met is a different—and sure to be highly litigated—question.

As a law based upon Congress’s powers under the Commerce Clause of the U.S. Constitution,¹⁴ it is necessary for the DTSA to

11. Defend Trade Secrets Act of 2015, H.R. 3326, 114th Cong. § 2(a) (2015).

12. See U.S. CONST. art. III, § 2 (delineating federal judicial power).

13. See *Ruhrigas AG v. Marathon Oil Co.*, 526 U.S. 574, 577 (1999) (noting that personal jurisdiction is an essential element of a district court’s jurisdiction, without which the court is powerless to proceed adjudication).

14. See 18 U.S.C. § 1832(a) (2012) (“Whoever, with intent to convert a trade secret, that is related to a product or service used in or intended for use in interstate or foreign commerce”); Defend Trade Secrets Act of 2015, H.R. 3326, 114th Cong. § 2(a) (2015) (“An owner of a trade secret may bring a civil action under this subsection if the person is aggrieved by a misappropriation of a trade secret that is related to a product or service used in, or intended for use in, interstate or foreign commerce.”).

THE DTSA: THE LITIGATOR'S FULL-EMPLOYMENT ACT 315

include a provision that establishes a sufficient and plausible connection between the alleged wrongdoing (trade secret misappropriation) and interstate commerce. In an attempt to make this connection, the DTSA includes language which reads:

An owner of a trade secret may bring a civil action under this subsection if the person is aggrieved by a misappropriation of a trade secret that is related to a product or service used in, or intended for use in, interstate or foreign commerce.¹⁵

While the intent of this language is clearly to satisfy the interstate commerce (and therefore, Constitutional) requirement, its practical implications—particularly in cases where preliminary relief is sought—have not been thought through and are bound to lead to various procedural motions concerning the Constitutional adequacy of both the language of the DTSA and the facts of cases brought under it. This is because proof of a connection with interstate commerce is not only an element of the cause of action that must be pleaded and proved by the plaintiff, but it is an essential factual and Constitutional predicate for federal court jurisdiction.

The essential problem with the DTSA's jurisdictional clause is that trade secrets, unlike trademarks, are—by definition—not visible to the world in a way that their connection to interstate commerce can easily be understood and tested by the courts. Furthermore, even when applying the broad definition of “in commerce” that is a feature of trademark jurisprudence,¹⁶ because the breadth and nature of trade secrets is different from trademarks, it is likely that a significant number of trade secrets exist in the United States that are not “related to a product or service that is used or intended for use in interstate commerce.” As a consequence of these two facts, it is also likely that trade secret litigation brought under the DTSA will involve frequent challenges to the jurisdiction of the federal courts, at great costs to the litigants and the federal judiciary.

15. H.R. 3326 § 2(a).

16. *See* *Rescuecom Corp. v. Google Inc.*, 562 F.3d 123, 127 (2d Cir. 2009) ([C]omplaint fails to state a claim under the Lanham Act unless it alleges that the defendant has made “use in commerce” of the plaintiff's trademark as the term “use in commerce” is defined in 15 U.S.C. § 1127.”).

But it is not just the litigation costs that should be of concern. Of even greater concern, particularly to trade secret owners, is how the jurisdictional clause of the DTSA threatens the secrecy of the alleged trade secrets and is likely to slow down trade secret litigation—particularly at the preliminary relief stage. By specifying a use requirement, plaintiffs in federal trade secret cases will be required to plead (in accordance with well-pleaded complaint jurisprudence)¹⁷ significant facts about their trade secrets that they ordinarily do not like to disclose early in a case. Specifically, they will not only have to allege the existence of viable and subsisting trade secrets, but also must disclose which products or services sold in interstate commerce are “related to” those secrets.

Because all trade secret owners like to delay the disclosure of specifics about their trade secrets until after the pleading stage of a case, due to the risk of inadvertent disclosure, the need to provide more specifics during the pleading stage will put such trade secrets at greater risk. Additionally, this pleading requirement will allow defendants to inquire deeper into plaintiffs’ business operations in order to determine whether and how the alleged trade secrets are “related to” interstate commerce.

As the key factual predicate for federal court jurisdiction, it is predictable that defendants in trade secret cases will challenge the jurisdiction of the federal courts by arguing that there are no alleged trade secrets and, even if there are, that such trade secrets are not related to a product or service that is used, or intended for use, in interstate commerce. In many types of cases, including criminal prosecutions under the EEA, a decision with respect to this issue might wait until after the discovery phase of a case, but civil trade secret cases are unlike most civil cases.

17. See, e.g., *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009)

To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to “state a claim to relief that is plausible on its face.” A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged.

(citation omitted).

Usually they involve requests for prompt preliminary relief (including the DTSA's proposed civil seizure remedy, discussed below), which federal courts have no power to grant without proper jurisdiction. Thus, cases brought under the DTSA are likely to require early discovery and pleadings concerning the factual basis for federal court jurisdiction, which is likely to both delay the grant of preliminary relief and complicate the normal processes of the federal courts.

Further complicating matters, if the existence of trade secrets is the necessary factual predicate for federal subject matter jurisdiction, what happens when—as happens in many trade secret cases—the alleged trade secrets cease to be trade secrets during the pendency of federal court litigation? If the existence of a trade secret related to a product or service in interstate commerce is the linchpin for federal subject matter jurisdiction, then arguably, the federal courts will lose their jurisdiction once the subject trade secrets cease to exist.

Another problem with the jurisdictional language of the DTSA is that it is necessarily limited and, thus, favors some types of trade secrets over others. For instance, it does not apply to trade secrets that are not in use or intended for future use, such as the so-called “negative information” that is protected under the UTSA.¹⁸ It also does not protect information concerning a company's research and development efforts that have not reached a point where a real (as opposed to a hypothetical) use has been determined. Perhaps most significantly, it would not apply to business information such as marketing plans and financial information concerning a business's overall operations unless, in some highly attenuated way, the language “related to” is construed to mean any information that somehow touches “a product or service used in interstate commerce.” In any case, what “related to interstate commerce means” will be a highly litigated issue.

C. The Proposed Seizure Remedy Is New and Untested and Is Likely To Be Highly Contested

18. UNIF. TRADE SECRETS ACT § 1(4) (UNIF. LAW COMM'N 1979).

One type of preliminary relief that a plaintiff is likely to seek in a case brought under the DTSA is the new and untested civil seizure order that is the central feature of the DTSA. In pertinent part, it provides that a plaintiff in a trade secret case may seek an *ex parte* order “providing for the seizure of property necessary to prevent the propagation or dissemination of the trade secret that is the subject of the action.”¹⁹

Modeled after similar remedies that are available under federal law for the seizure of products that bear counterfeit trademarks,²⁰ the proposed new trade secret remedy suffers from the same fundamental problem that the jurisdictional clause does; namely, trade secrets are not the same as counterfeit products. Counterfeit products are tangible and can be seen, handled, and physically seized. Trade secrets, on the other hand, need not exist in tangible form and are not readily visible. So what exactly is “the property” that will be seized under the civil seizure provisions of the proposed law? This is likely to be a highly litigated issue, particularly if the subject property is not the tangible manifestation of the trade secrets themselves, but something else—for instance, the computer system of an ongoing business.²¹

Although trade secret owners undoubtedly view this new remedy as a great addition to trade secret law, given the jurisdictional problems discussed above and the detailed requirements of the proposed remedy, a civil seizure order is bound to be met by fierce opposition and emergency motions for reconsideration that question the subject matter jurisdiction of the federal courts and the merits and scope of the proposed order. Further complicating this new remedy, and taking additional time and energy of the litigants and the federal courts, are the provisions of the proposed law that require: (1) that law

19. H.R. 3326 § 2(a).

20. See 15 U.S.C. § 1116 (2012) (“The several courts vested with jurisdiction of civil actions arising under this chapter shall have power to grant injunctions, according to the principles of equity and upon such terms as the court may deem reasonable . . .”).

21. For a more in-depth critique on this provision of the DTSA, see Eric Goldman, *Ex Parte Seizures and the Defend Trade Secrets Act*, 72 WASH. & LEE L. REV. ONLINE 284 (2015).

enforcement personnel be involved in the execution of civil seizure orders; (2) that federal courts take possession of the seized property; and (3) that defendants be allowed to obtain specified remedies when such orders are improperly granted.²²

The foregoing requirements add up to tremendous litigation costs that many targets of trade secret litigation—often, small businesses and start-up companies—are either unlikely to be able to afford or that will divert their attention and resources from their businesses. If the history of trade secret litigation in the United States revealed that the vast majority of plaintiffs won their cases, perhaps such costs would be justified as a means to protect legitimate trade secrets. But the reality is that such claims are often brought when no protectable trade secrets exist, often because the plaintiff is upset that a former employee left its employ to start a competitive business. Skewing the balance of trade secret litigation in favor of large companies that can afford the added litigation costs may provide some better and more efficient outcomes for those companies, but at the cost of making it more difficult for former employees of companies who have a good idea and the entrepreneurial bug to start a new business. Thus, Congress should think carefully about whether the dampening of the entrepreneurial spirit is a cost that it is willing to pay for a law that is largely duplicative of state law.

D. There Is No Federal Jurisprudence of Trade Secret Law to Fill the Gaps of the DTSA

Adding further to the costs of the DTSA is the fact that trade secret litigants and the federal judiciary will be required to spend a lot of time and energy figuring out how to apply the new federal law, including determining when and where it is appropriate to either borrow from state trade secret principles to fill gaps or create “new” federal trade secret jurisprudence. One can predict that, given the new playing field created by the DTSA, attorneys for both plaintiffs and defendants will argue for the creation of federal trade secret principles over established state law

22. H.R. 3326 §§ 2(a)(2)(E), 2(a)(2)(D), 2(a)(2)(G).

principles when it suits their client's interests and that numerous appeals will result.²³

Because trade secret law developed in the United States through the common law process, there is currently no federal trade secret jurisprudence, except the little that has developed under the EEA's criminal provisions. While this may seem like an insignificant fact, it is certain that the federal courts will be called upon to determine numerous issues that are not spelled out in the DTSA, but which have largely been resolved under each state's case decisions. Thus, far from improving the uniformity of trade secret law, the DTSA will create uncertainty for decades until a body of federal trade secret jurisprudence is developed. Even then, there will be two bodies of trade secret law in the U.S., likely leading to confusion and forum shopping.

One issue in particular that is sure to be highly contested concerns the doctrine of inevitable disclosure, which has been rejected by some state courts as an improper implied non-compete agreement, while embraced by others.²⁴ The remedies provision of the DTSA contains language that, at once, might be interrupted to both endorse and reject the doctrine of inevitable disclosure, thereby adding to the confusion that is sure to follow enactment of the DTSA. It states that injunctions can be ordered to prevent:

[A]ny actual threatened misappropriation described in paragraph (1) on such terms as the court deems reasonable, provided the order does not prevent a person from accepting as

23. There are examples of this debate in other areas of federal law. For instance, see the copyright case of *CCNV v. Reid*, 490 U.S. 730 (1989), where the parties and amici fiercely debated whether state law principles of agency should apply or a new definition of employment should be recognized.

24. Compare *Whyte v. Schlage Lock Co.*, 101 Cal. App. 4th 1443, 1447 (2002) ("In this opinion, we reject the inevitable disclosure doctrine. We hold this doctrine is contrary to California law and policy because it creates an after-the-fact covenant not to compete restricting employee mobility."), with *Cardinal Freight Carriers, Inc. v. J.B. Hunt Transp. Servs., Inc.*, 336 Ark. 143, 152–55 (1999) (noting that there was sufficient evidence to show threatened or inevitable misappropriation of former employer's trade secrets by former employees who had taken jobs with competitor to justify issuance of injunction to prevent new employer from conducting new business with four of former employer's customers for one year).

THE DTSA: THE LITIGATOR'S FULL-EMPLOYMENT ACT 321

offer of employment under conditions that avoid actual or threatened misappropriation described in paragraph (1).²⁵

By stating a proviso to the grant of an injunction against an employee, this language could be read to endorse the free trade, free competition, and employee mobility sensibilities of states like California that severely restrict the enforceability of non-compete agreements. But it can also be read to endorse the inevitable disclosure inquiry that California and other states reject. Either way, given the stakes surrounding this issue, the federal courts will be called upon frequently to settle an issue that is fairly well settled in all of the fifty states, albeit not in a uniform way due to the different values that each state brings to the issue.

IV. Conclusion

The debate concerning the DTSA is not a debate about a new law (like the CFAA) that is needed to address an entirely new problem affecting interstate commerce. Rather, putting rhetoric aside, it is a debate about whether some of the trade secret cases that are currently handled and enforced in state courts would be handled better and more efficiently in federal courts and the difficulties that some trade secret owners have had in enforcing their putative rights in some cases. But trade secret litigation, like all commercial litigation, is often difficult and costly and, for the reasons set forth above, adoption of the DTSA is actually likely to increase such costs. More importantly, while the DTSA may be a boon for large corporations who prefer to litigate in federal courts, it will not be a boon for other businesses—often small businesses and start-up companies—who must engage in the defense-side of such litigation. It will also not be a boon for the federal judiciary that must incur the costs of increased caseloads at both the trial and appellate levels. A better, and less costly, approach is for Congress to address concerns about cyber-espionage and foreign spies directly, leaving the more common trade secret cases involving allegations against former employees

25. H.R. 3326 § 2(a).

to be resolved by state courts where they have been effectively resolved for nearly 200 hundred years.