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Culture: Meeting Regulatory Expectations

Recent scandals in the corporate and financial spheres have served to highlight the importance of a strong and well-embedded institutional culture. It is difficult to pinpoint any such scandal that was not, to a material degree, attributable to cultural failings. It comes as little surprise therefore that the regulatory authorities have sharpened their focus on culture.

In the United States, the Financial Industry Regulatory Authority (FINRA) has identified culture as a key area of current supervisory focus; and resolved to formalize its assessment of firm culture. During these appraisals, FINRA will be reviewing how firms establish, communicate and implement cultural values, and whether cultural values are guiding business conduct. "As part of this review, we plan to meet with executive business, compliance, legal and risk management staff … to discuss cultural values. We would also like to discuss how your firm communicates and reinforces those values directly, indirectly and through its reward system. *We are particularly interested in how your firm measures compliance with its cultural values, what metrics, if any, are used and how you monitor for implementation and consistent application of those values throughout your organization.*" (emphasis added).

In a similar vein, corporate culture is a relevant consideration under the Department of Justice's guidelines for assessing corporate criminal liability. Wherein a strong culture will serve as a mitigant, a perceived poor culture will be regarded as an aggravating factor.

And such a concerted regulatory focus on culture is

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INSIDE

Leading Competition and Regulatory Lawyer Joins Quinn Emanuel Brussels Office

Trevor Soames has joined the firm as a partner based in its Brussels office. He is recognized by all the prominent legal directories and publications as one of the leading Brussels competition law practitioners. Mr. Soames' practice is global; it covers the full range of competition and antitrust matters, including mergers, monopolization (industry dominance), government investigations and litigation, state aid and cartel investigations in Europe and the USA, as well as contentious matters in the EU. A significant element of his practice relates to cases at the interface of intellectual property and antitrust. Q

Financial Services Regulatory and Investigations Authority Joins London Office

David Berman has joined the firm as a partner in London. David joins from UK firm Macfarlanes LLP, where he was head of its financial services group. Prior to becoming a lawyer, he was a managing director at an international investment bank, where he held senior level roles in legal, compliance and front office functions. Mr. Berman advises financial institutions (across both buy-side and sell-side) and other multinational organisations on regulatory and compliance issues. He counsels boards and senior management teams on regulatory issues of strategic significance. He specializes in providing strategic high-stakes advice; encompassing issue prevention, containment and resolution, including internal investigations. In addition, he has recently authored the leading publications *Senior Individual Accountability in the UK Financial Services Regulatory Environment–A Practical Guide* (Thomson Reuters 2014) and *Individual Accountability Under the Senior Managers Regime–A Practical Guide* (Thomson Reuters 2016). David is recognized as a "leading individual" by *Legal 500*; and regarded as "really on top of his game" by *Chambers & Partners*. Q by no means a US-specific phenomenon. In the UK, for example, it remains high on the agenda of the Financial Conduct Authority:

> "Culture remains a key driver of significant risks … and the root cause of high-profile and significant failings. Our focus on culture in financial services firms and its impact on conduct has been, and remains, a priority. We are interested in the direction of travel of firms' cultures *and if indicators show progress*. We will hold management to account … where cultural issues lead to internal controls that fail to promote and support the right outcomes for consumers and the market." (emphasis added) UK Financial Conduct Authority, 2016/17 Business Plan.

Significantly, cultural failings have featured increasingly of late in UK enforcement actions brought against both firms and individuals; and, in several instances, fundamentally underpinned the Regulator's case. Serious issues or misconduct have been readily attributed to a flawed culture - for which senior management is considered ultimately responsible. With the introduction of the UK Senior Managers Regime—and its inextricable link to culture—this trend can be expected to continue, resulting in a projected increase in related regulatory sanctions.

As indicated by highlighted extracts above, any credible culture program—in whatever industry or sector—will require a systematic approach to both: (i) the identification of a set of suitable cultural indicators/metrics, each accompanied by a measurable expectation; and, importantly, (ii) periodic assessment—to validate that the reality (the actual conduct of the firm and its employees) matches the expectation (set desired standards). A simple cultural values statement will not, without more, suffice.

Cultural Metrics

For many, culture is an inherently nebulous concept, difficult to define and measure. Although it will ultimately be for firms to choose their own particular metrics, FINRA has identified certain indicators by which it will assess culture:

- Whether control functions are valued within an organization (and adequately resourced);
- Whether policy and control breaches are tolerated;
- Whether the organization proactively seeks to identify risk and compliance events;
- Whether supervisors are effective role models of firm culture; and
- Whether sub-cultures that may not conform to overall corporate culture are identified and addressed.

Other cultural indicators might typically include:

- Responses to issues or incidents—was the response sufficiently credible and robust? Did it indicate a resolve on the firm's part to "do the right thing"?
- Complaints handling—how seriously is the firm treating complaints?
- Incentive structures—is an appropriate balance struck between the interests of clients and the firm?
- Performance management—are appropriate metrics being used to assess individuals' performance? Is there an over-focus on revenue generation and an under-focus on regulatory compliance?
- Demonstrable board and senior management engagement in regulatory compliance matters.
- Credibility of management response to adverse audit findings.
- Use of, and response to, employee surveys to help gauge culture.
- Approach to training—embraced, tailored and engaging; or off-the-shelf, unrealistic and a "necessary evil"?
- Credibility and robustness of approach to contravention of internal requirements - actions speak louder than words.
- Status of relationship with, and attitude towards, regulators—healthy and constructive; or hostile and awkward?
- Approach to product development and ongoing monitoring—is there an appropriate focus on customer/client interests?
- Quality and frequency of management information—are "red flags" highlighted, escalated and acted upon as appropriate?

To enable a measurable assessment, expectations must be set in respect of each chosen cultural indicator. For example (taking a firm's response to issues as the indicator):

> "Firm will respond credibly and robustly to material issues or incidents. In particular, any such issues or incidents will be expected to have been escalated appropriately [including to a member of the Executive Committee]; notified to the Regulator in a timely manner (where appropriate); duly prioritized, with the requisite sense of urgency; and managed at a suitable level of seniority within an appropriate governance framework [as approved by the Board]."

Measuring Culture

There is no single "right" or "wrong" way in which to measure culture. One obvious approach is through a periodic independent cultural appraisal conducted by, say, internal audit or external professionals. Such an assessment may be conducted by reference to an agreed set of cultural metrics and expectations—to benchmark actual conduct over the previous period against desired standards. Any material deviations would be analyzed to determine whether any lessons need to be learned and/or enhancements are required. Results would in turn be reported to senior management or the board. Outcomes would be incorporated, as appropriate, into compliance monitoring/audit plans and relevant risk assessments.

By way of illustration, one of Firm X's chosen cultural metrics is "response to issues or incidents." The related expectation is as per the italicized example above. Firm X has encountered two serious compliance issues over the past year. In this context, the cultural "audit" would (in simple terms) assess whether Firm X's actual response to these issues was consistent with expectation; and, if not, to highlight any scope for improvement.

Alternative or supplementary approaches to the assessment of culture include:

- Regular staff surveys—focused on issues such as: willingness/readiness to escalate suspicions or concerns; perception of the example being set by superiors and senior management; awareness of the firm's cultural values and expectations; and
- An independently-run program of tailored scenario-based workshops, involving a representative cross-section of employees at varying levels of seniority with different functions and tenures. Each scenario would incorporate one or more relevant "real life" dilemmas, designed to generate engagement and, importantly, to reveal cultural attitudes and mindset.

Clearly, these approaches are by no means mutually exclusive; and can be regarded as complementary to one another. Any firm wishing to undertake a comprehensive assessment may opt for all three of these initiatives at appropriate time intervals.

The Regulator's Perspective

For its part, the Regulator will typically assess a firm's culture by reference to certain key questions and criteria. For example (and to share but a few):

- Are the board and senior management adequately focused on understanding the culture that exists and seeing adherence to firm values and conduct as a strategic imperative?
- Is this evidenced in practices such as transparency for material transgressions, and owning the responsibility for identifying and dealing with problems?
- Do the firm's promotion and recruitment processes attribute material weight to compatibility with desired values and conduct; and consistent demonstration of the desired behaviors?
- Is there evidence of robust internal sanctioning, with material consequences for staff in the event of poor alignment with conduct and values?
- Does frontline management and staff demonstrate understanding of, and the ability to identify, values and conduct issues and act accordingly?

Such questions can serve as an invaluable and highly effective framework against which firms can self-appraise their overall cultural standing. In our experience, a concerted focus on these factors should be positively additive to any culture initiative.

Conclusion

Culture is, and will likely remain, high on the Regulator's agenda. The relative ease with which any serious issue or misconduct can be attributed to a "broken" culture (and consequently senior management held accountable) cannot be underestimated.

Regulatory expectations are clear. Firms which take culture seriously by adopting the measures advocated in this article should be well-placed, in the event of regulatory scrutiny. However, these measures should not be seen as solely defensive in nature. In our experience, if actively embraced, they can (and indeed should) add substantive value and result in a materially enhanced operating environment.

Quinn Emanuel's practitioners have extensive recent experience of assisting institutions with culture change and assessment projects—including:

- Undertaking firm-wide risk culture/assurance reviews (reporting to the board);
- Advising on culture change programs (including the identification of relevant cultural indicators);
- Assisting with the development of culture assessment frameworks;
- Culture benchmarking exercises;
- Advising in relation to the mitigation of cultural enforcement/attribution risk;
- Senior/middle management training and awareness–understanding regulatory expectations;
- Devising tailored scenario content;
- Running workshops and reporting feedback; and
- "Mock" supervisory visits/interviews, focused on culture and conduct risk. Q

Enhanced Patent Damages in the Wake of *Halo* May Not Be So Easy to Come By

Background

Last year, in *Halo Electronics, Inc. v. Pulse Electronics, Inc.*, 136 S. Ct. 1923 (2016), the Supreme Court weighed in on the question of enhanced damages in patent cases and rejected the then-existing Federal Circuit test finding that it was at odds with Congressionally-enacted patent law. The decision sparked countless headlines predicting that patent owners would soon cash in under *Halo*'s "relaxed" standard. Recent cases interpreting *Halo*, however, suggest a different conclusion.

Prior to *Halo*, the Federal Circuit established the standard for enhanced damages under section 284 of the Patent Act in *In re Seagate Technologies, LLC.*, 497 F.3d 1360, 1371 (Fed. Cir. 2007). *Seagate* created a two-part test requiring a patent holder to show by clear and convincing evidence (1) "that the infringer acted despite an objectively high likelihood that its actions constituted infringement of a valid patent," (*i.e.*, "objective recklessness") and (2) that this risk of infringement "was either known or so obvious that it should have been known to the accused infringer." *Id.* at 1371.

Halo rejected the *Seagate* test finding that it was directly at odds with the plain language of section 284. In particular, that section provides only that courts "*may* increase the damages up to three times the amount found or assessed"; it does not set forth any criteria for increasing such damages. 35 U.S.C. § 284. As a result, the Court reasoned that a finding of recklessness was not a prerequisite to awarding enhanced damages because section 284 contains no such requirement. *Halo*, 136 S. Ct. at 1932. Because "'the word 'may' [in section 284] clearly connotes discretion'" (*id.* at 1931), the Supreme Court held that "[d]istrict courts enjoy discretion in deciding whether to award enhanced damages, and in what amount." *Id.* at 1932. Nonetheless, the Court made clear that it was not *relaxing* the standard for enhanced damages; instead, the Court rejected *Seagate*'s "unduly rigid" and "inelastic constraints" in favor of providing trial courts with greater flexibility. *Id.* at 1932-34. Such flexibility was intended to permit district courts to assess enhanced damages against *more* culpable infringers, not *less* culpable ones. *See id.* at 1932.

*Post-*Halo *Cases*

Although less than one year old, *Halo* has already been extensively cited in more than 60 published and unpublished decisions and in nearly 200 treatises and published articles.

While much of the initial reaction to the Supreme Court's *Halo* decision wondered whether increased flexibility might lead to a dramatic increase in enhanced damage awards, so far this has not been borne out. Instead, courts appear to be exercising their discretion cautiously and granting enhanced damages only in instances where infringement is, as the Supreme Court put it, "willful, wanton, malicious, [in] bad-faith, deliberate, consciously wrongful, flagrant, or—indeed—characteristic of a pirate." *Halo*, 136 S. Ct. at 1932-34.

For example, many courts have used their discretion to deny enhanced damages *even after a jury finding of willful infringement*. For example, in *Trustees of Boston University v. Everlight Electronics Co.*, the court held that a finding of willful infringement did not require an award of enhanced damages where: "the defendants did not deliberately copy the '738 Patent, did not try to conceal the chips found to be infringing, did reasonably investigate the scope of the patent, and did form a good faith belief that their products did not infringe based on their view of the proper claim construction." No. 12-11935-PBS, 2016 WL 3976617, at *3-4 (D. Mass. July 22, 2016).

Similarly, in *Sociedad Espanola de Electromedicina y Calidad, S.A. v. Blue Ridge X-Ray Co., Inc.*, the court denied a motion for enhanced damages even after the jury found willful infringement, because "the jury's finding of willful infringement . . . does not mandate that damages be enhanced, much less mandate treble damages." No. 1:10-CV-00159-MR, 2016 WL 7473422, at *7 (W.D.N.C. Dec. 28, 2016). The court went on to state that "the touchstone for awarding enhanced damages after *Halo* is egregiousness" and the defendants engaged in no such conduct: "the Defendants presented evidence that they conducted a reasonable investigation of [the plaintiff's] patent claims and made a good faith determination that the patent was not infringed by their activities and that the patent was likely invalid." *Id.* at *7-8; *see also XY, LLC v. Trans Ova Genetics, LC*, No. 13-CV-0876-WJM-NYW, 2016 WL 6664619, at *3-4 (D. Colo. Nov. 10, 2016). Likewise, in *Presidio Components, Inc. v. American Technical Ceramics Corp.*, the court noted that "*Halo* . . . held an award of enhanced damages need not follow a finding of willful infringement" and denied the plaintiff's motion for enhanced damages because the action was nothing more than "a 'garden-variety' hard-fought patent infringement action between two competitors." No. 14-CV-02061-H-BGS, 2016 WL 4377096, at *20-21 (S.D. Cal. Aug. 17, 2016).

Other courts have exercised their discretion to deny enhanced damages in cases where infringement was not willful. For example, in *Radware, Ltd. v. F5 Networks, Inc.*, the court denied enhanced damages after finding that the defendant (1) never copied the plaintiff's patented technology, (2) never intended to harm the plaintiff, (3) took appropriate remedial actions, and (4) did not engage in misconduct during litigation. No. 5:13-CV-02024-RMW, 2016 WL 4427490, at *5-8 (N.D. Cal. Aug. 22, 2016). Likewise, in *Adrea, LLC v. Barnes & Noble, Inc.*, the court denied enhanced damages after finding "no evidence that [the defendant] deliberately copied the '703 Patent," and noting that the plaintiff never alleged that the defendant "sought to cover up or conceal its infringement." No. 13 CIV. 4137(JSR), 2017 WL 44954, at *7 (S.D.N.Y. Jan. 3, 2017).

Still other courts have exercised their discretion to grant enhanced damages, *but only in cases of willful infringement*. For instance, in *Imperium IP Holdings (Cayman), Ltd. v. Samsung Electronics Co.*, the court awarded enhanced damages after finding that the defendants intentionally copied the patented invention: "[d]efendants . . . sought information on how [the patent holder] made its camera"; "[the defendant] asked specifically about anti-flicker and flash technology, requested source code, and, in regard to higher megapixel cameras, control registers, signals, and the circuitry for the interface." No. CV 4:14-CV-371, 2016 WL 4480542, at *6 (E.D. Tex. Aug. 24, 2016); *see also Arctic Cat Inc. v. Bombardier Recreational Prod., Inc.*, No. 14-CV-62369, 2016 WL 4249951, at *9 (S.D. Fla. July 27, 2016) (stating that "[the defendant] is the wanton infringer that the Supreme Court [in *Halo*] sought to punish" because it willfully infringed the plaintiff's patent, never sought to acquire a license, and hired an agent to surreptitiously buy the plaintiff's patents without disclosing itself as the intended buyer); *Dominion Res. Inc. v. Alstom Grid, Inc.*, No. CV 15-224, 2016 WL 5674713, at *18 (E.D. Pa. Oct. 3, 2016) (stating that the defendant "willfully and egregiously induced [a third party's] infringement").

In sum, although *Halo* contains language that gives courts more flexibility in assessing enhanced damages under section 284, removing the "unduly rigid" framework of *Seagate*, courts so far appear to have proceeded cautiously, and in many cases have not granted enhanced damages except where the infringement was particularly egregious. It appears that the initial concern that *Halo* would unleash a wave of decisions granting enhanced damages has not come to pass, although time will tell what the true impact of *Halo* will be. Q

Law360 Names Five Quinn Emanuel Partners 2016 "MVPs of the Year"

Law360 has named five Quinn Emanuel partners as the 2016 "MVPs of the Year" in their practice areas. The "MVPs of the Year" are recognized as "elite attorneys whose successes in high-stakes litigation, record-breaking deals and complex global matters" have made the greatest contributions to their practice areas over the past year. The Quinn Emanuel lawyers named MVPs are: Paul Brinkman – International Trade, William Burck – White Collar, Michael Carlinsky – Insurance, Kevin Johnson – Technology, and Charles Verhoeven – Trials. Q

Insurance Litigation Update

In re Viking Pumps, Inc*: Sowing Confusion for Insurers and Policyholders Alike.* In May 2016, the New York Court of Appeals issued its decision addressing a question of first impression: how "anti-stacking" or "non-cumulation" clauses found in many insurance policies are to be applied when allocating a loss that spans multiple insurance policies. *In re Viking Pump, Inc. & Warren Pumps, LLC*, 2016 N.Y. Slip Op. 03413, 2016 WL 1735790 (May 3, 2016). The question came to the New York Court of Appeals on certified questions from the Delaware Supreme Court in a long-running coverage dispute that involved claims arising from long-term exposure to asbestos causing personal injury over the course of several years and even, in some cases, decades.

Courts have long grappled with the question of how liability for injury caused over time is allocated to successive insurance policies. This issue is important not only in cases involving asbestos, but also in cases involving long-term exposure to other toxic substances as well as claims for environmental damage. Certain jurisdictions allow policyholders to use an "all sums" method to allocate all liability to a single policy up to its limits. Other jurisdictions mandate a "pro rata" approach, allocating the liability to each applicable policy.

Until *Viking*, New York law required pro rata allocation of liability for long-term injuries under the New York Court of Appeals decisions in *Consolidated Edison Co. v. Allstate Insurance Co.*, 98 N.Y.2d 208 (2002) and *Roman Catholic Archdiocese v. National Union Fire Ins. Co.*, 21 N.Y.3d 139 (2013). Those cases cited policy language requiring the insurer to pay "all sums" for occurrences causing damage "during the policy period" and concluded that pro rata allocation was appropriate.

The *Viking* court distinguished that precedent and ruled that where a policy contains "non-cumulation" and "prior insurance" clauses, the policy is "substantively distinguishable" from the policies at issue in *Con. Ed.* Specifically, non-cumulation clauses generally provide that, if the "same occurrence" gives rise to injuries "partly before and partly within" one policy's annual period, the "occurrence limit and the applicable aggregate limit" of that policy must be "reduced by the amount of each payment made by" the insurer "with respect to such occurrence" under a "previous policy" or under "previous annual periods" of that policy. The court concluded that the policy language contemplates injury outside of the policy period, making it distinguishable from policies accounting for liability only "during the policy period." Given this, the court ruled that the policyholder was permitted to select a single policy period to pay "all sums" that otherwise would have been allocated pro-rata to multiple policy periods. The court reasoned that otherwise "the non-cumulation clauses would . . . be rendered surplusage—a construction that cannot be countenanced under our principles of contract interpretation."

Viking, however, is also important and equally clear in holding that non-cumulation clauses are unambiguous and must be enforced under New York law "in accordance with their plain language." The Court of Appeals explained that non-cumulation clauses have a definite meaning and purpose, namely, to prevent stacking—"the situation in which 'an insured who has suffered a long term or continuous loss which has triggered coverage across more than one policy period . . . wishes to add together the maximum limits of all consecutive policies that have been in place during the period of loss.'" *Viking*, Slip Op. at 15; (*citing* 12 Couch on Ins. § 169:5 (3d ed)). The Court acknowledged that its ruling requiring the enforcement of non-cumulation clauses will have a "limiting impact … on an insured's recovery (and, by extension, that of an injured plaintiff)."

Notwithstanding the court's prediction of a limiting impact on Plaintiffs' recoveries from its decision, policyholders had claimed victory because they generally favor the "all sums" approach, which allows them to collect insurance from a single policy period for losses that span multiple years, even decades in certain cases. Recently, however, the Appellate Division scaled back the holding of *Viking*, in *Keyspan Gas East Corp. v. Munich Reinsurance America, Inc.*, 37 N.Y.S.3d 85 (2016). There, the Appellate Division found that the Court of Appeals' limitation on "pro rata" recovery was limited to anti-stacking and anti-cumulation provisions. Absent those provisions, the "pro rata" approach articulated in *Con. Ed.* still applies.

Insurers are now able to obtain pro rata allocation under the ruling in *Keyspan*. In addition, in cases with non-cumulation provisions, the insurer will be citing *Viking* to enforce the plain terms of the non-cumulation clauses, which limit the policyholder's recovery to a single limit of insurance, where a loss or "occurrence" spans multiple policy periods covered by the same insurer. This will have the effect of *reducing* the policyholder's recovery in many cases.

Finally, it remains undecided how to allocate liability to multiple policies when only some of the policies contain the language at issue in *Viking,* while others do not contain those clauses. It is unclear how a court will blend both concepts and apply the rationale for policies with non-cumulation clauses, while also applying the "during the policy period" language requiring a pro rata allocation under the earlier New York Court of Appeals decisions in *Con. Ed.* and *Roman Catholic Archdiocese*.

EU Litigation Update

Asserting Standard Essential Patents in Germany After the European Court of Justice's* Huawei v. ZTE *Decision. In its *Huawei v. ZTE* decision (C-170/13) dated July 16, 2015, the European Court of Justice (ECJ) established a new legal basis for the owners of standard essential patents (SEP) for obtaining injunctive relief against an infringer without abusing their market dominant position under Art. 102 TFEU. The six steps set out by the ECJ are:

1. The patentee must notify the defendant of the alleged infringement;
2. The defendant then must show its willingness to license on FRAND terms;
3. The patentee must make a specific, written offer for a license on FRAND terms;
4. The defendant must diligently respond to that offer without delaying tactics;
5. If the defendant rejects the patentee's offer, it must make a counter-offer on FRAND terms; and
6. If the patentee rejects the counter-offer, the defendant must provide appropriate security (including for past use) and be able to render an account of its acts of use.

Since the decision of the ECJ, the German patent litigation chambers in Düsseldorf, Mannheim and Karlsruhe have rendered a number of fundamental and, in some instances, deviating decisions.

In a judgment dated January 24, 2017 (case no. 2 O 131/16), the Regional Court of Mannheim indicated that for the infringement notification by the patentee, it considers sufficient specifying the concerned SEP as well as the infringing acts of use and the infringing embodiments (no claim charts necessary) even to a parent entity. The Mannheim court found that a temporal offset between the infringement notice and the patent owner's initial offer is not required.

Moreover, the Regional Court of Düsseldorf (case 4a O 73/14) in a judgment dated March 31, 2016 stressed that a notification of infringement could be dispensable if the supplier learned about the infringement case, *e.g.*, by a third party notification or by being informed by the defendant of an already pending infringement case. The Düsseldorf Court of Appeals (case I-15 U 36/16) confirmed this view in a decision regarding the enforcement of a first instance judgment.

German case law is not uniform when it comes to the examination whether the patent owner's offer or patent user's counter-offer is actually FRAND. The courts in Mannheim and Düsseldorf have imposed different requirements for the standard of the examination, *i.e.*, whether only an evident contradiction to FRAND terms is relevant (*see* Regional Court Mannheim, judgment of March 4, 2016, case no. 7 O 96/14) or whether it must be positively determined that the offer meets the FRAND conditions (*see* Higher Regional Court Düsseldorf, decision of November 17, 2016, case no. I-15 U 66/15).

In the most recent case-law, both the Düsseldorf and Mannheim courts gave several indications on the requirements to be met by a license offer in order to be FRAND:

- In an indicative order dated November 17, 2016, the Higher Regional Court Düsseldorf (case no. I-15 U 66/15) indicated that the SEP owner has to present a full-fledged written licensing offer containing details with regard to all factors which are usually the subject matter of a licensing agreement. However, the Düsseldorf court acknowledged that the SEP owner has a certain amount of discretion, in particular, in terms of the determination of the FRAND license fee. It stated that, however, the patent owner has to specify "*the way in which the royalty is to be calculated*" by disclosing all factors that as such contribute to the concrete amount instead of merely referring to the claimed royalty rate and the respective calculation base. The Court also brought forward that a FRAND-compliant offer would require "adaption clauses", *e.g.*, in terms of the royalty rate allowing for adoptions in cases of clearly perceivable changes in the SEP-portfolio.
- According to the Düsseldorf court, the determination of a non-discriminatory FRAND-offer requires proof from the patent owner that the licensing offer is in line with

an established licensing practice by, *e.g.*, production of already existing licensing agreements with third parties to the court. The 7th Chamber of the Regional Court Mannheim (case no. 7 O 19/16) has taken a similar approach and, in a judgment dated November 17, 2016, dismissed the plaintiff's action, because it found that the plaintiff had not met its obligation to sufficiently disclose to the alleged infringer the reasons why it considered the demanded per-unit royalty FRAND. Contrary to this view, the 2nd Chamber of the Regional Court Mannheim, in its decision dated January 24, 2017 (case no. 2 O 131/16), stated that, even though the offer has to contain all conditions that are generally listed in a license agreement for the respective field of business, a pre-trial explanation of the requested amount of the license fee is not necessary under the ECJ's decision.

- When it comes to the scope of the license offer, the Regional Court of Mannheim (judgment of March 4, 2016, case no. 7 O 96/14) and Düsseldorf (judgment of March 31, 2016, case no. 4a O 126/14) have taken a similar approach and found an offer containing a worldwide portfolio license FRAND if that was common in the pertinent field and if at least the alleged infringer uses the SEP worldwide.

The decisions issued so far show that there is not yet a uniform approach of the German courts in establishing the FRAND conditions in accordance with the *Huawei v. ZTE* decision of the ECJ. In particular, there is no uniform standard line concerning the requirements for both the patent owner's offer and the patent user's counter-offer to comply with the FRAND terms. Thus, it is essential for both the owner of an SEP and the alleged infringer to be informed with respect to recent decisions and to develop a clear strategy in order to comply with the requirements established in the case law based on the ECJ's decision.

Appellate Litigation Update

The Effect of the New Presidency on Business Litigation in the United States Supreme Court. With Justice Scalia's seat unfilled for a year since his death in 2016, and with President Obama's nomination of Chief Judge Merrick Garland to that seat stymied in the Senate, President Trump's election gave him the chance to make a consequential appointment to the Nation's highest court. On January 31, 2017, the President nominated Judge Neil Gorsuch of the U.S. Court of Appeals for the Tenth Circuit to fill that vacancy, choosing him from a list of 21 candidates publicly disclosed during the campaign. Although much commentary has focused on the potential effect of a Gorsuch confirmation on social issues like immigration and abortion, a comparison between Judge Gorsuch's and Justice Scalia's records helps predict the impact the new appointment will likely have on business litigation in such areas as deference to administrative agencies, arbitration, and religious exemptions in employment law.

Chevron *Deference.* For over three decades, the doctrine of *Chevron* deference has directed courts to defer to Executive agencies' interpretation of their own regulations in areas of their expertise. First authored by Justice Stevens in *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), the doctrine was expounded by Justice Scalia in cases like *Auer v. Robbins*, 519 U.S. 452 (1997). Later in his career, however, Justice Scalia became more skeptical of allowing "the person who promulgates a law to interpret it as well," suggesting that this is inconsistent with the separation of powers. *Talk Am., Inc. v. Mich. Bell Tel. Co.*, 564 U.S. 50 (2011) (Scalia, J., concurring). Justice Alito remarked after Justice Scalia's death that he had been "rethinking the whole question of *Chevron* deference" out of concern that "agencies were exploiting *Chevron* to usurp Congress' lawmaking authority."

Judge Gorsuch's record suggests that he may have a similar skepticism toward *Chevron* deference. In a notable recent concurrence, he stated that "[m]aybe the time has come to face the behemoth" of *Chevron* deference because such deference "permit[s] executive bureaucracies to swallow huge amounts of core judicial and legislative power and concentrate federal power in a way that seems more than a little difficult to square with the Constitution of the framers' design." *Gutierrez-Brizuela v. Lynch*, 834 F.3d 1142 (10th Cir. 2016) (Gorsuch, J., concurring). In response to criticism of this view, he replied, "We managed to live with the administrative state before *Chevron*. We could do it again." *Id.* at 1158. Should Judge Gorsuch help move the Court toward retreat from *Chevron* deference, this development would encourage businesses to challenge more regulations, both offensively and defensively, with greater confidence that courts will not simply defer to agency interpretations in cases of regulatory ambiguity.

Legislative developments may well accelerate this trend. The House of Representatives recently passed a bill, the Regulatory Accountability Act of 2017, which provides that, "[i]f the reviewing court determines that a statutory or regulatory provision relevant to its decision contains a gap or ambiguity, the court shall not interpret that gap or ambiguity as an implicit delegation to the agency of legislative rule making authority" and also "shall not rely on such gap or ambiguity as a justification either for interpreting agency authority expansively or for deferring to the agency's interpretation on the question of law." H.R. 5, 115th Cong. § 202(1)(B) (as passed by the House, Jan. 11, 2017). If enacted, the Act will likely cabin *Chevron* deference even apart from any changing jurisprudence on the Court.

Arbitration. Justice Scalia authored a number of opinions for the Court strongly favoring arbitration and taking an expansive view of the Federal Arbitration Act ("FAA"). For example, he authored a 5-3 decision upholding arbitration clauses that waive the right to pursue class actions, *American Express Co. v. Italian Colors Restaurant*, 133 S. Ct. 2304 (2013), and a 5-4 decision holding that the FAA preempted a state-law rule deeming class-action waivers in arbitration clauses unconscionable, *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333 (2011). Arbitration-friendly rulings such as these have encouraged the increasing presence of arbitration clauses in a wide variety of consumer and other contracts.

Judge Gorsuch's opinions suggest he will closely adhere to the statutory text of the FAA and the fundamental contractual principles underlying arbitration. For example, he authored an opinion reversing a denial of a motion to compel arbitration and holding that the parties were entitled to a swift trial on the issue of whether they in fact agreed to arbitrate their disputes, as the text of the FAA requires. *Howard v. Ferrellgas Partners, L.P.*, 748 F.3d 975 (10th Cir. 2014). As he noted, "even under the FAA it remains a 'fundamental principle' that 'arbitration is a matter of contract,' not something to be foisted on the parties at all costs." Where the parties do clearly evince the intent to arbitrate their disputes, however, he has expressed strong willingness to compel arbitration. *See Ragab v. Howard*, 841 F.3d 1134 (10th Cir. 2016) (Gorsuch, J., dissenting).

Religious Exemptions. A third area in which Judge Gorsuch's views may affect business litigation is employers' claims of exemption from regulation based on religious conviction. The Supreme Court decision in *Burwell v. Hobby Lobby Stores, Inc.*, 134 S. Ct. 2751 (2014), which upheld a religion-based challenge to a section of the Affordable Care Act that required closely held corporations to provide contraception coverage in employer-sponsored health plans, affirmed a decision in which Judge Gorsuch filed a concurring opinion, *Hobby Lobby Stores, Inc. v. Sebelius*, 723 F.3d 1114 (10th Cir. 2013) (en banc). Judge Gorsuch's concurrence showed considerable deference to the decisions of corporate owners and directors to make their own determination about the degree of "complicity" they can undertake in conduct "their religion disallows." It remains to be seen to what extent Justice Gorsuch would protect religious individuals from taking actions they deem incongruous with their faith when such individuals work at large corporations that are not closely held, or when religious conviction clashes with generally applicable antidiscrimination laws. Q

Rare Products Liability Summary Judgment Victory in West Virginia

West Virginia state court is not a venue where defendants often have high expectations that their motions to dismiss or for summary judgment will succeed, let alone that they can end a mass tort litigation there without a single case being tried or settled. But on February 15, 2017, the Mass Litigation Panel of West Virginia entered an order granting summary judgment in favor of Quinn Emanuel's client Pfizer in the last two West Virginia cases involving allegations that the prescription antidepressant Zoloft causes birth defects.

For several years, a team of Quinn attorneys has been defending Pfizer in Zoloft birth defect litigation. Most of the cases were centered in a federal MDL in the Eastern District of Pennsylvania, where Pfizer was able to obtain exclusion of plaintiffs' causation experts, leading to voluntary dismissal of over 300 cases and summary judgment in over 300 other cases. But there have also been hundreds of cases filed in state courts around the country as well.

One plaintiffs' attorney with a large number of cases from all over the country chose to file them in West Virginia. He began with approximately 40 cases, which were assigned to West Virginia's Mass Litigation Panel. In 2014, Quinn Emanuel successfully obtained dismissal of 29 cases on grounds of forum non conveniens, in a decision affirmed by the West Virginia Supreme Court. The precedent established by this case makes it more difficult for attorneys to file cases in West Virginia on behalf of plaintiffs from other states against non-West Virginia defendants.

Other West Virginia Zoloft birth defect cases were voluntarily dismissed, leaving only 4 cases remaining to be tried. In August 2016, Quinn Emanuel obtained summary judgment for Pfizer in one of those cases. Summary judgment was granted in a second case in October, 2016.

In the last two cases, the plaintiffs designated former FDA Commissioner David Kessler as their expert on the adequacy of the Zoloft label. After plaintiffs withdrew him rather than produce him for deposition, Pfizer moved for summary judgment. In motion papers prepared by Quinn Emanuel, Pfizer argued that West Virginia law requires expert testimony to support plaintiffs' claims that the Zoloft label was inadequate, especially in light of the fact that Zoloft had an FDA-approved warning regarding use in pregnancy and a consensus within the scientific community that the evidence does not support a causal relationship between Zoloft and birth defects. Although the West Virginia Supreme Court had not had a chance to speak to this particular issue, Pfizer argued that in several cases involving complex medical and scientific questions, the West Virginia Supreme Court had held that expert testimony is required on matters that are beyond the common knowledge and experience of the average jurors. The Panel agreed with Pfizer's arguments, held that expert testimony was required and granted Pfizer's motion for summary judgment.

Complete Victory for Cosmetics Manufacturer

In a hotly disputed case involving dozens of claims and counterclaims, the firm recently obtained a complete victory for its client, including a permanent injunction, millions in damages, and more than $1 million in attorneys' fees, all without the expense of a trial.

In 2012, the firm was retained to represent American Rena International Corporation—distributor of cosmetics products under the RENA and RENA BIOTECHNOLOGY trademarks—against a former sales agent who started selling competing products under a copycat brand called "aRena." Within weeks of being engaged, the firm had obtained a far-reaching preliminary injunction from the Central District of California enjoining defendants from selling their infringing products and requiring them to turn those products over to the firm. The Ninth Circuit affirmed that injunction.

Defendants responded by upping the ante: they claimed for the first time that *they* had actually used their mark *before* American Rena, giving them priority and rendering American Rena the infringer. Defendants provided three consumer declarations attesting to early purchases of "aRena" products to substantiate this allegation.

The firm immediately took focused discovery into these declarations—and obtained proof that they were fabrications. The first came from an individual who does not exist. The second came from an individual who testified that she did not sign it and had never seen it. The third came from a witness who testified that she was tricked into signing the declaration, which she could not read. None of the witnesses had purchased defendants' products at the points in time that defendants claimed.

Armed with this (and much more) evidence of litigation misconduct, the firm moved for terminating sanctions—the most severe sanctions a court can impose. The district court granted that motion in full, and recently entered a final judgment dismissing defendants' counterclaims, entering judgment against defendants on all of American Rena's affirmative claims, awarding American Rena $1.2 million in attorneys' fees, awarding American Rena millions more in damages, and making the preliminary injunction barring sales of defendants' products permanent. It is very unusual for a federal court to grant relief of this magnitude in sanctions.

It took a year of tenacious efforts by the firm to obtain proof of defendants' misconduct notwithstanding their efforts to cover up their tracks. Those efforts were clearly worthwhile.

Summary Judgment Victory for Moldex-Metric in Antitrust Suit

The firm secured an important summary judgment ruling for its client Moldex-Metric, in *Moldex Metric, Inc. v. 3M Company et al.*, when the Honorable Joan N. Ericksen of the District Court of Minnesota found that an earlier patent suit that 3M had pursued against Moldex, and in which the firm had prevailed, was so completely baseless as to constitute objectively baseless litigation under the Sherman Act and state malicious prosecution law. The case involves non-linear attenuation earplugs used by the U.S. Military which block loud percussive sounds (gun blasts) that can damage hearing, while still allowing the wearer to hear softer spoken words from a fellow combatant. For a decade, 3M had a virtual monopoly in supplying these products to the entire U.S. Military. In 2011, however, Moldex developed a competing product that the Army began ordering instead of the 3M product. 3M filed suit against Moldex in 2012 claiming that Moldex's new earplugs infringed a 3M patent directed to a particular type of earplug, in which two different settings could be obtained depending on which end of the plug was inserted into the wearer's ear. Moldex's accused earplug was not a dual-ended plug; rather, it was a single-ended plug similar to various prior art plugs cited in and distinguished over in the patent asserted by 3M.

After 3M aggressively prosecuted its infringement suit against Moldex for over one year, forcing Moldex to incur large litigation costs in discovery, 3M served Moldex with a covenant not to sue on its earplug patent on the eve of a hearing on the parties' summary judgment papers, thereby stripping the court of jurisdiction and resulting in the dismissal of 3M's claim with prejudice. One year later, Moldex brought suit alleging that 3M's prior patent infringement claim violated Section 2 of the Sherman Act, and state malicious prosecution law, because no reasonable litigant in 3M's position would have expected to be successful on the merits of the claim, *i.e.,* the claim was objectively baseless, and because 3M pursued the claim with the anticompetitive and predatory purpose of driving Moldex out of the non-linear attenuation earplug military market, *i.e.,* the claim was subjectively baseless. In its recent ruling granting Moldex's motion for summary judgment on objective baselessness, after noting the heavy burden faced by Moldex in overcoming 3M's *Noerr-Pennington* immunity which typically blocks sham litigation claims like the one brought by Moldex, the court concluded in this case the specification of 3M's asserted patent made clear that it read on dual ended earplugs only, and that 3M could not have reasonably expected to succeed on the merits of that claim. The case will now proceed to jury trial to determine whether 3M's prior claim was subjectively baseless. Q

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Prior results do not guarantee a similar outcome.

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