August 2017

quinn emanuel

quinn emanuel urquhart & sullivan, llp | business litigation report

los angeles | new york | san francisco | silicon valley | chicago | washington, d.c. | houston | seattle | tokyo | london
mannheim | hamburg | munich | paris | moscow | hong kong | sydney | brussels | zurich | shanghai | perth

Supreme Court Highlights Importance of Statute-Specific Venue Rules

The Supreme Court upended nearly thirty years of practice when it ruled, in the *TC Heartland LLC v. Kraft Foods Group Brands LLC* U.S. __, 137 S.Ct. 1514 (May 22, 2017), that actions for patent infringement may only be brought in the location the alleged infringement occurred or in the alleged infringer's state of incorporation. The decision alters the approach patent plaintiffs and courts must use to determine what venue is appropriate for each case. The decision also shines a spotlight on one of the more confusing aspects of federal civil procedure: the question of residence for the purpose of venue.

Venue and Residence: A Historical Overview

Unlike the doctrines of personal and subject-matter jurisdiction, which concern the *authority* of a court to adjudicate a dispute, the rules of venue dictate *which courts* among the 94 federal judicial districts are available as a forum for the litigants. Since 1789, Congress has provided specific criteria for identifying the appropriate court or courts—but those criteria have changed over time.

(continued on page 2)

INSIDE

Leading Competition and Regulatory Lawyers Join Brussels Office

Stephen Mavroghenis and Miguel Rato have joined the firm as partners in the Brussels office. Both join from Shearman & Sterling where Stephen was the leader of Shearman & Sterling's worldwide antitrust practice and managing partner of the Brussels office. Stephen's practice covers the full range of competition and antitrust matters, including complex mergers and joint ventures, monopolization (industry dominance), government investigations and EU litigation, vertical arrangements, state aid and cartel investigations in Europe the USA and Asia, as well as contentious matters in the EU. Miguel also advises clients on contentious and non-contentious EU competition law issues, with a particular focus on complex unilateral conduct matters, transactions, and IP licensing in high-tech industries. Q

Former U.S. Ambassador to Czech Republic Rejoins Quinn Emanuel

Andrew Schapiro has rejoined the firm as a partner. Andy left the firm in late 2014 to serve as the U.S. Ambassador to the Czech Republic. He will now divide his time between the firm's Chicago and New York offices. With a focus on intellectual property, white-collar criminal defense, and appeals, Andy has more than two decades of trial and appellate experience representing major corporations and individuals in sensitive, high-profile, and high-stakes matters. He has first-chaired numerous trials, managed large litigation teams, and argued and won important appeals in state and federal courts. As U.S. Ambassador, Andy led America's 240-member, multi-agency diplomatic post in Prague through a time of significant changes and challenges in Europe, overseeing all aspects of the U.S. relationship with an important Central European NATO ally and trading partner. Andy is a *magna cum laude* graduate of Harvard Law School, where he was an editor of *The Harvard Law Review* and winner of the Sears Prize. He clerked for Judge Richard A. Posner on the Seventh Circuit Court of Appeals, and then for Justice Harry Blackmun on the U.S. Supreme Court. He then practiced for five years as a trial lawyer with the Federal Defenders' Office for the S.D.N.Y., defending individuals accused of a wide range of federal offenses and serving as lead counsel in numerous jury trials with favorable verdicts. Q

Initially, venue in a civil suit was proper both where the defendant was an "inhabitant" and where the defendant could "be found" to be served with process. This came to be seen as subject to abuse, as it allowed plaintiffs to force defendants to litigate away from their home states if they happened to become subject to service of process by, for example, travelling to another state. Congress therefore amended the law in the late 19th century, restricting venue to the district in which the defendant was an "inhabitant" (or, in a case between citizens of different states, the district where either party was an "inhabitant").

These early venue statutes naturally raised the question of where exactly a party was an "inhabitant," especially if the party in question was a corporation. The answer, according to an 1892 Supreme Court case, was that a corporation was an "inhabitant" only of the state in which it was incorporated. As a result, a corporation could only be sued in a civil suit in the federal courts in its state of incorporation (or in the state of the plaintiff's incorporation, if different), regardless of where the alleged wrongdoing took place and regardless of whether the corporation was subject to the jurisdiction of federal courts in other states.

With the continued growth and increased national scope of corporate activity in the first half of the twentieth century, the strict limits on venue in cases involving corporate defendants came to be seen as unfair to plaintiffs. If, for example, a Connecticut corporation was doing business in New Jersey and its activities caused injury to a resident of Virginia travelling through New Jersey on her way to New York, the plaintiff would be forced to choose between filing suit in Virginia or in Connecticut; the federal courts in New Jersey, closest to the activities giving rise to the claim, would be unavailable as a venue for the claim.

In response to such concerns, Congress once again liberalized the venue rules in 1948 by passing what has come to be known as the "General Venue Statute" (codified at 28 U.S.C. § 1391), which substituted the term "resident" for "inhabitant" in the prior law and also, for the first time, expressly defined the residence of a corporate defendant as "any judicial district in which it is incorporated or licensed to do business or is doing business." Together with further amendments in the 1960s that permitted venue in the locations where the events giving rise to the claim occurred (so-called "transactional venue"), the 1948 law represented a clear shift away from the strict approach to corporate residence that had been embodied in the earlier venue statutes.

Additional amendments to the General Venue Statute in 1988 and 2011 furthered the expansion of venue in cases involving corporate parties. In 1988, Congress redefined the residence of a corporate defendant to include "any judicial district in which it is subject to personal jurisdiction at the time the action is commenced." Congress further refined the definition in 2011, providing that "for all venue purposes," the residence of a corporate defendant includes any judicial district in which it "is subject to personal jurisdiction with respect to the civil action in question." Since personal jurisdiction essentially depends on the availability of lawful service of process on the defendant, the 2011 amendments to the General Venue Statute appeared to take the general federal venue rules full circle: as in the earliest federal venue statute, a corporate defendant could again be sued not only in its state of incorporation but in any state where it is subject to service of process.

TC Heartland *and the Patent Venue Statute*

The 2011 amendments to the General Venue Statute appear to provide a simple framework for determining whether venue is proper in a civil suit against a corporate defendant: if the defendant is incorporated in the state in which the court sits, or if it has sufficient contacts with the state to be properly served with process and thereby become subject to the court's personal jurisdiction, then venue is proper. The Supreme Court's decision in *TC Heartland* is a reminder that things are not always that simple.

Kraft Foods Group Brands LLC, the plaintiff in the case, filed suit against TC Heartland LLC in federal court in Delaware, alleging patent infringement. *TC Heartland*, 137 S.Ct. 1517. Although the allegedly infringing products had been shipped into Delaware—an act that could give rise to personal jurisdiction over TC Heartland in Delaware federal courts—the company sought a transfer of venue to Indiana where it was incorporated and headquartered, arguing that a 1957 Supreme Court case had interpreted a venue-related provision of the Patent Act to mean that an alleged infringer could only be sued in its state of incorporation *Id.* Relying on a 1990 decision of the Federal Circuit, the district court and the Court of Appeals both rejected TC Heartland's argument, ruling that the word "resident" in the Patent Act's venue provision (the 'Patent Venue Statute') had the same meaning as the word "resident" in the General Venue Statute—namely any state in which a corporate defendant "is subject to personal jurisdiction with respect to the civil action in question." *Id.* at 1517-18.

In an 8-0 opinion, the Supreme Court reversed. Writing for the Court, Justice Thomas noted that as far back as 1897, Congress had provided separate venue rules specifically applicable to cases under the Patent Act that limited venue to the district in which the defendant was an "inhabitant" (as well as districts in the location where the alleged infringement occurred). *Id.* at 1518. Although Congress had subsequently replaced the word "inhabitant" with the word "resident" in the Patent Venue Statute (now codified at 28 U.S.C. § 1400(b)), it had neither included a further definition of "resident" in the Patent Venue Statute nor indicated, explicitly or implicitly, that the words of the Patent Venue Statute were to be interpreted according to the terms of the General Venue Statute. *Id.* at 1520. In fact, even though the General Venue Statute expressly states that its definition of "resident" is to apply "for all venue purposes," the Supreme Court held that the General Venue Statute's introductory phrase "Except as otherwise provided by law" constituted a "safe-harbor" that preserved the separate and independent effect of special venue rules in other statutes. *Id.* at 1521.

As a result, although both the General Venue Statute and the Patent Venue Statute allow for venue in the district where a corporate defendant is a "resident," the term "resident" can—and does—mean different things in each statute. In the General Venue Statute, it is expressly defined as any district in which the defendant is subject to personal jurisdiction. In the Patent Venue Statute, it retains the meaning it has always had: a corporate defendant in a patent infringement suit resides only in its state of incorporation.

Applying its reasoning to the facts of the case, the Supreme Court held that because TC Heartland was not incorporated in Delaware it was therefore not a "resident" of Delaware for purposes of the Patent Venue Statute. *Id.* Coupled with the fact that TC Heartland was an Indiana corporation headquartered in Indiana, the Court's ruling meant that the federal courts in Delaware constituted an impermissible venue for Kraft's patent infringement suit under the Patent Venue Statute.

The Continued Importance of Special Venue Statutes

The Supreme Court's decision in *TC Heartland* has attracted considerable attention among the patent bar, because its holding may effect a significant change in the practice of patent litigation in the United States. Since 1990, plaintiffs alleging patent infringement have taken advantage of the Federal Circuit's now-overruled interpretation of "residence" in the Patent Venue Statute to file suit in specific federal districts—most famously the Eastern District of Texas—that are perceived as more favorable to infringement claims but that often have no immediate connection to the parties or the dispute. In the wake of *TC Heartland*, patent plaintiffs may have to make a greater showing of a connection between their desired forum and the acts of infringement and business activities of the alleged infringer, or risk transfer to the courts in the state of the defendant's incorporation.

Yet *TC Heartland* is important beyond the world of patent litigation, because it highlights the importance and continued viability of special venue provisions in federal statutes. The Patent Act is not unique in providing specific venue rules for claims arising under it; commentators have identified at least a hundred separate federal statutes that establish special venue rules, many of which tie venue in at least certain circumstances to the "residence" of one or both of the parties.

In fact, *TC Heartland* can be seen as simply the latest in a series of Supreme Court decisions exploring the relationship between the General Venue Statute and the various specific venue provisions of other federal statutes. In 1942, and again in 1957, the Supreme Court held that the Patent Venue Statute was the "exclusive provision controlling venue in patent infringement proceedings" which was "not to be supplemented by" the General Venue Statute. But in the 1966 case *Pure Oil Company v. Suarez*, the Supreme Court came to the opposite conclusion with respect to the venue provisions of the Jones Act governing certain claims involving merchant mariners. Distinguishing its Patent Act decisions, the Supreme Court ruled that the General Venue Statute provided a default rule "that applies to all venue statutes using residence as a criterion, at least in the absence of contrary restrictive indications in any such statute." 384 U.S. 202, 204-05 (1966). More recently, in the 2000 case *Cortez Byrd Chips, Inc. v. Bill Harbert Construction Co.*, the Supreme Court noted that it had applied a restrictive interpretation to the special venue provisions of statutes governing not only patent infringement claims but also litigation against national banks and Title VII employment discrimination claims; according to the Court, these cases "simply show that analysis of special venue provisions must be specific to the statute." 529 U.S. 193, 204 (2000).

In light of *TC Heartland*, therefore, litigants in cases arising under federal statutes should take a close look at any such specific venue rules to determine whether the litigation is proceeding in the right court. An example illustrates the issue. The Federal Interpleader Act allows a party in possession of property to sue two or more people who each have competing claims to the property, effectively forcing the claimant-defendants to resolve their dispute rather than subjecting the stakeholder-plaintiff to multiple separate claims on the same property. Like the Patent Act, the Federal Interpleader Act contains a special venue provision stating that an interpleader action under the Act may be filed "in the judicial district in which one or more of the claimants reside[s]." 28 U.S.C. § 1397.

Does "resides" in the Federal Interpleader Act mean the same thing as "resides" under the General Venue Statute, or—as in the Patent Venue Statute—does it have a different meaning? The answer might significantly affect a stakeholder's venue options. As noted above, the General Venue Statute defines the residence of a corporate defendant in terms of its susceptibility to personal jurisdiction, which can be established through lawful service of process. The Federal Interpleader Act, however, allows for nationwide service of process by stakeholders on claimants. 28 U.S.C. § 2361. If the definition of "residence" in the General Venue Statute applies to the Federal Interpleader Act, then venue would at least arguably be proper in an interpleader action in any district court in the country, so long as one of the claimants had sufficient ties to the state in question to allow lawful service of process.

In fact, one district court has come to exactly that conclusion. In *Fort Dearborn Life Insurance Co. v. Jarrett*, an Illinois insurer filed an interpleader action in the Western District of Michigan against two individual defendants—both residents of the Eastern District of Michigan—and a corporate defendant incorporated in Delaware with its principal place of business in Indiana. Absent any controlling decisions from higher courts, and absent any specific definition of "resident" in the Federal Interpleader Act, the district court concluded that the definition of "resident" in the General Venue Statute should apply. The district court then concluded that because the Federal Interpleader Act permits nationwide service of process, "there effectively is nationwide venue in any statutory-interpleader action having a corporate claimant." --- F. Supp. 2d ---, 2010 WL 203537, at *2 (W.D. Mich. May 20, 2010).

Notably, the Seventh Circuit Court of Appeals came to a contrary conclusion when interpreting the special venue provisions of the Employee Retirement Income Security Act (ERISA). In the 2002 case *Waeltz v. Delta Pilots Retirement Plan*, the court reasoned that if Congress had intended nationwide service of process to suffice to give rise to nationwide venue, it would not have specified other statutory bases for venue such as the place where a retirement plan is administered. 301 F.3d 804, 808-09 (7th Cir. 2002).While the ERISA venue provision focuses on where a party "may be found" rather than where it "resides," the Seventh Circuit's logic could at least arguably apply to statutory venue provisions that include residency among various alternative bases for venue.

TC Heartland is therefore a useful reminder to litigants that even when a federal statute gives rise to a cause of action, that does not mean the cause of action may be litigated in any district court—nor even the district court most convenient to the plaintiff. Parties should be careful to read any special venue provisions closely to determine whether they are likely to be governed by the General Venue Statute, which makes venue co-extensive with personal jurisdiction over a corporate defendant, or whether instead Congress has chosen to restrict—or expand—the list of district courts in which the action can proceed. Q

Disgorgement in SEC Cases Limited to Five Years

Background

On June 5, 2017, the Supreme Court unanimously held in *Kokesh v. Securities and Exchange Commission*, 581 U.S. __, No. 16-529 (2017), that the Securities and Exchange Commission's ("SEC") claims for disgorgement are subject to the five-year statute of limitations set forth in 28 U.S.C. § 2462. The impact of this decision on the SEC's enforcement program is profound, as the SEC has been seeking, and obtaining, disgorgement since the 1970s without regard to a statute of limitations. *Kokesh* will significantly limit the availability of disgorgement to the SEC going forward, and it remains to be seen how the SEC will shift the other remedial levers at its disposal to compensate for the loss.

***Facts in* Kokesh**

Kokesh began in late 2009, when the SEC alleged that Charles Kokesh used two investment adviser firms he owned to misappropriate approximately $34.9 million from four registered funds between 1995 and 2009. Kokesh did so by using the authority of his investment adviser firms to cause the funds to transfer money to the advisers that were not included in their advisory contracts, including salaries for Kokesh and his officers and rent for the advisers' offices. The SEC sought both civil monetary penalties and disgorgement—a remedy intended to recover the defendant's ill-gotten gains. A jury found Kokesh liable for the misappropriation, and the district court then turned to determining remedies.

Section 21(d) of the Securities Exchange Act of 1934 authorizes the SEC to bring civil injunctive actions against alleged violators of the federal securities laws. The Supreme Court has previously held that the five-year statute of limitations of 28 U.S.C. § 2462 applies to the imposition of civil monetary penalties in those proceedings. *See Gabelli v. SEC*, 568 U.S. 442, 454 (2013). The limitations statute provides a five-year limit for the government to seek any "fine, penalty, or forfeiture, pecuniary or otherwise." The district court ordered Kokesh to pay a penalty of $2,54,593, or "the amount of funds that [Kokesh] himself received during the limitations period." *Kokesh* at 4.

The district court next considered the SEC's request for disgorgement of $34.9 million—$29.9 million of which was attributable to Kokesh's conduct outside the statute of limitations. Kokesh objected, arguing that disgorgement was limited by the same five-year limitations period as the civil monetary penalty. The district court disagreed, holding that disgorgement was not a "fine, penalty, or forfeiture" and therefore not subject to it. The district court ordered Kokesh to pay the full disgorgement requested by the SEC, representing his gains from the scheme for the entire 15 year period. Kokesh appealed to the 10th Circuit Court of Appeals, which affirmed the lower court's ruling that disgorgement was not a penalty subject to the five-year statute of limitations.

The Supreme Court's Opinion

The key question for the Supreme Court was whether the SEC's disgorgement was a "fine, penalty, or forfeiture" as described in 28 U.S.C. § 2462. The Circuit Courts of Appeals had split on this question, with the Eleventh Circuit Court of Appeals holding that the statute of limitations did apply to disgorgement claims (*see SEC v. Graham*, 823 F. 3d 1357, 1363 (11th Cir. 2016)) and the First, Tenth, and D.C. Circuit Courts of Appeals holding that it did not (*see, e.g.*, *Riordan v. SEC*, 627 F. 3d 1230, 1234 (D.C. Cir. 2010)).

The Supreme Court stated that whether the relief sought is considered a "penalty" turns on two basic principles: (1) whether the wrong to be redressed is a wrong to the public or a wrong to an individual; and (2) whether the relief sought is for the purposes of punishing the offender and deterring others from engaging in the same behavior or compensating the victim. The Supreme Court found that disgorgement in SEC actions was a penalty because: (1) the SEC sought disgorgement for the violation of public laws as wrongs against the United States; (2) disgorgement has been used historically as a deterrent against other persons committing the same violation; and (3) disgorgement in many cases is not "compensatory," or returned to the victim of the defendant's wrongdoing, because the district court overseeing the action determines how the disgorgement proceeds are distributed.

The SEC argued that its use of disgorgement was not punitive because it served to re-establish the "status quo" that the defendant had disrupted through his or her illegal actions. The Supreme Court was not persuaded—it stated that disgorgement was not remedial for a number of reasons, including: (1) in some cases, a defendant can be ordered to disgorge more than his gains from his illegal conduct, such as in an insider trading case in which a tipper who does not trade is ordered to disgorge the trading profits of a downstream tippee who did; and (2) disgorgement can be ordered without accounting for the defendant's expenses in generating the illegal profits.

Impact

The Supreme Court's decision will likely have a significant impact on the SEC and the consequences will be felt immediately in ongoing litigation or investigations. *Kokesh* itself is a telling example, as the Supreme Court's opinion noted that only approximately 14% of the disgorgement ($5 million of the $34.9 million originally awarded) could be traced to conduct that fell within the limitations period. Additionally, in *In the Matter of Lynn Tilton, et al.*, File No. 3-16462, the SEC's Enforcement Division originally sought approximately $208 million from the defendants in disgorgement. Shortly after *Kokesh* was decided, however, the Division admitted that $45,447,417 of the requested disgorgement was tied to misconduct outside the limitations period and it informed the administrative law judge that it was no longer seeking disgorgement of those funds.

For those who find themselves in the Division of Enforcement's crosshairs, there are several practical considerations to navigating an investigation in the aftermath of *Kokesh*. First, the staff may respond to *Kokesh* by attempting to seek larger penalty amounts, where the statutory guidelines give it considerable flexibility in imposing penalties "for each violation." *See, e.g.*, 17 U.S.C. § 78u(d)(3) (Exchange Act Section 21(d)(3)). So, in a case where a significant amount of disgorgement would be lost to the statute of limitations, it is possible the staff will now instead seek a commensurately larger penalty than it otherwise would have. For example, in a typical offering fraud, the staff may view each misleading offering document sent to investors as a separate violation warranting its own penalty as a mechanism to increase recovery where the action is brought after the statute had run on some of the conduct.

Second, in cases that are headed toward settlement, the staff may ask that a defendant voluntarily undertake to repay harmed investors disgorgement that would otherwise be foreclosed by the statute of limitations, particularly where getting the money back to investors would be straightforward.

Third, barring voluntary undertakings, the SEC may attempt to have courts appoint more receivers. Receivers are appointed by a federal district court judge and are officers of the court, not employees of the SEC. They have broad powers to recover and protect assets for stakeholders and the court. Because receivers operate under the broad equitable powers of the court, they enjoy significant latitude to marshal assets and fashion plans of distribution. Receivers, however, are costly and therefore whether to seek to have one appointed can depend on the value of the potential receivership estate. Post-*Kokesh*, where the SEC may be limited in its ability to recover disgorgement directly, it is possible the SEC will shift its typical cost-benefit analysis for those decisions.

Finally, and importantly, it remains to be seen how *Kokesh* will affect the SEC's—and potential defendants'—approach to tolling agreements. The SEC uses tolling agreements to suspend the statute of limitations, allowing the SEC more time to complete its investigation after it discovers the potential misconduct. *See Gabelli*, 568 U.S. at 454 (holding that statute of limitations of § 2642 begins to tick after the alleged fraud occurs, and the government may not take advantage of the discovery rule). However, those being investigated must agree to the tolling agreement, which they typically do to avoid hasty (and potentially unwarranted) action by the SEC, and to gain time to persuade the SEC to not pursue or to reduce potential charges. When a civil penalty was previously the only SEC relief subject to the limitations period, granting tolling agreements to the SEC was relatively pro-forma for those under investigation. Now *Kokesh* may persuade parties to resist, or negotiate, tolling agreements more strenuously because the tolling agreement also preserves additional disgorgement exposure.

Conclusion

While it is true that *Kokesh* will fundamentally limit the SEC's ability to recover disgorgement, we can be sure that the agency will also adapt its existing approaches to compensate. Precisely how it addresses this new challenge remains to be seen. Kokesh and others may benefit in the short term from this decision, but those under investigation now and in the future should carefully watch the signals from the Division of Enforcement for new approaches to the issue. Q

Securities & Structured Finance Litigation Update

New York's First Department Creates Split Authority on Inducement Claims by Guaranty Insurers, Weighs in on "Backstop" Claims in RMBS Suits. On May 16, 2017, the New York Appellate Division, First Department, issued a decision in *Ambac Assurance Corporation, v. Countrywide Home Loans, Inc.*, --- N.Y.S.3d ----, 2017 WL 2115841 (1st Dep't 2017), that creates a conflict within New York law regarding the elements of an insurer's cause of action for inducement of a contract by misrepresentation. Ambac, a financial guaranty insurer, sued the mortgage loan originator Countrywide over 17 residential mortgage-backed securities ("RMBS") trusts. Ambac had issued unconditional and irrevocable insurance policies for the trusts, which guaranteed payments of principal and interest to the trusts' investors. Ambac alleged it had issued the policies based on Countrywide's application, and that in the application Countrywide purportedly made a series of false statements about its own operations and about the securitized loans.

Reversing the motion court, the First Department held that, to prevail on its inducement by a misrepresentation claim, Ambac had to prove both its justifiable reliance on Countrywide's false statements and also that the false statements caused Ambac's losses—just as is required for a common-law fraud claim. *Id.* at *1. Relying principally on cases outside of the insurance context, the court concluded that New York's Insurance Law §§ 3105 and 3106 do not dispense with the general common-law requirements that fraud plaintiffs must prove loss causation and justifiable reliance. *Id.* at *2. The court also held these Insurance Law provisions did not abrogate the common-law fraud rules by implication. *Id.*

Remarkably, the unanimous *Ambac* panel expressly declined to follow a prior ruling by another unanimous First Department panel in *MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, 963 N.Y.S.2d 21 (1st Dep't 2013), which held insurers did *not* need to prove loss causation to prevail on a claim for inducement by misrepresentation. In *MBIA*, in which the insurer MBIA brought fraud and breach-of-contract claims against Countrywide, the First Department had held that "pursuant to Insurance Law §§ 3105 and 3106, plaintiff was not required to establish causation in order to prevail on its fraud and breach of contract claims." *Id.* at 22.

In *Ambac*, the First Department acknowledged its prior decision in a footnote, but stated: "We decline to follow that part of the decision." *Ambac*, 2017 WL 2115841 at *2 n.3. The court provided no further explanation. As a result, *Ambac* creates a split within the First Department as to whether insurers must establish loss causation in pursuing inducement by misrepresentation claims. Ambac has petitioned the First Department for leave to appeal to the New York Court of Appeals, to resolve the contradictory decisions.

* * *

On May 11, 2017, the New York Appellate Division, First Department, issued a decision in *Bank of New York Mellon, v. WMC Mortgage, LLC*, --- N.Y.S.3d ----, 2017 WL 1946017 (1st Dep't 2017), that clarified the time-frame for bringing certain types of claims for repurchase of defective loans in RMBS. Bank of New York Mellon ("BONY"), as Securities Administrator of an RMBS trust, had brought (among others) claims against WMC Mortgage, which originated the loans, and JP Morgan Mortgage Acquisition Corp ("JPMMAC"), which securitized the loans. BONY sued WMC for breaching the warranties it had made in a mortgage loan purchase agreement, and it sued JPMMAC for breaching a promise it had made in a separate pooling and servicing agreement to repurchase loans that breached WMC's warranties if WMC did not do so.

The motion court and the First Department concluded that JPMMAC's breach-of-warranty claims against WMC were time-barred, because they were brought more than six years after WMC made and allegedly breached its warranties. JPMMAC argued that this meant its "backstop" obligation to repurchase defective loans was effectively void—because, it argued, if WMC was no longer "obligated" to repurchase the loans, then JPMMAC was not required to do so either.

The First Department issued a split decision. It noted that, under Court of Appeals precedent, "[t]he law is now well-settled that the expiration of a time period set forth in a statute of limitations does not extinguish the underlying right, but merely bars the remedy." *Id.* at *3. Despite this, the court held that "WMC's legal obligation to repurchase effectively expired when the statute of limitations ran." *Id.* at *4. The court thus concluded that BONY could not pursue backstop claims based on notices of defective loans provided to WMC after the limitations period for breach-of-warranty claims against WMC had run.

The First Department did allow backstop claims against JPMMAC based on notices of defective loans provided to WMC *before* the limitations period against WMC ran, even though BONY did not file suit against JPMMAC until after that time. The court noted that, under the contracts, BONY was required to seek to enforce WMC's repurchase obligation before JPMMAC's backstop obligations were triggered, hence "[t]o the extent the backstop obligation is attached to a valid WMC liability—albeit one that cannot be enforced against WMC because it is time-barred—the JPMAC obligation came into existence when WMC failed to repurchase." *Id.* at *5. The First Department thus allowed BONY to pursue backstop claims against JPMMAC based on a notice of defective loans provided to WMC shortly before the limitations period for claims against WMC expired.

Both parties have petitioned the First Department for leave to appeal its decision to the New York Court of Appeals.

Product Liability Litigation Update

Hot Topic: Plaintiffs' Efforts to Evade the Burden of Supporting Products Liability Claims with Expert Testimony. The core allegations in many product liability cases are that the manufacturer failed to adequately warn of its product's risks and that the product caused an injury. To meet their burden, the plaintiffs usually proffer expert testimony on issues such as causation and the adequacy of the product warnings. Recently, however, where courts have excluded the plaintiffs' expert evidence as unreliable under *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993), or analogous state standards, the plaintiffs have tried to pivot from proffering expert evidence to arguing instead that they can meet their burden of proof without expert evidence, and survive summary judgment, by relying on non-expert evidence and so-called "admissions" that are taken from the defendant's company documents.

The appeal of these arguments for plaintiffs is obvious. If allowed, plaintiffs would be allowed to sidestep *Daubert*, avoid the expenses associated with expert discovery and briefing, and proceed to trial more quickly and with a lower burden of proof. These issues are front and center in appeals arising out of mass tort litigations that are currently pending before federal and state appellate courts across the country.

For example, in *In re Mirena IUD Products Liability Litigation*, 202 F. Supp. 3d 304 (S.D.N.Y. 2016), *appeal pending*, No. 16-2890(L) (2d Cir. 2016), it was alleged that an intrauterine birth control device, Mirena, caused secondary perforation in the uterus. The multidistrict litigation (MDL) court excluded the plaintiffs' causation experts and granted summary judgment for the manufacturer, Bayer, because the plaintiffs lacked admissible and sufficient evidence of causation—an essential element of all their claims. As the MDL court observed, courts have long held that "[e]xpert testimony is required in cases involving complex causation issues" outside common knowledge and lay experience. *Id.* at 311. The plaintiff argued that no expert testimony was needed because non-expert evidence sufficiently established causation, including FDA-approved labeling for Mirena and Bayer's labeling for another intrauterine product, letters to doctors about Mirena, employee statements, and internal documents.

The MDL court addressed each of these documents and rejected the plaintiffs' arguments, holding that "no court has held that admissions can substitute for required expert testimony, and this Court will not be the first. Such a ruling would disregard the purpose of the requirement for expert testimony, leaving jurors to speculate, and would chill free and frank discussion by manufacturers of drugs or devices." *Id.* at 320. The MDL court added that it "need not go so far as to say that admissions can *never* substitute for expert testimony." *Id.* But "if such statements could ever suffice," they would have to be "clear, concrete or detailed" enough for a jury to find a causal nexus without speculating. *Id.* at 320, 327. The non-expert evidence cited by the plaintiffs, the MDL court found, was far too "ambiguous." *Id.* at 320.

Mirena is currently on appeal in the U.S. Court of Appeals for the Second Circuit where the court will decide whether the non-expert evidence can sufficiently take the place of expert evidence of causation.

Likewise, in *In re Lipitor (Atorvastatin Calcium) Marketing, Sales Practices and Products Liability Litigation*, --- F. Supp. 3d. ---, 2017 WL 87067, at *13-17 (D.S.C.), *appeal pending*, No. 17-1140(L) (4th Cir. 2017), the MDL court held that expert testimony was required to establish the plaintiffs' claims that Lipitor causes diabetes. The court rejected the plaintiffs' arguments that non-expert evidence, such as an internal email and foreign Lipitor labeling, amounted to "admissions" of causation, and granted summary judgment for the defendant manufacturer, Pfizer, because the plaintiffs lacked expert evidence of causation, among other reasons. *Lipitor* is now on appeal in the U.S. Court of Appeals for the Fourth Circuit, where Quinn Emanuel is lead counsel to Pfizer.

Whereas *Mirena* and *Lipitor* illustrate attempts to move away from the requirement of expert evidence on causation, the plaintiffs in another mass litigation, *In re: Zoloft Litigation*, 2017 WL 665299, at *8 (W.Va. Cir. Ct.), *appeal pending sub. nom J.C. v. Pfizer, Inc.*, No. 17-0282 (W. Va. 2017), attempted to make the same argument to avoid the need for expert testimony on whether prescription drug labeling was adequate to apprise physicians of the supposed potential side effects.

Zoloft was litigated before a West Virginia mass litigation panel and involved claims that maternal use of Pfizer's antidepressant, Zoloft, during pregnancy caused children to be born with heart defects. The plaintiffs were unable to present expert evidence to show that Zoloft's labeling failed to adequately warn of the alleged risk of birth defects and sought to rely instead on the defendant's internal documents concerning scientific interpretations of observational data, animal studies and toxicology reports, adverse event reports on birth outcomes, and foreign labeling language regarding use during pregnancy.

The Panel reviewed each of the documents and held that they could not substitute for expert testimony. To the contrary, the court reasoned that the parties' differing interpretation of these internal scientific or medical documents "clearly illustrates the complexity of the issues presented by Plaintiffs' failure to warn claims," putting the issues "beyond the knowledge and experience of the average juror such that expert testimony is required." *Id.* at *17. The plaintiffs appealed this decision, which is currently pending before the Supreme Court of Appeals of West Virginia, where Quinn Emanuel is lead counsel to Pfizer.

Mirena, *Lipitor*, and *Zoloft* are recent examples of tactics by plaintiffs in complex mass tort cases to forestall summary judgment by pivoting from using expert evidence when that evidence is otherwise inadmissible and instead relying more heavily on company documents. For manufacturers faced with products liability exposure, these will be important appellate cases to watch.

Life Sciences Litigation Update

***Mylan Institutional LLC v. Aurobindo Pharma Ltd.*, No. 2017-1645, 2017 WL 2192945 (Fed. Cir. May 19, 2017).** On May 19, 2017, the Federal Circuit issued a precedential opinion in *Mylan Institutional LLC v. Aurobindo Pharma Ltd.* The decision provides useful guidance for the application of the doctrine of equivalents with respect to chemical compounds. In its opinion, the Federal Circuit attempted to address the issue of "sparse and confusing case law concerning equivalents, particularly the paucity of chemical equivalence case law, and the difficulty of applying the legal concepts to the facts." *Id.* at 12. The Federal Circuit also noted that "the law on the doctrine of equivalents as applied to chemical materials is not clear, and its misapplication can lead to unsound results." *Id.*

In *Mylan*, the patentee held two patents concerning methods of making isosulfan blue ("ISB"), a dye used to map lymph nodes, using silver oxide as a solvent (the "process patents"). *Id.* at 2. The patentee also held a third patent concerning the purity of the ISB dye, but that patent is not relevant to the doctrine of equivalents issues discussed in this article. The accused infringer in *Mylan*, Aurobindo Pharma Ltd ("Aurobindo"), claimed that it did not infringe the process patents because it made ISB using manganese dioxide instead of the claimed silver oxide. Mylan countered by arguing that Aurobindo's process infringed the process patents under the doctrine of equivalents because the substitution of manganese dioxide for silver oxide was not sufficient to escape an infringement finding under the either the "function-way-result" test (whether the accused product performs substantially the same function in substantially the same way to obtain the same result) or "insubstantial difference" test (whether the accused product or process is substantially different from what is claimed) established by the Supreme Court in 1950 in *Graver Tank & Manufacturing Co. v. Linde Air Production Co.* Chemically, both manganese dioxide and silver oxide are oxidizing agents, but manganese dioxide has a substantially stronger oxidation strength than silver oxide.

The district court agreed with Mylan and found that Aurobindo likely infringed the process patents under the doctrine of equivalents based on a finding that:

> the difference in oxidation strength between silver oxide and manganese dioxide is "irrelevant" under both the "function-way-result" ("FWR") and "insubstantial differences" tests for equivalence.

Id. at 6. Accordingly, the district court issued a preliminary injunction precluding Aurobindo from making, using, selling, offering to sell, and importing the accused ISB product. *Id* at 2. On appeal, Aurobindo argued that it had raised a substantial question of infringement under the doctrine of equivalents because manganese dioxide works in a substantially different *way* than silver oxide because of the difference in oxidation strength.

In its opinion, the Federal Circuit addressed both the function-way-result test (also referred to as the FWR or "triple identity" test) and insubstantial

(continued on page 11)

Airplane Securitization Victory

For more than five years, a securitization vehicle organized by a now-defunct airplane leasing company unlawfully withheld cash from its noteholders. Retained in 2016, Quinn Emanuel has now put an end to the wrongful conduct, securing victory for the trustee and noteholders by prevailing on a Rule 12(c) motion for judgment on the pleadings and beating back an opportunistic preliminary injunction request in the United States District Court for the Southern District of New York.

Airplanes Limited and Airplanes U.S. Trust, jointly known as Airplanes Group, were in the business of acquiring, leasing, and selling aircraft in various jurisdictions, including Brazil. To finance the initial acquisition of aircraft in 1996, Airplanes Group issued around $3.7 billion of notes.

In connection with its leasing and operations, Airplanes Group worked with GECAS (the airplane financing arm of GE). GECAS was sued in Brazil for unfair collection practices. A Brazilian trial court entered a judgment in 2007 against GECAS and several other entities, including Airplanes Group, for violating Brazilian law. Subsequently, two orders to pay were entered by Brazilian courts directing Airplanes Group to pay as much as $139 million.

As the judgment wound its way up and down the Brazilian appellate system, Airplanes Group ceased payments to A-9 noteholders and began to reserve those funds. Airplanes Group contended that the purpose of those reserved funds was to protect the company if the judgment were ever to be enforced.

While maintaining in its annual reports that it could face a loss of up to $15 million plus interest and legal costs, Airplanes Group ultimately socked away $190 million, which it moved around in a shell-game attempt to keep the funds from noteholders. First, Airplanes Group held the money in an account designated for aircraft maintenance. Yet even after Airplanes Group sold the last of its aircraft in May 2016, the money remained in a maintenance account. Then, intent on keeping the money, Airplanes Group moved the funds into a different account meant for required expenses.

In 2013, a Brazilian appellate court reversed the prior Brazilian judgment in several significant respects—primarily cancelling the orders to pay. The reversal was upheld in 2016 and again earlier this year. Notwithstanding the cancellation of the orders to pay and reversal of the judgment against Airplanes Group, the company still held on to the $190 million.

Quinn Emanuel argued that the reserve was improper because it was not an expense and even if it was an expense, it was not anticipated to become due and payable because of the Brazilian courts' reversal of the judgment against Airplane Group. Granting the firm's motion for judgment on the pleadings, the District Court noted the absurdity of Airplanes Group keeping the reserve in an aircraft maintenance account when there were no more aircraft to maintain and declared that the reserve was unlawful, resulting in an event of default, paving the way for the trustee to access its cash collateral.

Global Victory for Varian Medical Systems

The firm recently guided our Silicon Valley-based client Varian Medical Systems to a walkaway settlement in a global patent war initiated by its primary competitor, Elekta, based in Sweden. Varian is the world's leading developer of cancer treatment systems, with a long history of innovation going back to its pioneering history as one of the first technology companies spun out of Stanford University. In June 2015, Elekta and its licensor Beaumont Hospital sued Varian in the Eastern District of Michigan for patent infringement seeking a permanent injunction and damages. Varian hired our firm to turn the tables. We filed a complaint at the International Trade Commission in Washington, D.C.; another in the District of Delaware; another in the Northern District of California; two cases in Germany; and another in the United Kingdom (in cooperation with another firm). As a result, we had several cases scheduled for trial ahead of Elekta.

Our firm landed a pivotal victory at the International Trade Commission. The dispute was tailor-made for the ITC, which is tasked with protecting American domestic industries from foreign companies that import infringing products. Varian's patented inventions, implemented on its industry-leading radiotherapy systems designed and manufactured in the United States, represented a breakthrough in cancer therapy. Using these systems, cancer treatment sessions that previously took 20 or 30 minutes now took only 2 or 3 minutes—making cancer treatments more effective, safer, and available to more patients. The patents' inventor received numerous awards for his pioneering work, and his published paper on the subject became the most cited paper in the history of medical physics. Most people in the field initially did not believe the inventions could work; one of Varian's competitors offered a $250,000 reward for anyone who could show it worked better than existing treatments. This initial skepticism, followed by the resounding success of the inventions and widespread adoption by others in the industry, was a textbook demonstration of the novelty of the inventions.

At the ITC trial, this theme took center stage. Testimony of Varian's witnesses and cross-examination of Elekta's demonstrated that Varian's patents revolutionized the radiotherapy field and that Elekta used these inventions in its latest equipment. In a 465-page decision dated October 27, 2016, the judge found infringement of all three patents litigated by Quinn Emanuel and recommended an exclusion order barring importation of Elekta's infringing radiotherapy systems. After Elekta requested review of the decision, the judge reaffirmed his findings on March 31, 2017 that the patents were not invalid and that there was a violation. Less than one week later, facing potentially severe disruption to U.S. sales, Elekta agreed to settle all pending disputes with Varian, resulting in no payments exchanged between the parties and no future financial obligations. Q

(Practice area updates continued from page 9)

differences test. The Federal Circuit explained that the "chemical arts" were generally not well-suited for consideration under the triple identity test. *Id.* at 13. Specifically, the Federal Circuit explained:

> Especially when evaluating an equivalents dispute dealing with chemical compositions having many components, chemical compounds with many substituents (which are usually claimed as separate limitations), and those having a medical or biological use, it is often not clear what the "function" or "way" is for each claim limitation. How a particular component of a composition, or substituent of a compound, functions in a human or animal body, or in what way, may not be known or even knowable (although, as technology evolves, that may change). And precedent requires that, for infringement under the doctrine of equivalents, each limitation must satisfy an equivalence test.

Id. at 14. In the context of admonishing the district court not to ignore the "way" prong of the triple identity test, the Federal Circuit explained that the "function" and "way" portions of the triple identity test often will overlap. *Id.* at 15.

The Federal Circuit further explained that "a compound may appear to be equivalent under the FWR test, but not under the substantiality of the differences test" and used aspirin and ibuprofen as examples:

> consider the well-known compounds aspirin and ibuprofen, which chemists would not usually consider to be structural equivalents under the insubstantial differences test. Chemical compounds are characterized by their structures, and these two compounds differ substantially in structure (see appendix). However, the two compounds would seem to be substantial equivalents under the FWR test. They each provide analgesia and anti-inflammatory activity ("function") by inhibiting prostaglandin synthesis ("way") in order to alleviate pain, reduce fevers, and lessen inflammation ("result").

Id. at 17. The aspirin/ibuprofen example was intended to show a situation where the triple identity test would lead a court to the wrong conclusion because "a compound may appear to be equivalent under the FWR test, but not under the substantiality of the differences test." *Id.*

The Federal Circuit stated that both the function-way-result test and the insubstantial differences tests have been "blessed" by the Supreme Court, "leaving to the lower courts in future cases the choice of which to apply." *Id.* at 13. However, the Federal Circuit gave a clear indication that the substantial difference test would likely prove superior in determining whether manganese dioxide and silver oxide are equivalents within the context of the process patents at issue:

> Manganese dioxide and silver oxide are substantially different in many respects. For example, manganese and silver are in different groups of the Periodic Table. In oxide form, manganese has an oxidation state of +4, while silver is +1. Those differences may well be relevant to equivalence at trial.

Id. at 18. Thus, while the Federal Circuit stated that the triple identity test still can be used, it admonished the district court that it should not use the triple identity test alone and that the insubstantial differences test is likely more appropriate in the chemical arts.

Despite its critical treatment of the application of the triple identity test by the court below, the Federal Circuit let the preliminary injunction against Aurobindo stand on other grounds. Q

quinn emanuel
865 South Figueroa Street, 10th Floor, Los Angeles, California 90017

PRESORTED
STANDARD
U.S. POSTAGE
PAID
PERMIT NO. 4338
INDUSTRY, CA

business litigation report
quinn emanuel urquhart & sullivan, llp

Published by Quinn Emanuel Urquhart & Sullivan, LLP as a service to clients and friends of the firm. It is written by the firm's attorneys. The Noted with Interest section is a digest of articles and other published material. If you would like a copy of anything summarized here, please contact Elizabeth Urquhart at +44 20 7653 2311.

- We are a business litigation firm of more than 720 lawyers — the largest in the world devoted solely to business litigation and arbitration.
- As of August 2017, we have tried over 2,600 cases, winning 88% of them.
- When we represent defendants, our trial experience gets us better settlements or defense verdicts.
- When representing plaintiffs, our lawyers have garnered over $60 billion in judgments and settlements.
- We have won five 9-figure jury verdicts.
- We have also obtained thirty-four 9-figure settlements and fifteen 10-figure settlements.

Prior results do not guarantee a similar outcome.

LOS ANGELES
865 S. Figueroa St.,
10th Floor
Los Angeles, CA 90017
+1 213-443-3000

NEW YORK
51 Madison Ave.,
22nd Floor
New York, NY 10010
+1 212-849-7000

SAN FRANCISCO
50 California St.,
22nd Floor
San Francisco, CA 94111
+1 415-875-6600

SILICON VALLEY
555 Twin Dolphin Dr.,
5th Floor
Redwood Shores, CA 94065
+1 650-801-5000

CHICAGO
191 North Wacker Dr.,
Suite 2700
Chicago, IL 60606
+1 312-705-7400

WASHINGTON, D.C.
777 6th Street NW,
11th Floor
Washington, DC 20001
+1 202-538-8000

HOUSTON
Pennzoil Place
711 Louisiana St.,
Suite 500
Houston, TX 77002
+1 713-221-7000

SEATTLE
600 University Street,
Suite 2800
Seattle, WA 98101
+1 206-905-7000

TOKYO
NBF Hibiya Bldg., 25F
1-1-7, Uchisaiwai-cho,
Chiyoda-ku
Tokyo 100-0011
Japan
+81 3 5510 1711

LONDON
90 High Holborn
London WC1V 6LJ
United Kingdom
+44 20 7653 2000

MANNHEIM
Mollstraße 42
68165 Mannheim
Germany
+49 621 43298 6000

HAMBURG
An der Alster 3
20099 Hamburg
Germany
+49 40 89728 7000

MUNICH
Hermann-Sack-Straße 3
80331 Munich
Germany
+49 89 20608 3000

PARIS
6 rue Lamennais
75008 Paris
France
+33 1 73 44 60 00

MOSCOW
St. Petersburg Tower,
"Capital City" Complex
"Moscow City" Business Center
8, Presnenskaya Nab., Bld 1, Floor 19,
Office 193
Moscow, 123317
Russia
+7 499 277 1000

HONG KONG
1307-1308 Two Exchange Square
8 Connaught Place
Central Hong Kong
+852 3464 5600

SYDNEY
Level 15
111 Elizabeth Street
Sydney, NSW 2000
Australia
+61 2 9146 3500

BRUSSELS
Rue Breydel 34
1040 Brussels
Belgium
+32 2 416 50 00

ZURICH
Dufourstrasse 29
8008 Zürich
Switzerland
+41 44 253 80 00

SHANGHAI
Level 20, The Center
989 Changle Rd
Shanghai 200031
+86 21 5117 5859

PERTH
Level 24, Suite 24.28
Allendale Square
77 St Georges Terrace
Perth WA 6000 Australia