The Asset Management Industry
SERVING INDIVIDUAL INVESTORS
INVESTMENT COMPANY INSTITUTE

MEMO# 26969

February 5, 2013

Congress Closes Loophole that Kept Former Employee from Being Criminally Liable for Theft of Proprietary Trading System

[26969]

February 5, 2013

TO: COMPLIANCE MEMBERS No. 9-13
PRIVACY ISSUES WORKING GROUP No. 4-13
SEC RULES MEMBERS No. 17-13
SMALL FUNDS MEMBERS No. 11-13
TECHNOLOGY COMMITTEE No. 4-13 RE: CONGRESS CLOSES LOOPHOLE THAT KEPT FORMER EMPLOYEE FROM BEING CRIMINALLY LIABLE FOR THEFT OF PROPRIETARY TRADING SYSTEM

As we previously informed you, last June the U.S. Court of Appeals for the Second Circuit overturned the criminal conviction of a computer programmer who had been found guilty of two counts of stealing and transferring proprietary computer source code used in his employer's high frequency trading system. [1] The conviction was overturned, in part, based on the court's determination that the programmer had not, in fact, violated the portion of the Economic Espionage Act of 1996 (the "EEA") that he was convicted of violating. [2] The relevant section of the EEA read as follows:

> Whoever, with intent to convert a trade secret, that is related to or included in a product that is produced for or placed in interstate or foreign commerce, to the economic benefit of anyone other than the owner thereof, and intending or knowing that the offense will, injure any owner of that trade secret, knowingly . . . without authorization . . . downloads, uploads, . . . transmits, . . . or conveys such information is guilty of a federal offense, and may be imprisoned for up to 10 years. [Emphasis in original.]

The court noted that the scope of this provision is limited to products that are "produced for" or "placed in" interstate or foreign commerce. Because the employer's high frequency trading system was neither 'produced for' nor 'placed in' interstate or foreign commerce, the employee could not be guilty of violating this provision of the EEA. His conviction was, therefore, overturned.

Last December, the “Trade Secrets Clarification Act of 2012” was signed into law to address the above loophole in the EEA. [3] The Act closes this loophole by revising the italicized language in the above except to read instead “that is related to a product or service used in or intended for use in interstate or foreign commerce.” In addition to closing the loophole, the new Act also expands the scope of the EEA to “services” used in or intended for use in interstate or foreign commerce.

Tamara K. Salmon
Senior Associate Counsel

endnotes

[1] See Institute Memorandum No. 26244 (June 15, 2012), which summarized the facts of the case and the court’s holding.

[2] Apparently, after the programmer’s conviction was overturned by the court, he was criminally charged by the Manhattan District Attorney with the unlawful use of secret scientific material and duplication of computer-related material, each of which is a felony under New York State law. If convicted on these state charges, he could be imprisoned for 1-4 years. See Former Goldman Programmer is Arrested Again, Peter Lattman, NY Times.com (August 9, 20112). This case remains pending.

[3] A copy of the Act is available at: http://www.gpo.gov/fdsys/pkg/BILLS-112s3642enr/pdf/BILLS-112s3642enr.pdf.