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Pleading Common Law Fraud Under Rule 9(b): Conflicting Circuit Court Interpretations

Federal Rule of Civil Procedure 9(b) prescribes the standards for pleading a common law fraud claim. The Rule states that "[i]n alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake." But "[m]alice, intent, knowledge, and other conditions of a person's mind may be alleged generally." Hence, these two sentences spell out two distinct rules: (i) there is a special requirement for pleading fraud or mistake for at least certain elements; but (ii) scienter needs to only be pled through "general[]" allegations.

Despite its plain language, judicial interpretation of Rule 9(b) has resulted in widely differing camps on what is actually required to plead scienter in common law fraud claims. The complexity increased when the Private Securities Litigation Reform Act ("PSLRA") added the "strong inference" requirement for pleading scienter, but intended to do so only for claims under federal securities fraud statutes. Finding the "correct" interpretation of Rule 9(b)'s scienter requirement was further complicated when the Supreme Court put teeth into the basic pleading requirements of Rule 8 in *Iqbal* and *Twombly*, calling into question what it means to plead "generally" to begin with.

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INSIDE

Quinn Emanuel Opens Zurich Office

The firm has opened an office in Zurich, led by partner Dr. Thomas Werlen, formerly a partner at Allen & Overy and General Counsel of Novartis. Quinn Emanuel has been representing Swiss-based clients in high-stakes international disputes and investigations since Dr. Werlen joined the firm in 2012. Notable representations include the Fédération Internationale de Football Association (FIFA) in criminal investigations in the U.S. and Switzerland, a number of major Swiss banking and financial institutions in DOJ and IRS investigations, as well as international companies in a series of complex financial and regulatory disputes in the U.S., the Middle East, and Asia.

The focus of the Zurich office will be on high-stakes disputes with a substantial international dimension. In addition to its white collar and corporate investigations expertise, the practice of the Zurich team focuses on transnational litigation, international arbitration, and complex disputes in finance, pharma and life sciences, commodities, and international sports. Clients of the Zurich office will benefit from the firm's international network when faced with regulatory or litigation exposure in the United States, the European Union, and Asia. This is the firm's eighth European office. The others are located in Brussels, Hamburg, London, Mannheim, Moscow, Munich, and Paris. Q

Quinn Emanuel London Partner, Stephen Jagusch, Appointed Queen's Counsel

Quinn Emanuel London partner Stephen Jagusch has been appointed Queen's Counsel in the 2015-2016 Queen's Counsel selection. This appointment is bestowed on lawyers who demonstrate an "excellence in advocacy in the higher courts." It is awarded only to "truly excellent advocates" who "have demonstrated the [necessary] competencies to a standard of excellence." Mr. Jagusch is worldwide chair of the firm's international arbitration practice. He is regularly recognized by legal publications, such as *Chambers*, the *Global Arbitration Review*, and many others as one of the top advocates in the field of international arbitration. Stephen joins Sue Prevezer as a fellow QC in the London office. Q

Pleading Scienter Under Rule 9(b): Time for Supreme Court Intervention

The language of the second sentence of Rule 9(b) is simple: "Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally." F.R.C.P. 9(b). But the interpretation of that clause has resulted in a complex array of legal rules, such that the same pleading is now being treated very differently based on the Circuit in which the plaintiff happens to file. There are two reasons why the time may be ripe for Supreme Court intervention. First, there is a clear Circuit split, with the Second Circuit applying a standard ("strong inference") that is distinct from that used by the other Circuits. Second, the other Circuits have not uniformly harmonized Rule 9(b)'s "generally" language with the newfound "plausibility" requirement of Rule 8.

1. The Second Circuit's "Strong Inference" Standard

The Second Circuit has held that Rule 9(b) requires fraud complaints to allege facts that lead to a "strong inference" that the defendant has the requisite state of mind. *See, e.g.*, *IKB Int'l S.A. v. Bank of Am. Corp.*, 584 F. App'x 26, 27 (2d Cir. 2014) ("We have repeatedly required plaintiffs to plead the factual basis which gives rise to a strong inference of fraudulent intent."). When it does comment on the matter, which is rare, the Second Circuit has justified the imposition of this requirement by observing that it is a reasonable way to prevent baseless fraud claims (sometimes called strike suits) that can damage a defendant's public reputation. *See Ross v. A.H. Robins Co.*, 607 F.2d 545, 558 (2d Cir. 1979) (establishing the strong inference test because "[i]t is reasonable to require that the plaintiffs specifically plead" scienter); *see also O'Brien v. Nat'l Property Analysts Partners*, 936 F.2d 674, 676 (2d Cir. 1991).

While protection from strike suits may be a noble cause, no other Circuit has adopted the Second Circuit's "strong inference" requirement. These other Circuits reason that other provisions of Rule 9(b) already adequately protect defendants, without holding plaintiffs' feet to the fire with respect to pleading scienter as well. Most notably, the *first* half of Rule 9(b) can be seen as doing the necessary work—under it, plaintiffs must provide defendants the tools to defend themselves by requiring they delineate the who, what, and when of the misrepresentation claim. And Rule 8 post-*Iqbal/Twombly* may now also be seen as a relatively powerful tool against "strike suits."

More basically, the Second Circuit has not been followed because other courts do not view it as within their power to substitute one phrase ("generally") with another, facially inconsistent one ("strong inference"). The Ninth Circuit has directly criticized the Second Circuit for this very reason. *See In re GlenFed, Inc. Securities Litig.*, 42 F.3d 1541, 1546-47 (9th Cir. 1994) (superseded on other grounds) ("Whether the [strong inference] test has such an effect [of deterring 'strike suits'] is beside the point. We are not permitted to add new requirements to Rule 9(b) simply because we like the effects of doing so.").

It merits emphasis that the challenges of keeping the Rules straight increased when Congress passed the PSLRA. Enacted in 1995, the PSLRA expressly heightened the scienter requirement for federal securities fraud claims, requiring that "complaint[s] . . . state with particularity the facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2) (2006). In *Tellabs, Inc. v. Makor Issues & Rights.*, 551 U.S. 308 (2007), the Supreme Court interpreted the PSLRA's "strong inference" language as requiring a broad balancing test: "A complaint will survive, we hold, only if a reasonable person would deem the inference of scienter cogent and at least as compelling as any opposing inference one could draw from the facts alleged." *Id.* at 324. In other words, there is now a nationwide interpretation of "strong inference" for claims brought under PSLRA.

But although *Tellabs* may have brought consistency to the standards for pleading claims under the federal securities fraud statutes, it has only increased the confusion for pleading other types of fraud. Congress plainly did *not* intend to re-write the pleading rules for *any other* type of claim—even, common law claims brought in the same complaint on the same securities. *See Frank v. Dana Corp.*, 547 F.3d 564, 570 (6th Cir. 2008) ("the PSLRA imposes additional and more '[e]xacting pleading requirements' for pleading scienter in a securities fraud case"). And it is clear that Congress did *not* intend to codify the Second Circuit's case law that determined what strong inference means. *See, e.g.*, H.R. Conf. Rep. 104-369, at 740 (1995).

This has caused problems in many ways. Within the Second Circuit, courts are now expected to apply one "strong inference" test to the common law portions of a complaint, and another purportedly higher "strong inference" test to the federal statutory portions of the same complaint. It is questionable whether courts can faithfully and consistently apply two different "strong inference" standards at all, let alone whether they could do so while still hewing to the plain meaning of the "may be alleged generally" text of Rule 9(b). *See JBCHoldings NY, LLC v. Pakter*, 931 F. Supp. 2d 514, 533 n. 15 (S.D.N.Y. 2013) ("It is worth nothing that

Tellabs interpreted the 'strong inference' requirement of the Private Securities Litigation Reform Act, and not the general pleading requirements under Rule 9(b) . . . However, numerous district courts in this Circuit have applied the *Tellabs* framework to common law fraud laws.").

But even worse, because of the sheer number of securities-fraud cases handled in New York, the amount of confusing precedent can create trouble for litigants and courts even outside the Second Circuit. Courts elsewhere may not fully understand that many Second Circuit dismissals are the product of a pleading standard that is inapplicable to the claims brought before them, and may miss the fact the PSRLA is simply irrelevant to common law claims despite the fact the Second Circuit has used confusingly identical language long before its passage. *See, e.g.*, *The Prudential Ins. Co. of Am. v. Bank of America, N.A.*, 14 F. Supp. 3d 591, 599 (D.N.J. Apr. 17, 2014) (applying "strong inference" pleading standard to common law fraud claims based on reading of Third Circuit case involving a federal statutory claim, which in turn cited to Second Circuit cases applying the different "strong inference" standard that pre-dated the PSLRA).

2. Different Approaches Even to Pleading "Generally"

Apart from the split between the Second Circuit and every other Circuit, there is a second reason why Supreme Court intervention on Rule 9(b) may be necessary: courts are confused on what it means to plead scienter "generally" in light of the recently invigorated Rule 8.

In *Bell Atl. Corp. v. Twombly*, 550 U.S. 544 (2007), the Supreme Court held that "a plaintiff's obligation to provide the 'grounds' of his 'entitlement to relief' requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do[.]" *Id.* at 555. The Court did not mean to "impose a probability requirement at the pleading stage," instead, it was "[a]sking for plausible grounds to infer an agreement[.]" *Id.* at 556. Two years later, the Supreme Court again spoke on the general pleading standard in *Ashcroft v. Iqbal*, 556 U.S. 662 (2009). The Court held that the plausibility standard in *Twombly* did not require "detailed factual allegations, but it demanded more than an unadorned, the-defendant-unlawfully-harmed-me accusation . . . 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." *Id.* at 677-78.

If Rule 8's "plausibility" requirement trumps the second part of Rule 9(b), then to plead "generally" just means that scienter must be plead "plausibly" like everything else under *Iqbal/Twombly*. In this reading, the second sentence of Rule 9(b) (state of mind "may be alleged generally") is merely meant to ensure that the burden of pleading state of mind is *no higher* than that normally expected of plaintiffs, a clarifying sentence made necessary because of the targeted provisions of the first sentence of Rule 9(b) ("circumstances" must be pled with "particularity").

The First, Third, Fifth, Sixth, Seventh, Eighth, and Federal Circuits have seemingly taken something akin to a 'generally means plausible' approach, which—intentionally or not—can be seen as harmonizing the two Rules post-*Iqbal/Twombly* while still stopping far short of the Second Circuit's "strong inference" conclusion. *See, e.g.*, *Schatz v. Republican State Leadership Comm.*, 669 F.3d 50, 58 (1st Cir. 2012) ("But, to make out a plausible [ ] claim . . . a plaintiff must still lay out enough facts from which [scienter] might reasonably be inferred."); *Faistl v. Energy Plus Holdings, LLC*, 2012 WL 3835815, at *4 (D.N.J. Sept. 4, 2012) ("Plaintiff has failed to plead *any* facts that would allow this Court to draw the reasonable inference that any of the Defendants *knew* any representations they made, respectively, were in fact false."); *Flaherty & Crumrine Preferred Income Fund, Inc. v. TXU Corp.*, 565 F.3d 200, 213 (5th Cir. 2009) (requiring facts that "support an inference" of scienter); *Heinrich v. Waiting Angels Adoption Servs., Inc.*, 668 F.3d 393, 406 (6th Cir. 2012) ("The courts have uniformly held inadequate a complaint's general averment of [scienter] . . . unless a complaint *also* sets forth specific facts that make it reasonable[.]"); *Tricontinental Indus., Ltd. v. PricewaterhouseCoopers, LLP*, 475 F.3d 824, 833 (7th Cir. 2007) ("[S]tates of mind [ ] may be pleaded generally under Rule 9(b); nevertheless, the complaint must afford a basis for believe that plaintiffs could prove scienter."); *In re K-tel Int'l, Inc. Sec. Litig.*, 300 F.3d 881, 894 (8th Cir. 2002); *Exergen Corp. v. Wal-Mart Stores, Inc.*, 575 F.3d 1312, 1327 (Fed. Cir. 2009).

On the other hand, some would argue that even this does violence to the plain text and history of Rule 9(b). In this view, Rule 9(b)'s second sentence is more than just a carve-out to the first-sentence of Rule 9(b), but an explicit denial of the requirement to do *anything* more than simply say that the act was done knowingly. The legislative history supports this view. The Advisory Committee Notes to Rule 9(b) indicate that the rule was drawn from Rule 22 of the English Practice Rules of 1937. The English Rule provides that knowledge may be alleged *without* asserting the facts from which that knowledge is inferred: "Wherever it is material to allege malice, fraudulent intention, knowledge, or other condition of the mind of any person, it shall be sufficient to allege the same as a fact without setting out the circumstances from which the same is to be inferred." *See* The Annual Practice, Order 19, Rule 22 (1937).

There is also Circuit-level precedent (though most of it pre-*Iqbal/Twombly*) supporting the view that "generally" means scienter can be alleged simply by saying it existed. The Ninth and Tenth Circuits historically took this position, holding that plaintiffs "may aver scienter generally, just as the rule states—that is, simply by saying that scienter existed." *In re GlenFed*, 42 F.3d at 1546-47; *Schwartz v. Celestial Seasonings, Inc.*, 124 F.3d 1246, 1252 (10th Cir. 1997) (same); *but see United States v. Corinthian Colleges*, 655 F.3d 984, 997 (9th Cir. 2011) (asking whether there were facts to "support an inference or render plausible" the claim). There is some support for the view that the District of Columbia, Fourth, and Eleventh Circuits also interpreted Rule 9(b) this way—at least prior to *Iqbal/Twombly*. *See, e.g.*, *U.S. ex rel. Totten v. Bombardier Corp.*, 286 F.3d 542, 552 (D.C. Cir. 2002); *Harrison v. Westinghouse Savannah River Co.*, 176 F.3d 776, 784 (4th Cir. 1999) ("The second sentence of Rule 9(b) allows conclusory allegations."); *Urquilla-Diaz v. Kaplan Univ.*, 780 F.3d 1039, 1051 (11th Cir. 2015).

Expressly clarifying how Rule 9(b) and Rule 8 interact following *Iqbal/Twombly* is something every Circuit Court should do, though Supreme Court ruling interpreting Rule 9(b) for all courts would obviously be preferable.

Conclusion

In sum, the federal courts are currently split over the proper interpretation of Rule 9(b), and the situation cries out for Supreme Court intervention. The bench and bar need clarification as to whether the Rule allowing allegations of scienter to be pled "generally" is or is not compatible with either the "strong inference" standard that has long been used in the Second Circuit, or the "strong inference" standard created by the PSRLA and interpreted by the Court in *Tellabs*. They also need clarification as to how Rule 9(b)'s "generally" allowance should be harmonized with Rule 8's "plausibility" requirement. Does pleading "generally" under Rule 9(b) simply mean that scienter need only be pled to the same "plausible" level as other elements of other claims? Or does it suffice to simply say scienter existed, as was the case under the English rule upon which Rule 9 was based, and as was long the case in many Circuits?

Given Rule 9(b) comes into play in virtually every fraud-based civil filing made in federal court, it is of the utmost importance for there to be a nationwide standard of application, so that a plaintiff is not dismissed for insufficient pleading merely because its case is venued in one Circuit rather than another. Until the Supreme Court brings consistency to this area of the law, all counsel should be mindful of the potentially important differences between the Circuits. Q

NOTED WITH INTEREST

Alaska Electrical Pension Fund v. Bank of America: A Key Decision for Plaintiffs in the ISDAFix Antitrust Litigation

A significant decision was recently issued in the ISDAfix antitrust class action, titled *Alaska Electrical Pension Fund v. Bank of America, N.A.*, 2016 WL 1241533 (S.D.N.Y. Mar. 28, 2016), in which Quinn Emanuel is co-lead counsel for the class. ISDAfix is an interest rate benchmark used to determine the settlement value of cash-settled swaptions (options on interest rate swaps) and other financial derivatives. Plaintiffs' basic allegation was that the fourteen major Wall Street banks who set the ISDAfix rate each day conspired to rig ISDAfix in order to extract higher profits on financial instruments that are linked to ISDAfix.

On March 28, 2016, Judge Jesse Furman issued an in-depth, 36-page opinion largely upholding the complaint. Judge Furman sustained the antitrust, breach of contract, and unjust enrichment claims, while dismissing the tortious interference and breach of implied duty of good faith and fair dealing claims. The court's decision has important implications for financial benchmark litigation in particular, and antitrust litigation in general.

The case is one of a number of large financial-misconduct cases being put together through quantitative analysis of public and quasi-public data. The use of "screens" to detect subtle but consistent pricing and other anomalies was also used, for example, in LIBOR. In *Alaska Electrical*, the "screens" revealed that: (1) the banks repeatedly claimed to have had identical offer/bid rates; (2) the level of uniformity of the banks' submissions was undermined by concurrent market rates; (3) the level of uniformity in the banks' submissions abated once regulatory scrutiny increased; and (4) the change in the banks' behavior cannot be explained by an increase in volatility, or other market forces. The analyses also show that (5) the banks "banged the close" in the market for ISDAfix-related instruments to manipulate the reference rate; (6) the banks conspired with the ISDAfix rate administrator, ICAP, to delay the publication of transactional information; and (7) these behaviors also began to dissipate when the banks came under increased scrutiny from regulators in late 2013.

The *Alaska Electrical* court's upholding of the complaint is another judicial stamp of approval on this approach to "plausibly" pleading a claim based primarily on analyses of pricing data. This approach allows plaintiffs to take the initiative to immediately pursue their claims, rather than wait for news stories or government investigations to fully develop. The court rejected many common defense arguments, such as that their non-nefarious alternative explanations for the data should hold sway at the pleading stage, and that the court had to blind itself to the banks' wrongdoing in other areas. 2016 WL 1241533, at *4-5. To the contrary, Judge Furman recognized that the fact the banks had held together a conspiracy in other financial areas, provided additional support for the allegation they conspired here as well. This is because it took the air out of the defense argument that the alleged conspiracy was simply too complex, across a too-diverse set of banks, to make economic sense.

The case is also important because it highlighted a split amongst the district courts with regard to the issue of "antitrust standing." The court rejected the banks' argument that plaintiffs cannot establish antitrust injury because the setting of ISDAfix was "based on a cooperative process." *Id*. at *6. The banks relied on *In re LIBOR-Based Financial Instruments Antitrust Litigation*, 935 F. Supp. 2d 666 (S.D.N.Y. 2013) ("*LIBOR I*"), where Judge Naomi Buchwald held that "the process of setting LIBOR . . . was a cooperative endeavor wherein otherwise-competing banks agreed to submit estimates of their borrowing costs . . . to facilitate calculation of an interest rate index." *Id*. at 688. Judge Buchwald concluded that if the banks "subverted this process by conspiring to submit artificial estimates . . . it would not follow that plaintiffs have suffered antitrust injury. Plaintiffs' injury would have resulted from defendants' misrepresentation, not from harm to competition." *Id.*

Judge Furman disagreed for two reasons. First, he found that a benchmarking conspiracy that was carried out not only through the reference-rate process, but also through "banging the close" market activities, distinguished the ISDAfix case from the LIBOR cases. 2016 WL 1241533, at *6. More "broadly," Judge Furman "disagree[d] with the *LIBOR I* Court's legal conclusion" that engaging in a purportedly "cooperative" process to manipulate prices insulates the participants from antitrust liability. *Id.* at *6-7. He began his analysis with Supreme Court precedent, which says that the specific "machinery employed by a combination for price-fixing is immaterial" to the antitrust laws. He also disagreed with Judge Buchwald's conclusion that the LIBOR claims are essentially fraud allegations, writing that "[i]t would be perverse to grant such wrongdoers immunity from liability under the antitrust laws."

Notably, Judge Lorna Schofield of the S.D.N.Y., who is overseeing litigation involving alleged manipulation of foreign currency exchange, similarly concluded that collusion in the setting of a benchmark rate results in antitrust injury and disagreed with Judge Buchwald. Judge Furman's decision is timely because *LIBOR I* is now before the Second Circuit, which heard oral arguments last November. The decisions by Judges Furman and Schofield may increase the chances that the Second Circuit will see Judge Buchwald's decision as an outlier and reverse.

Another common area of dispute in these large financial cases, which the *Alaska Electrical* court had chance to weigh in on, is whether the parties bringing the claims are the "right" plaintiffs. Defendants have argued that particular plaintiffs cannot show "standing" without pleading "injury-in-fact" with great specificity—*i.e.*, tying their investment to a specific day, time of day, and type of demonstrated misconduct. The *Alaska Electrical* court held that the basic "standing" requirement is a "low threshold" for plaintiffs. 2016 WL 1241533, at *4. The court found that the ISDAfix plaintiffs easily met the standard by alleging that they "transacted in interest rate derivatives . . . directly impacted" by the manipulation of ISDAfix, recognizing that a "paid too much" or "received too little" harm is a "classic" economic injury-in-fact. The court thus rejected the argument that the plaintiffs had to detail their investments, and the wrongdoing, down to the exact minute.

The banks also regularly argue that their misconduct may have benefitted the plaintiffs. A movement in one

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way that harmed those who bought, simultaneously helped those who sold. The court held that these "netting" issues are simply not a pleading question. *Id*. The plaintiffs' only burden is to plausibly plead some harm, which the *Alaska Electrical* plaintiffs did. As the court observed, the fact "that an injury may be outweighed by other benefits, while often sufficient to defeat a claim for damages, does not negate standing."

Finally, on the statute of limitations, Judge Furman found allegations that the conspiracy to manipulate ISDAfix was secretive by nature, and thus fraudulently concealed, well-pled. *Id*. at *12-13. The court rejected the banks' argument that plaintiffs should have known of their allegations earlier because the underlying economic data was publicly available. The court noted that "the trends identified in the Amended Complaint are subtle and required the aggregation of massive quantities of data." This aspect of the decision is thus another significant victory for the data-driven approach to pleading benchmarking conspiracies, as pleading a case based on publicly available data is always potentially a dual-edged sword with respect to the statute of limitations.

PRACTICE AREA NOTES

Patent Litigation Update

District Court Rules Non-Public Sales or Offers for Sale No Longer Apply to the "On-Sale" Bar Under the AIA. The on-sale statutory bar is a limitation on patentability that prohibits an inventor from obtaining a patent, when his invention has been sold or offered for sale for over one year prior to filing for a patent. Although Congress has never defined what constitutes a "sale" for purposes of the "on-sale" bar, courts have historically held that secret sales and offers for sale, could be prior art and preclude patentability under the on-sale bar. *See, e.g.*, *Metallizing Eng'g v. Kenyon Bearing*, 153 F.2d 516 (2d Cir. 1946) (Hand, J.).

In 2011, the America Invents Act ("AIA") changed the statutory language surrounding the on-sale bar by adding the catchall phrase "or otherwise available to the public" at the end of the enumerated list of prior art categories under 35 USC § 102(a)(1). Shown below are the AIA amendments made to the original statutory language:

> *Novelty; Prior Art—A person shall be entitled to a patent unless—(1) the claimed invention was patented, ~~or~~ described in a printed publication, ~~in this or a foreign country~~ or in public use, ~~or~~ on sale, ~~in this country,~~* ***or otherwise available to the public*** *~~more than one year prior to the date of application for patent in the United States~~ before the effective filing date of the claimed invention;*

These changes suggest that the on-sale bar now requires sales and offers for sale to be made "available to the public" in order for them to be eligible as prior art, which would mean that defendants may no longer use non-public, secret sales activity for an on-sale bar defense.

The District Court of New Jersey recently analyzed the effect of this amendment in *Helsinn Healthcare v. Dr. Reddy's Labs.*, No. 11-3962, 2016 U.S. Dist. LEXIS 27477 (D.N.J. Mar. 3, 2016). In *Helsinn*, four patents from the same family were in dispute. Each patent claimed priority to the original provisional application date, January 30, 2003, although each had different effective filing dates. Defendants raised the on-sale bar defense for all four patents, asserting as prior art various agreements that Helsinn had entered into with third parties before the critical date, which was January 30, 2002. Because of their different effective filing dates, three patents were subject to the pre-AIA on-sale bar, and one was subject to the new post-AIA on-sale bar (the post-AIA on-sale bar applies to patents with effective filing dates on or after March 16, 2013).

Although the Court concluded that Helsinn's agreements could not be invalidating prior art because the evidence did not establish that the claimed invention was "ready for patenting" as of the critical date, the Court engaged in a lengthy statutory interpretation analysis on the meaning of the phrase "otherwise available to the public" and whether it requires sales activity to be publicly available in order to potentially qualify as prior art under the AIA. The Court concluded that only evidence of a *public* sale could qualify as potential prior art under the AIA, arriving at that conclusion based on: (i) statutory construction principles; (ii) published guidelines from the USPTO; (iii) legislative history of the AIA; and (iv) public policy goals underlying the AIA.

First, the Court cited the "associated-words" canon of statutory construction, which states that "when several words are followed by a clause which is applicable as much to the first and other words as to the last, the natural construction of the language demands that the clause be read as applicable to all." *See Paroline v. United States*, 134 S.Ct. 1710, 1721 (2014). Second, the USPTO guidelines, which the Court noted are instructive but not binding, state that the Office views the AIA as "indicating that secret sale or use activity does not qualify as prior art," and the relevant inquiry is focused on "whether the sale . . . made the invention available to the public." 78 Fed. Reg. 11,062–63 (Feb. 14, 2013). Third, the legislative intent, including the "undisputed" AIA Committee Report, as the Court put it, includes statements in Senate hearings such as: "The word 'otherwise' makes clear that the preceding clauses describe things that are of the same quality or nature as the final clause . . . all of them are limited to that which makes the invention 'available to the public.'" (Mar. 8, 2011 Congressional Record); and "contrary to current precedent, in order to trigger the bar in new 102(a) … an action must make the patented subject matter 'available to the public.'" (Sept. 8, 2011 Congressional Record). Fourth, with respect to public policy goals underlying the AIA, the Court found that the new requirement comports with Congress's goal to modernize and streamline the patent system.

Applying these principles to the facts, the Court found that Helsinn's agreements could not be invalidating on-sale art under the AIA because they were essentially non-public agreements that were entirely subject to and performed under confidentiality restrictions. One noteworthy example was the MGI Agreement, which contracted for the supply and purchase of Helsinn's commercial product. The Court found that the MGI Agreement did not make the claimed invention available to the public and therefore was not a public sale under the AIA. However, the Court ruled it was a "sale" under the pre-AIA on-sale bar because it was a contract for a "future commercial product," and therefore could be considered a potentially invalidating sale for the three patents that were governed by the pre-AIA law. Thus, in theory, Defendants could have invalidated three patents in a family, but not a fourth patent, based on the same sales activity, depending on nothing other than when the patent was filed.

One Defendant, Teva Pharmaceuticals, has appealed the ruling and, as of yet, no court decisions have commented on or cited to *Helsinn*. However, the ruling is significant in several ways. First, it departs from decades of precedent holding that secret, non-public sales apply to the on-sale bar and eliminates a whole category of disclosures available as potential prior art. Second, it allows sales activity to be potential prior art to some patents in a family, and to not others, even though they share the same critical date. Third, it raises the issue of whether inventors may commercially exploit their inventions substantially beyond the patent term by first conducting secret sales and then filing a patent application. Fourth, it will eliminate the substantial discovery efforts often needed to obtain evidence of a secret sale, which can be an expensive endeavor, particularly where those sales may be in foreign countries. Finally, it eliminates a whole category of evidence that is heavily or wholly reliant on potentially interested third-party witness testimony. By requiring the sale or offer for sale to be publicly available, evidence to support an on-sale defense will necessarily be, by definition, publicly available.

International Arbitration Update

García's *Green Light to Dual Nationals in Investor-State Arbitration.* The decision in *Serafín García Armas v. República Bolivariana de Venezuela*, PCA Case No. 2013-3, Decision on Jurisdiction (Dec. 14, 2014) touches on a very interesting question that will surely see greater discussion and debate within the investment dispute settlement community in the years to come. That question is whether an investor who is a national of State A but who also is a dual national of State B and who makes an investment in State A may invoke the protections of the bilateral investment treaty ("BIT") between State A and State B as an investor of State B. In other words, can the investor invoke his State B nationality to sue State A under the BIT between both countries, even though he also is a national of State A? *García* answered this question affirmatively, marking a significant opening for claims by dual nationals against countries of which they are nationals.

Key Background and Jurisdictional Issue. In *García*, Serafín García Armas and Karina García Gruber both sued Venezuela for expropriation in violation of the Spain-Venezuela BIT. García Armas was a Spanish national by birth and later acquired a second nationality from Venezuela; García Gruber was a Venezuelan national by birth and later acquired Spanish nationality. They both sued Venezuela under the Spain-Venezuela BIT opting for an investment treaty arbitration under the UNCITRAL rules rather than under the ICSID Convention.

Venezuela objected to the jurisdiction of the arbitration tribunal on various grounds, including that the Garcías were nationals of Venezuela and, as such, did not have standing to sue Venezuela under the Spain-Venezuela BIT. They reasoned that only nationals of Spain could sue Venezuela under the BIT and that Venezuelan nationals—even those who also had Spanish nationality—were not parties who could sue it under the BIT.

Venezuela argued that there was a general prohibition against claims by dual nationals against their own states in investor-state arbitrations, and suggested that this was an implied principle or tenet of customary international law. Specifically, Venezuela argued that as a general rule of international law, it could not be sued by its own nationals under an investment treaty that it signed with another country to promote investment by foreign nationals of that country. It further argued that in the case of dual nationals, the tribunal should consider the dominant and effective nationality of the investors, which according to Venezuela was Venezuelan. This "dominant and effective nationality test" would have required a detailed, factual analysis by the tribunal to determine which nationality was the dominant one utilized by the investors at certain times.

Though the Spain-Venezuela BIT and the UNCITRAL rules do not expressly prohibit claims by dual nationals, Venezuela argued that when Venezuela offered its consent to arbitration under the BIT, it did so under, among others, the ICSID Convention, and thus implicitly incorporated the exclusion of dual nationals that is contained in Article 25(2)(a). Venezuela also argued that the BIT's definition of a national as a person who has the nationality of "*one*"—in the singular—"of the Contracting Parties" excluded persons who had the nationality of *two* (both) states.

Tribunal's Decision. The tribunal rejected Venezuela's arguments and found that it had jurisdiction over the Spain-Venezuela BIT claims filed by the Garcías against Venezuela. In so doing, the tribunal gave primacy to the specific provisions of the Spain-Venezuela BIT over implied principles and the general rules of customary international law, as the BIT was the *lex specialis*. In interpreting the language in the BIT, the tribunal considered various other legal sources, such as the Treaty of Friendship Between Venezuela and Spain, the Vienna Convention on the Law of Treaties, and customary international law. In the end, the key reasoning underlying its holding was based on the text of the BIT.

The Tribunal concluded that the BIT's definition of "national of one contracting state" included persons who had Spanish nationality even if those persons also had Venezuelan nationality. It found that the BIT did not contain express restrictions against dual nationals bringing claims against either contracting state. The tribunal held that the reference to "*one* of the Contracting Parties" is not a numerical limitation on nationality but part of a non-exclusive distinction between "one" and the "other," not between "one" and "two." The tribunal held that under the text of the Spain-Venezuela BIT, it did not matter whether the Garcías' Spanish nationality was "merely formal." Given the absence of any express limitations in the BIT prohibiting dual nationals from advancing claims against its own states, it was sufficient that the Garcías had Spanish nationality. To hold otherwise, according to the tribunal, would be to revise the text of the BIT by adding a restriction that could have been included (as it was in other BITs) but was not.

Importantly, the tribunal also rejected Venezuela's invitation to apply the dominant and effective nationality test to the question of whether the Garcías could sue Venezuela as Spanish nationals under the Spain-Venezuela BIT. Again, the tribunal examined the text of the BIT's language and found that no such requirement was included within the BIT. It thus rejected the application of this test as irrelevant to its analysis.

There are a few important features of this case that limit its potential applicability. First, that the Garcías sued under the UNCITRAL rules and not under the ICSID Convention is an important point of distinction with other investment treaty cases bought under the ICSID Convention. Unlike the ICSID Convention, whose Article 25 expressly excludes claims by dual nationals against countries whose nationality they shared on the date on which the parties consented to submit their dispute to arbitration as well as on the date on which the request for arbitration was registered, the UNCITRAL rules have no such prohibition. Thus, while the *García* holding is of important applicability in the context of non-ICSID investment treaty arbitrations, it is not applicable to investor-state disputes brought under the ICSID Convention. Of course, numerous BITs provide access to UNCITRAL arbitration, which further confirms the relevance and potential impact of the *Garcia* case.

A second point of distinction centers on the language of the Spain-Venezuela BIT. Unlike other investment treaties that Venezuela has entered into, the Spain-Venezuela BIT does not define "nationals" in a way that excludes claims against it by dual nationals. The absence of an express exclusion in the Spain-Venezuela BIT of claims against Venezuela by dual nationals along with the precise wording of the definitions within the BIT of "nationals" were key factors for the tribunal's analysis allowing for dual nationals to claim against Venezuela in *García*, as the tribunal distinguished the express prohibitions in other instruments. For example, the tribunal noted that the Italy-Venezuela BIT expressly excludes from the ambit of that BIT "nationals of both Parties," while the Spain-Venezuela BIT defines "nationals" as persons "who have the nationality of one of the Contracting

Parties . . . and make investments in the territory of the Other Contracting Party." The tribunal noted that this latter definition in the Spain-Venezuela BIT allowed for claims by dual nationals whereas Venezuela had expressly excluded such dual national claims within the Italy-Venezuela BIT. Thus, the *García* case will only be applicable in cases were the investment treaty has language that does not expressly exclude dual nationals from suing countries whose nationality they share.

Though a single case does not establish a trend, the tribunal's reasoning could have wide applicability, as many investment treaties lack express restrictions on claims by dual nationals, and further provide for UNCITRAL arbitration. For dual nationals considering claims against their host states, *García*'s holding marks an important step toward providing them with an avenue to redress their claims.

The Future of Claims by Dual Nationals. In the wake of *García*, there have been at least two cases brought by dual nationals against their own states. In one case, a Russian-French dual national is suing Russia. In a second case, a French-Mauritian dual national is suing Mauritius. Both cases are under the UNCITRAL rules.

Nonetheless, there remain clear limits to claims by dual nationals. First, as noted, *García* does not affect claims filed under the ICSID Convention, or claims filed under investment instruments that expressly prohibit claims by dual nationals against their own states. Second, some investment treaties define "nationals" or "investors" in a way that requires a deeper examination of the investor's nationality than was necessary in *García*. For example, treaties that require a tribunal to examine an investor's "dominant and effective" nationality will require that the investor have substantial connections to the country whose nationality he claims during the relevant time periods. Such treaties are designed to prevent "passport shopping."

And, finally, the question of *when* a nationality must be held for purposes of jurisdiction will most certainly be the subject of future discussion and debate. Indeed, this was the topic of a dissenting opinion in *García*. The dissenting arbitrator opined that the nationality requirement must be satisfied when the investment is made, whereas the majority held that the only key dates were when the alleged violations occurred and when the dispute was submitted to arbitration.

Conclusion. *García* appears to have paved the way for dual nationals to sue their own states in certain cases. *García* will likely influence not only arbitrations involving dual nationals, but also broader considerations of investors and states in respect of potential investment treaty claims

Some relevant considerations for investors:

- Acquiring a second nationality may prevent dismissal for lack of jurisdiction over a claim against the investor's own state. If the governing BIT allows it, a dual national may initiate arbitration under the UNCITRAL arbitration rules against a state whose nationality he or she possesses and thereby avoid the restriction against dual nationality in the ICSID Convention.
- Under certain circumstances, a dual national may be able to avoid jurisdictional problems by renouncing the nationality of the respondent state.
- Corporate claimants owned by dual nationals may face jurisdictional objections, especially in cases under the ICSID Convention.

Considerations for states:

- When negotiating investment treaties, states may wish to expressly exclude claims by dual nationals.
- States should not count on implied principles or general rules of customary international law as to the standing of dual nationals; any desired exclusion should be express.
- Short of banning claims by dual nationals, investment treaties can impose requirements that make such claims harder to pursue. These requirements include a "dominant and effective" test or similar requirement to prevent passport shopping. Q

Federal Circuit Affirms Inequitable Conduct and *Walker Process* Fraud Judgment

The firm obtained a unanimous Federal Circuit decision affirming a finding of inequitable conduct before the Patent and Trademark Office ("PTO") and a $26 million award consisting primarily of trebled attorneys' fees as antitrust damages based on *Walker Process* fraud on the PTO.

The firm represents TransWeb, LLC, a manufacturer of respirator filters. TransWeb developed a process for plasma fluorinating filtration media. In 1997, TransWeb distributed filter samples at an industry expo attended by 3M, the only other supplier in the world of similar media. More than one year later, 3M sought its own patents on this technology. Although 3M eventually disclosed the TransWeb samples to the PTO, it falsely asserting that the samples were received pursuant to a confidentiality agreement and thus did not constitute prior art. Several years later, 3M brought suit against TransWeb alleging infringement of the patents. After 3M's suit was voluntarily dismissed due to personal jurisdiction issues, TransWeb brought a declaratory judgment action in the District of New Jersey and 3M counterclaimed for infringement.

After a two-week trial, the jury unanimously found that 3M's patents were not infringed but were invalid as obvious. The jury also rendered an advisory verdict that the patents were unenforceable due to 3M's inequitable conduct by deceiving the PTO regarding the prior art nature of the TransWeb samples. The jury further found that 3M had committed a *Walker Process* antitrust violation by using fraudulently obtained patents in an attempt to monopolize the relevant filter markets and that TransWeb was entitled to its attorneys' fees as damages. The district court entered judgment in accordance with the jury verdicts and awarded TransWeb over $26 million in damages, which included lost profits and TransWeb's trebled attorneys' fees defending against the patent claims. 3M retained Seth Waxman, a former U.S. Solicitor General, to seek reversal.

The Federal Circuit affirmed. First, the Court affirmed that 3M had engaged in inequitable conduct by failing to disclose to the PTO that its pending patents were based on TransWeb's prior art samples. In so holding, the Court addressed the "corroboration" standard in patent cases. Oral testimony by an interested party is ordinarily insufficient to invalidate an issued patent; such testimony must be corroborated by other evidence. 3M argued that TransWeb was required to corroborate *all* material facts. The Court disagreed, noting that "3M's legal argument attempts to lead us to a legal conclusion that this court has repeatedly rejected." Instead, the Court reiterated a "rule of reason" approach ensuring that the oral testimony is credible as a whole, noting that "there are no hard and fast rules as to what constitutes sufficient corroboration, and each case must be decided on its own facts." Applying that flexible standard, the Court found that TransWeb provided sufficient corroborating evidence that its founder distributed prior art samples at the industry expo. Specifically, documentary evidence that TransWeb had produced, distributed, and offered for sale the filter samples as well as sought patent protections was sufficient corroborating evidence.

The Court next affirmed that 3M had engaged in inequitable conduct before the PTO and that its suit violated antitrust laws. In *Walker Process*, the Supreme Court held that a party could bring an action under the Sherman Act based on the enforcement of a fraudulently obtained patent. *See Walker Process Equip., Inc. v. Food Mach. & Chem. Corp.*, 382 U.S. 172, 174 (1965). The Federal Circuit held that 3M's suit was an attempted monopolization that sought to force TransWeb out of the filter markets. The Federal Circuit also confirmed that attorneys' fees incurred defending against infringement claims based on fraudulently obtained patents qualify as antitrust damages, which are subject to trebling. As the Court noted, "3M's unlawful act was in fact aimed at reducing competition and would have done so had the suit been successful." The Court therefore affirmed an award of approximately $26 million to TransWeb, consisting primarily of trebled attorneys' fees incurred defending against the patent claims. In so holding, the Court retained an important defense for parties confronted with bet-the-company litigation involving fraudulently obtained patents.

Victory in *Pro Bono* Asylum Application

The firm recently obtained asylum for a *pro bono* client from the U.S. Citizenship and Immigration Services ("USCIS"). Quinn Emanuel was able to expedite the process, notwithstanding a severe backlog in asylum applications, achieving a grant of asylum only 14 months after the client's application was filed. The client is relieved that he will not be forced to return to his homeland, where he risks prison and death. He is now on the path to permanent residency and citizenship.

The client is from Chad. He was arrested by the national police in May 2013, falsely accused of participating in an attempted coup against the President. In fact, he had merely made public comments about standing up for free speech. The country is not a democracy, and anyone seen as an enemy or troublemaker risks being arrested and killed. The client was also involved with a human rights organization, and he is an ethnic minority, which exacerbated the physical abuse he received after his arrest.

The client was imprisoned in secret for four months, where he was beaten, only given food and water once a day, and forced to sleep on a stone floor—no bed. He had only one shower in four months, without soap. At the end of his imprisonment he was kept in an underground hole too small to stand up in. A senior Army officer friend located him and got him out of prison, then hid the client in the countryside while the officer obtained a passport, visa, and plane ticket for him.

The client flew to J.F.K. in December 2013. He retained the firm 10 months later, after a referral from Human Rights First, and submitted his asylum application in December 2014. The application claimed eligibility for asylum based on his political opinions, his membership in a persecuted minority, and the Convention Against Torture (8 C.F.R. § 1208.13). The client attested to past persecution and a well-founded fear of future persecution if he were forced to return to Chad.

The USCIS had a 2-1/2-year backlog for scheduling interviews on asylum applications, which meant the client would likely not have had an interview until mid-2017. The firm wished to expedite the interview because he is separated from his family and his wife and son are in danger. His son was a newborn when the client was arrested, and is three years old now. His family is hiding in a remote village in Chad, having left their home in the capital, because they are afraid that the government might find them and kill them for their relationship to the client.

The Immigration and Naturalization Act ("INA") provides that an asylum interview "shall commence" within 45 days of filing an asylum application, and adjudication of an application "shall be completed" within 180 days of filing. 8 U.S.C. § 1158(d)(5)(A). Those time limits had expired. Although the facts therefore supported a *mandamus* action, which would compel the USCIS to schedule the client's interview, the USCIS has begun opposing such filings more strenuously in recent years. Moreover, several courts had recently denied relief under 8 U.S.C. § 1158(d)(5)(A), based on a statutory exception to the 45-day and 180-day deadlines for "exceptional circumstances."

Instead of filing for *mandamus*, Quinn Emanuel instead appealed directly to the director of the regional USCIS asylum office, asking for an expedited interview in light of the client's separation from family and their risk of harm. The USCIS scheduled his interview within weeks, and the interview was held in February 2016, 18 months sooner than it would have been given the backlog. The asylum application was exhaustively supported by detailed affidavits from the client, his wife, his father and uncles, the Army officer that rescued him, his former employers, Amnesty International's expert on Chad, and two groups of psychologists. The client was granted asylum two weeks later. He and his family were overjoyed.

The firm has since applied with the USCIS for permission for the client's wife and son to immigrate to live with him and is also assisting him with seeking employment in his professional field, working for humanitarian non-governmental organizations. Q

Litigation & International Arbitration Star Jennifer Selendy Joins Quinn Emanuel

Jennifer Selendy has joined Quinn Emanuel as a partner in the firm's New York office. Ms. Selendy, formerly a partner at Kirkland & Ellis, has a broad trial practice focusing on complex commercial disputes and international arbitration in diverse practice areas including antitrust, RICO, intellectual property, bankruptcy, securities, and toxic torts. She has represented blue-chip clients in both plaintiff and defense cases across a range of industries. She received her J.D., *cum laude*, from Harvard Law School and is a Marshall Scholar. Ms. Selendy is a member of multiple boards, including the Advisory Board of the Tufts Institute for Global leadership, where she was recognized with a Distinguished Alumni Award, and the National Center for Law & Economic Justice, where she is Chairman. Ms. Selendy is also a leader in the movement to reform gifted education and is co-founder of a school for accelerated learners. Q

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business litigation report

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