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Converium Decision by Dutch Court Promotes European Venue for Binding Settlement of Mass Claims

The Amsterdam Court of Appeal's recent decision in *Converium Holdings AG* may signal the emergence of Dutch courts as a forum in which parties can settle cross-border mass claims, subject only to opt outs. In November 2010, that court held that it could declare binding a proposed settlement in a case in which 12,000 investors, only 200 of whom were from the Netherlands, alleged securities fraud on the part of Converium, a Swiss reinsurer with no securities listed on Netherlands-based exchanges. *Scor Holdings AG (f/k/a Converium Holdings AG)*, Gerechtshof Amsterdam [HoF] [Amsterdam Court of Appeal], Amsterdam, 12 Nov. 2010 NJ—(Neth.) The decision notably expanded the jurisdiction the same court had exercised a year before in approving a settlement between Royal Dutch Shell and a class of non-U.S. investors who alleged that Shell had misstated its proven reserves. *Shell Petroleum N.V./Dexia Bank Nederland N.V.*, Gerechtshof Amsterdam [HoF] [Amsterdam Court of Appeal], Amsterdam, 29 May 2009 NJ 506 (Neth.) (hereinafter "*Shell Petroleum*").

The significance is that the Netherlands is the only European country that, like the United States, provides for the binding settlement of mass claims. Although *Converium* will be provisional pending a fairness hearing later this year, it will likely become final, thus making the settlement binding, at a minimum, in all EU member states, as well as Switzerland, Iceland, and Norway, under the Brussels I Regulation and the Lugano Convention.

The Amsterdam Court of Appeal appears to be acting consciously to create a forum for cross-border mass claims; it referenced limitations imposed, for example, by the U.S. Supreme Court in *Morrison v. National Australia Bank Ltd.*, __U.S.__, 130 S. Ct. 2869 (2010), restricting the extra-U.S. application of Section 10(b) of the Securities Exchange Act. *Id.* at 2884 (holding that Section 10b-5 applies "[o]nly [to] transactions in securities listed on domestic exchanges, and domestic transactions in other securities"). Aggrieved shareholders already appear to have recognized *Converium's* significance: A foundation representing a global consortium of shareholders filed a securities fraud class action on January 10, 2011, in the Utrecht Civil Court against Fortis—once the largest financial institution in Belgium and the Netherlands that collapsed in spectacular fashion following its ill-fated acquisition of ABN Amro. Moreover, in the Fortis case, shareholders are not presenting a proposed settlement, but rather are raising claims for adjudication.

Overview of Dutch Class Action System

Unique to European legal systems, Dutch law provides rudimentary elements of a class action system. The two most important provisions are the Dutch Act on the

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Quinn Emanuel Selected as One of *Law360*'s Insurance Groups of the Year

Law360 recently announced that Quinn Emanuel is one of the top five "Insurance Groups of 2010." *Law360* noted that its editors solicited nominations from more than 300 law firms before selecting the five that had "wrack[ed] up crucial victories for their clients." The publication highlighted Quinn Emanuel's successes in: (1) persuading the U.S. Court of Appeals for the Second Circuit to vacate a $35 million jury verdict against American International Group Inc. in a suit brought by rival insurer AXA Versicherung AG, and (2) obtaining a dismissal with prejudice of a nationwide class action against AIG spinoff Chartis Insurance Group in a case in which investors sought reimbursement for losses suffered as a result of having invested in Bernard Madoff's ponzi scheme. Q

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Collective Settlement of Mass Claims (Wet collectieve awkikkeling massaschade or "WCAM") and Article 3-305a of the Dutch Civil Code, authorizing parties to bring collective actions.

WCAM, passed in 2005, allows parties to petition Dutch courts to declare a mass settlement binding on a class or classes of persons whose members suffered similar injury. See BW (Civil Code) Art. 9:907. Under WCAM, parties to a prior-negotiated settlement may petition the Amsterdam Court of Appeal—a court akin to a U.S. federal circuit court—to declare the agreement binding on a class whose members suffered similar damages. Parties to the settlement must include both those that inflicted the harm and will pay compensation and a foundation organized under Dutch law to represent the interests of the class and administer the settlement. *Id.* The court may reject a proposed settlement if the interests of the persons on behalf of whom the settlement was concluded are not adequately safeguarded or if the foundation is not adequately representative of the class. See *id*. at Art. 9:707(3).

Although WCAM authorizes the settlement of mass claims, it provides no authority to bring claims on behalf of a class. Parties seeking to bring a collective action in Dutch courts must do so under Article 3:305a of the Civil Code. Like WCAM, Article 3:305a allows a foundation organized for the express purpose of representing the legal interests of a class to bring claims on its behalf. Article 3:305a does not, however, provide for the award of compensatory damages. As a result, collective actions are generally styled as declaratory judgment actions to determine certain facts and issues of liability on a class-wide basis. Once liability is established, the foundation generally moves to settle claims on a class-wide basis under WCAM.

***Transnational Securities Fraud Class Actions in Dutch Courts:* Shell Petroleum *to* Converium**

Dutch courts first waded into the field of transnational securities fraud class actions in *Shell Petroleum*, when the Amsterdam Court of Appeal issued a landmark decision declaring binding a $352 million settlement between Royal Dutch Shell (and its affiliates) and non-U.S. shareholders. To recover for losses incurred as a result of Shell's misstatement of its oil reserves, Shell's non-U.S. shareholders attempted to join a U.S. class action filed in January 2006. *In re Royal Dutch Shell Transp. Sec. Litig.* 522 F. Supp. 2d 712 (D.N.J. 2007). However, even under the more forgiving conduct and effects jurisdictional test then applied by U.S. federal courts, the non-U.S. shareholders faced an uphill battle even to obtain a hearing in a U.S. court. As foreign shareholders suing a foreign corporation whose stock they purchased on a foreign exchange, their claims had little, if any, connection to the U.S.

The existence of jurisdiction was never determined by a U.S. court. Instead, frustrated in their efforts to negotiate a global settlement, Shell's attorneys approached the class of non-U.S. shareholders and separately negotiated a $352 million settlement. See Robert J. Giuffra, Jr., *Dutch Case Has Implications for Global Class Actions*, Harv. Forum on Corp. Governance, June 6, 2009, available at http://blogs.law.harvard.edu/corpgov/2009/06/21/dutch-decision-has-implications-for-global-class-actions/.

To enforce that settlement, the parties turned to WCAM. The non-U.S. shareholders joined a foundation organized under Dutch law and petitioned the Amsterdam Court of Appeal to use its authority under WCAM to declare the settlement binding. Five other applicants joined the petition: Shell Petroleum N.V.; Shell Transport and Trading, a Shell subsidiary incorporated in the U.K.; two Dutch foundations representing the interests of pension funds; and the Dutch Investors' Association, a private association that acts on behalf of Dutch shareholders generally but did not represent individual investors.

The central question considered jurisdiction because the proposed settlement was the first attempt to apply WCAM to a significant number of claimants domiciled outside the Netherlands. *See* Helene Van Lith, The Dutch Collective Settlements Act and Private International Law, at 19-22 (2010). Because Shell is Dutch, the court was primarily concerned with whether it could exercise WCAM jurisdiction over the non-U.S. shareholders—many of which were domiciled outside the Netherlands. As to shareholders domiciled in the Netherlands, elsewhere in the EU, Norway, Switzerland, and Iceland, the court declared itself competent to declare the settlement binding under the Brussels Regime—the set of rules governing which European courts have jurisdiction in civil or commercial legal disputes. See *Shell Petroleum*, ¶¶ 5.18, 5.26-5.27. The assertion of jurisdiction over shareholders residing elsewhere posed a more difficult question, but the court based jurisdiction over them on the fact that five of the six applicants seeking to have the settlement declared binding were domiciled in the Netherlands. *Id.*, ¶ 5.16. Having found jurisdiction, the Amsterdam Court of Appeal then declared the Shell settlement binding on all class members that failed to opt-out in a timely fashion. *Id.*, ¶ 9.

Although *Shell Petroleum* drew attention, observers were uncertain how far Dutch courts would extend their reach over the settlement of mass claims. *Shell Petroleum*, after all, involved Shell, a Dutch company with shares traded on Euronext Amsterdam, and a class of investors predominately domiciled in the Netherlands.

Converium was significant because the parties and claims had far less connection to the Netherlands. The allegations of securities fraud arose after Converium, a Swiss reinsurer with shares listed on the Swiss Exchange and the NYSE, restated its available loss reserves, causing a drop in stock price. Shareholders filed a class action on behalf of all investors in the Southern District of New York. *In re SCOR Holding (Switz.) AG Sec. Litig.*, 537 F. Supp. 2d 556, 569 (S.D.N.Y. 2008). The court, however, certified only a limited class of Converium shareholders owing to concerns over subject matter jurisdiction and dismissed the claims of any non-U.S. shareholder that had purchased claims on the Swiss Exchange.

As in *Shell Petroleum*, the *Converium* parties turned to WCAM. They formed a foundation to represent the interests of non-U.S. Converium shareholders in settlement negotiations and to present the settlement to the Dutch court for approval alongside Converium's parent, SCOR Holdings AG. Notwithstanding that none of the potentially liable parties and few of the shareholders (200 of 12,000) were domiciled in the Netherlands, the court ruled that it had jurisdiction to declare the settlement binding. *Converium*, ¶ 3. The court's action implied strongly that *Shell Petroleum* had not set an outer limit to the court's jurisdiction. Its decision also demonstrated awareness that it was making available a forum where none might otherwise be available. It referenced the Supreme Court's decision in *Morrison*, noting that to refrain from exercising jurisdiction would leave non-U.S. shareholders that had purchased Converium shares on the Swiss Exchange without a court in which to bring their claims. *Id.*, ¶¶ 2.6-2.7.

The court began its analysis by ruling that because the settlement agreement would be performed in the Netherlands (*i.e.,* the settlement would be paid there), provisions of the Brussels Regime conferring jurisdiction to enforce contracts in the place of performance provided the initial grant of jurisdiction. *Id.*, ¶ 2.8 The Brussels Regime also allowed the court to declare the settlement binding between shareholders domiciled in the Netherlands, elsewhere in the EU, Norway, Switzerland, and Iceland. *Id.*, ¶ 2.12. To assert jurisdiction over shareholders residing elsewhere, the court relied exclusively on the fact that, as required by WCAM, a foundation organized under Dutch law represented the class of non-U.S. shareholders and would administer the settlement. *Id.* In the court's view, the foundation's connection to the Netherlands, along with the fact that the settlement would be executed in the Netherlands, sufficed to authorize the exercise of jurisdiction. *Id.*, ¶ 3.

Converium thus dramatically expanded the potential reach of the Amsterdam Court of Appeal to settle mass claims. After *Converium,* the presence of a foundation organized under Dutch law to represent shareholders seems to be the only prerequisite to the exercise of jurisdiction to declare a binding settlement. Although *Converium* does not make the point explicitly, its logic suggests that Dutch courts may exercise jurisdiction over transnational mass claims whenever WCAM itself is satisfied—*i.e.*, so long as the interests of the persons on behalf of whom the settlement was concluded are adequately safeguarded and the foundation's membership is adequately representative of the class of injured persons. See BR (Civil Code) Art. 9:707(3).

Current State of Play

Converium's expansion of Dutch jurisdiction should prompt shareholders and foreign securities issuers alike to take note that Dutch courts may be filling the void created by *Morrison*. As noted above, aggrieved Fortis shareholders have already sought to build on *Converium* and capitalize on the continued opening of Dutch courts to cross-border class actions. Tellingly, *Morrison* incorporates all the claims brought by the global class of investors in a suit previously dismissed in the U.S. federal courts. See *Copeland v. Fortis*, 685 F. Supp. 2d 498 (S.D.N.Y. 2010). To press their claims in the Dutch courts, the Fortis shareholders have joined a foundation, officially known as the Stichting Investor Claims Against Fortis ("SICAF"), to pursue an action under Article 3-305a to obtain a class-wide declaratory judgment that Fortis violated duties owed to investors. *See* http://investorclaimsagainstfortis.com.

SICAF's lawsuit seeks to approximate a U.S.-style class action and is the first of its kind in that it is not presenting a pre-packaged settlement. Instead, it is an Art. 3:305a collective action claim unaccompanied by a request under WCAM for approval of a settlement. If it is successful at the declaratory judgment stage, SICAF will have bound its members to participate in any settlement negotiated under WCAM. Given the expansive breadth of Dutch jurisdiction under *Converium*, SICAF's suit may portend a wave of shareholder-plaintiffs turning to Dutch courts to press cross-border mass claims, including ones that are barred in the U.S. Q

Mostly Good News for Defendants in ERISA Stock-Drop Cases

Most public companies offer their own stock as one investment option in their 401(k) plans. Over the past several years, many have seen some of their stock price drop, even if it later rebounded. These circumstances are often enough to prompt lawyers to target a company for an ERISA "stock drop" lawsuit, claiming that plan fiduciaries should not have allowed investments in company stock during periods of price decrease, and should have provided much more cautionary information to participants, perhaps even non-public inside information. Courts have become increasingly skeptical of such claims absent compelling facts, and are increasingly willing to dismiss them on the pleadings alone. Several recent decisions continuing the trend favoring defendants are particularly worth noting.

The leading case establishing a higher standard for suing plan fiduciaries in relation to company stock is *Moench v. Robertson*, 62 F.3d 553 (3d Cir. 1995). *Moench* recognized a "presumption of prudence" when plan fiduciaries allow company stock as an investment option. See *id.* at 571. Rebutting that presumption requires a substantial showing. *Id. Moench* has been followed by most circuit courts of appeal.

In the 15 years since *Moench,* litigation has focused on a number of key issues, all of which have been the subject of very recent cases:

- Is the *Moench* presumption a standard applicable at the pleadings stage on a Rule 12 motion, or is it an evidentiary presumption that comes into play later?
- Does *Moench* apply only when the company stock investment option is mandated by an Employee Stock Option Plan ("ESOP"), or does it apply to any Eligible Individual Account Plan ("EIAP") that allows investment in company stock, even if such investment is not required?
- What is required to rebut the presumption, including on a Rule 12 motion to dismiss under *Bell Atlantic Corp. v. Twombley*, 550 U.S. 544 (2007)?
- Does ERISA Section 404(c), which provides a "safe harbor" when a plan holds each participant's assets in a separate account and enables the participant to exercise control over his or her own assets, also protect plan fiduciaries from claims that company stock should not have been selected or continued as an investment option?
- Can a misrepresentation claim be based on statements in SEC filings?
- To state a viable misrepresentation claim, must a plaintiff plausibly allege actual reliance on the alleged misrepresentation?

Two recent cases discussed the interplay between the Section 404(c) safe harbor and claims against fiduciaries alleging it was imprudent to offer company stock as an option. *Pfeil v. State Street Bank and Trust*, 2010 WL 3937165 (E.D. Mich. Sept. 30, 2010) addressed the General Motors ESOP. The court held that the plaintiff had alleged facts sufficient to state a claim that the fiduciary acted imprudently in continuing to offer GM stock as an option in the face of numerous "red flags" as GM headed toward bankruptcy. See *Id.* at *5. The court granted a motion to dismiss, noting that Section 404(c) relieves a fiduciary of liability for a loss "caused" by the participant's exercise of control over his or her assets. See *id.* at *5. Finding that it was undisputed that the plan offered other investment options not at issue, that the participants "had total control over how to allocate their assets," since the fiduciary "cannot be held liable for actions which Plaintiffs controlled," the court held that "Plaintiffs cannot show causation." *Id.* at *6.

The Department of Labor has filed amicus briefs in several cases, maintaining its position that the Section 404(c) safe harbor should not apply to the selection or continuation of company stock as an investment option.

In *Howell v. Motorola*, 2011 WL 183966 (7th Cir. Jan. 21, 2011), the Seventh Circuit agreed with the Department of Labor, noting that "the purpose of section 404(c) is to relieve the fiduciary of responsibility for choices made by someone beyond its control," but that "the choice of which investments will be presented in the menu that the plan sponsor adopts is not within the participant's power." For that reason, the court distinguished an earlier opinion suggesting a different conclusion, and instead followed *DiFelice v. U.S. Airways, Inc.*, 497 F.3d 410, 418 (4th Cir. 2007). See *Howell*, 2011 WL 183966 at *15. It held that "the selection of plan investment options and the decision to continue offering a particular investment vehicle are acts to which fiduciary duties attach, and that the safe harbor is not available for such acts." *Id.*

Nevertheless, the court found the presumption of prudence applied and that the plaintiffs could not overcome that presumption. See *id.* at *15. Even though it rejected Section 404(c) as an absolute defense, it found that the availability of other investment options, and the ability of participants to "move their dollars away from the Motorola stock fund into a different fund," ensured that "no participant's retirement portfolio could be held hostage to Motorola's fortunes." *Id.* at *16-17. The court also noted that despite the stock drop at that time, Motorola was by no means facing "imminent collapse"—the test many courts use when applying the *Moench* presumption—and was "fundamentally a sound company." *Id.* at *17.

After many missed opportunities, the Ninth Circuit finally adopted the *Moench* presumption in *Quan v. Computer Scis. Corp.*, 623 F.3d 870 (9th Cir. 2010). The court acknowledged that its historical reluctance to follow *Moench* "was that it was not sufficiently deferential to or protective of fiduciaries, not that it placed too great a burden on those asserting breach-of-fiduciary duty claims." *Id. Quan* held that the deferential *Moench* presumption applies not just to mandatory ESOPs, but also to all EIAPs when "plan terms require or encourage the fiduciary to invest primarily in employer stock." *Id.* Without expressly saying that Section 404(c) also applies to fiduciary decisions to allow investments in company stock, the court stated that applying the *Moench* presumption "will allow fiduciaries to 'fulfill their duties in the safe harbor that Congress seems to have intended to provide them' for managing EIAPs and ESOPs." *Id.* at 882. *Quan* also articulated a high standard concerning "how bad do things have to be" before reasonable fiduciary would disallow company stock as a permitted investment. *Id.* Following other courts that reached similar conclusions, it held that plaintiffs must make plausible allegations that either "clearly implicate the company's viability as an ongoing concern," or show both "a precipitous decline" in the stock price together with other evidence "that the company is on the brink of collapse or is undergoing serious mismanagement." *Id.*

Other courts have also applied *Moench* broadly. In *Dudenhoeffer v. Fifth Third Bancorp*, 2010 WL 4970767 (S.D. Ohio Nov. 24, 2010), an Ohio court granted a motion to dismiss, holding that the principal inquiry is whether the particular fund "invests primarily in qualifying employer securities." Other cases applying *Moench* to EIAPs include *In re Bank of America Corp. Sec., Derivative and ERISA Litig.,* 2010 WL 3448197 (S.D.N.Y. Aug. 27, 2010) *Wright v. Medtronic,* 2011 WL 31501 (D.Minn. Jan. 5, 2011) and *Acosta v. MEMC*, 2010 WL 4069202 (E.D. Mo. Oct. 18, 2010).

The Southern District of New York has rendered many recent opinions in "stock drop" cases, including suits related to the inclusion of company stock in the Bear Stearns, American Express, Bank of America, Citibank, and Sallie Mae plans. The opinion in *In re Bear Stearns Cos., Inc. Sec., Derivative and ERISA Litig.*, 2011 WL 223540 (S.D.N.Y. Jan. 19, 2011), contains an exhaustive discussion of fiduciary duties in relation to company stock. The *Bear Stearns* court dismissed all breach of fiduciary duty claims. Rejecting its earlier holding to the contrary in *In re Morgan Stanley ERISA Litig.*, 696 F. Supp. 2d 345 (S.D.N.Y. 2009), it held that the *Moench* presumption applies at the motion to dismiss stage. See 2011 WL 223540, at *133. *Bear Stearns* also emphasized that the *Moench* presumption is a "substantial shield," and creates a very high bar for the plaintiff in suits alleging the improper selection and continuation of the company stock investment option. *Id.* at *134. The court then held that allegations that the stock plummeted from $171 to $5 per share were insufficient to survive a Rule 12 motion notwithstanding the further allegations that the shares had been artificially inflated by misrepresentations and omissions, and that the company was grossly mismanaged and in such financial extremes that it collapsed during the alleged class period. *Id.* at *135-36. The court deemed such allegations conclusory and held that when a plaintiff alleges a danger of imminent collapse, he or she must be specific as to exactly when the danger existed, and when the fiduciaries should have known of it. *Id.* at *136; *see also In re Bank of America Corp. Sec., Derivative and ERISA Litig.,* 2010 WL 3448197 (S.D.N.Y. Aug. 27, 2010)*Bear Stearns* also held, as have other courts, that plan fiduciaries are not "investment advisors" and have no duty to disclose non-public information to plan participants, even if such information would be highly relevant to the prospects for the company stock. *In re Bear Stearns*, 2011 WL 223540 at *133; *see also In Re Constellation Energy ERISA Litig.*, 2010

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Patent Litigation Update

Discovery Ordered Regarding Identification of Anonymous Web-Posters: In *In re Anonymous Online Speakers*, 2011 WL 61635 (9th Cir. Jan. 7, 2011), the Ninth Circuit addressed for the first time whether and when a provider of online content must disclose the identities of individuals who have used pseudonyms when making website posts. The answer, the court held, depends on the type of speech involved.

The defendant had allegedly facilitated an online smear campaign against the plaintiff via postings on the defendant's websites. On First Amendment grounds, the defendant refused to reveal the identities of the individuals posting on its websites. The plaintiff moved to compel, and the pseudonymous posters contested the motion.

The trial court distinguished between statements that were "factually based and thus capable of a defamatory meaning" and statements that constituted opinions. It ordered disclosure of the identities of those who had posted fact-based statements and denied the motion to compel with respect to those who had posted opinions. The pseudonymous posters then sought a writ of mandamus from the Ninth Circuit.

Although the Ninth Circuit declined to adopt a particular approach to issues related to anonymous and pseudonymous postings, it held that the district court had offered the posters too much protection. It noted that although both online speech and the right to speak anonymously are protected by the First Amendment, "the degree of scrutiny varies depending on the circumstances and the type of speech at issue" and that commercial speech enjoys less protection than political speech. The Ninth Circuit left to the district court "the details of fashioning the appropriate scope and procedures for disclosure of the identity of the anonymous speakers." It did not provide any specific guidance to the district court other than to identify a protective order with different levels of disclosure for different categories of documents as "just one of the tools available to the district court to oversee discovery of sensitive matters that implicate First Amendment rights."

Federal Circuit Abolishes 25 Percent Rule for Calculating Damages: The Federal Circuit recently rejected the so-called "25 percent rule of thumb" for calculating damages in patent lawsuits.

Prior to *Uniloc USA, Inc. v. Microsoft Corp.*, 2011 WL 9738 (Fed. Cir. Jan. 4, 2011), damages calculations in patent cases often began with a baseline royalty rate of 25 percent of the value of the accused product. That rate was then adjusted up or down in accordance with applicable *Georgia-Pacific* factors.

In *Uniloc*, however, the Federal Circuit found that "evidence relying on the 25 percent rule of thumb … fails to tie a reasonable royalty rate to the facts of the case at issue." Specifically, the court found that the 25 percent rule: fails to account for the unique relationship between the patent and the accused product; fails to account for the unique relationship between the parties; and is essentially arbitrary because it bears no relationship to the hypothetical negotiation model that should guide a damages analysis. As the Federal Circuit explained, "the 25 percent rule of thumb would predict that the same 25% / 75% royalty split would begin royalty discussions between, for example, (a) TinyCo and IBM over a strong patent portfolio of twelve patents covering various aspects of a pioneering hard drive, and (b) Kodak and Fuji over a single patent to a tiny improvement in a specialty film emulsion." Accordingly, it held that evidence relying on the 25 percent rule of thumb is inadmissible under *Daubert* and the Federal Rules of Evidence.

Securities Litigation Update

Securities Class Actions Continue to Decline as Percentage of All Securities Litigation: Using different statistical methods, year-end studies published by both Advisen and Cornerstone Research found that, despite a strong surge in filings in the latter part of 2010, the number of securities class actions filed in 2010 was below the historical average. The reports noted that class actions have dropped from approximately 33 percent of all securities litigation prior to 2006 to just 16 percent in 2010, although the number of securities class actions filed in 2010 increased slightly from 2009. The decrease in class action filings as a percentage is significant given that both Advisen and Cornerstone found a significant drop in credit-crisis-related filings. Cornerstone indeed reported a 76 percent drop from 2009. With heightened pleading standards and other obstacles to prosecuting securities actions, derivative and single-/joint-party suits have become more common.

Nonetheless, the reports noted that securities class actions are still one of "the most commonly filed types of security suits," and "typically produce most of the largest settlements." For example, Advisen termed "eye-popping" the tentative $600 million class action settlement agreed to by Countrywide Financial in 2010. Cornerstone also noted that many analysts expect a higher number of M&A transactions in 2011, which may translate into sustained, if not increased, securities class action filings this year.

Supreme Court Rules That Facts Can Be Material, Even if Not "Statistically Significant": In a much-anticipated decision clarifying materiality standards for pleading a claim under the federal securities laws, the Supreme Court ruled unanimously on March 22, 2011 that a company cannot withhold information from shareholders simply because it doesn't meet the scientific standard of statistical significance. In *Matrixx Initiatives, Inc. v. Siracusano*, No. 09-1156, the Court resolved a split in the circuit courts concerning the need to plead "statistical significance" to establish materiality for purposes of a securities fraud claim. The First, Second, and Third Circuits had held that a pharmaceutical company's failure to disclose complaints concerning a drug is not materially misleading unless the company is alleged to have had knowledge that the drug caused "a statistically significant number of" medical problems. *See N.J. Carpenters Pension and Annuity Funds v. Biogen IDEC Inc.*, 537 F.3d 35 (1st Cir. 2008); *In re Carter-Wallace, Inc. Sec. Litig.*, 150 F.3d 153 (2d Cir. 1998); *Oran v. Stafford*, 226 F.3d 275 (3d Cir. 2000). In *Siracusano*, however, the Ninth Circuit had held that a bright-line rule to determine materiality is inappropriate and that questions of materiality should generally be left to the trier of fact. *Siracusano v. Matrixx Initiatives, Inc.*, 585 F.3d 1167 (9th Cir. 2009), *cert. granted*, __U.S.__, 130 S. Ct. 3411 (2010). In a decision by Justice Sonia Sotomayor, the Court agreed with the Ninth Circuit that there is no "bright-line rule" governing when companies must disclose information to shareholders; "[g]iven that medical professionals and regulators act on the basis of evidence of causation that is not statistically significant, it stands to reason that in certain cases reasonable investors would as well." Unfortunately for companies making disclosure decisions, the Court did not specify what a "reasonable investor" would consider material. The Court, however, did not "create an affirmative duty to disclose any and all material information," but instead required disclosure "only when failure to disclose would render other statements misleading."

Supreme Court to Consider Expansive View of "Primary Violator" Liability: Also currently under consideration by the Supreme Court is *Janus Capital Group, Inc. v. First Derivative Traders*, No. 09-525, a case involving a Fourth Circuit decision that potentially expands the definition of "primary violator" under the federal securities laws. In *Janus Capital*, investors in mutual funds sued the funds' holding company (Janus Capital Group) and investment advisor (Janus Capital Management), alleging that the mutual funds were mismanaged, resulting in a loss to investors. The Fourth Circuit found that investors had asserted a viable Section 10b-5 claim because the Janus entities had helped to draft and disseminate the funds' prospectuses. The funds argued that they could not be liable for assisting in preparation of the prospectuses, given the Supreme Court's rulings in *Cent. Bank of Denver v. First Interstate Bank*, 511 U.S. 164 (1994), and *Stonebridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, __U.S.__, 128 S. Ct. 761 (2008), which eliminated aiding and abetting liability in private Rule 10b-5 actions and confirmed that only "primary violators" are liable for securities fraud.

The questioning at the December oral argument suggested that the justices might be divided as to whether a fund's investment manager can be subject to liability as a "primary violator" under the federal securities laws based on alleged misstatements in the fund's prospectuses. Several justices asked about the relationship between an investment advisor and a fund, including whether an investment advisor should be viewed as the equivalent of a corporate manager liable for a corporation's misstatements. A decision upholding the Fourth Circuit's decision might represent a significant expansion of the current scope of "primary violator" liability under the securities laws.

Speculators Bet on Madoff Claims: The latest securities to attract the attention of distressed-investment Wall Street traders are claims in the notorious Bernard L. Madoff bankruptcy case, in which total losses are estimated at roughly $20 billion. As the *New York Times* has reported, hedge funds and other investment firms have quietly been contacting Madoff victims whose loss claims have been approved by the Madoff trustee, Irving Picard. See http://dealbook.nytimes.com/2010/12/13/speculators-are-eager-to-bet-on-madoff-claims/. The funds offer to buy approved Madoff claims immediately for cash, but at a sharp discount from their face value, ranging from 20 to 34.5 cents on the dollar. With the trustee already having collected more than $2 billion and the estate continuing to commence big-ticket actions, the Madoff bankruptcy process is viewed by some as creating an opportunity to earn big returns. Recent filings have included lawsuits against deep-pocketed banks such as JPMorgan Chase, UBS and HSBC, among others.

Bankruptcy lawyers expect the legal fights will take years to resolve, with no guarantee of recovering any of the billions being sought. But for small investors caught in the Madoff fraud who cannot afford to wait years to recover, getting some cash now might be more attractive than waiting for a future litigation payoff.

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SEC to Implement Whistleblower Reward Program by Mid-April: The Wall Street Reform and Consumer Protection Act, signed into law by President Barack Obama on July 21, 2010, sets a deadline of April 15, 2011, for the SEC to implement its so-called "reward" program, codified in Section 21F of the Securities Exchange Act of 1934. The objective of the program is to reward whistleblowers who offer information about securities law violations.

The commentary accompanying proposed Regulation 21 F, issued in November 3, 2010, offered insights into the SEC's intentions. Among other things, the SEC has attempted to strike a balance between encouraging whistleblower reporting directly to the SEC and preserving the incentive for employees to report violations internally. Proposed Regulation 21F thus allows a whistleblower to wait up to 90 days between reporting violations internally and providing information to the SEC without compromising eligibility for a cash reward. The SEC hopes that this "grace period" will give corporations a sufficient amount of time to conduct internal investigations and respond appropriately to a whistleblower's information. In addition, the SEC will consider a whistleblower's cooperation with his or her company's internal compliance program as a favorable factor in determining the percentage of any recovery that the whistleblower receives as reward.

Japanese Litigation Update

Quinn Emanuel Foundation to Donate Towards Japan Relief: On March 11th, Japan was hit by one of the largest earthquakes ever recorded. Rescue and recovery efforts have already begun and are expected to last for months, with numerous international organizations and governments offering assistance. During this time of crisis in Japan, the firm wishes to extend our thoughts and support to the victims of the earthquake and its aftermath. Our firm, through the Quinn Emanuel Foundation, will be accepting donations. Our goal is to focus on helping families, children, schools, and others that will continue to be impacted as the government tries to rebuild infrastructure. If you would like to contribute, please contact Jackie Toth at the Quinn Emanuel Foundation, jackietoth@quinnemanuel.com. The Foundation is a 501(c)(3). All contributions are fully tax deductible.

Public Prosecutor Arrested: In one of the most publicized scandals in the history of the Japanese Public Prosecutors Office, a former Chief Prosecutor of the Special Investigation Squad of the Osaka District Public Prosecutors Office, Tsunehiko Maeda, was arrested September 21, 2010. He has been charged with falsifying evidence in a case against a former official of the Ministry of Health, Labor and Welfare. In Japan, with its 99 percent conviction rate, the scandal has led to further questioning of prosecutorial conduct. Japanese prosecutors have greater ability to lead police-like investigations than their counterparts in many other countries.

In Mr. Maeda's case, the Prosecutor's Office has charged that the ministry official improperly allowed groups to take advantage of postal discounts reserved for the disabled. A key piece of allegedly incriminating evidence was a disk which purported to show a falsified certificate. Mr. Maeda is charged with altering the time stamp on the disk to make it better fit the prosecution's timeline. The official in the underlying case was acquitted September 10, 2010, and the Osaka District Public Prosecutors Office chose not to appeal the acquittal. To make matters worse for the Prosecutors Office, the former Chief and Deputy Chief of the Special Investigation Squad were arrested for attempting to cover up the prosecutor's wrongdoing.

Upon taking over the position of Public Prosecutor General, Haruo Kasama stated at a press conference that it would be his mission to ensure that prosecutors follow the laws they are charged with upholding.

First Judgment on Product Liability Suit Against Manufacturer of Konjac Jelly: On November 17, 2010, the Kobe District Court, Himeji Branch, dismissed a claim under the Japanese Product Liability Act for damages against a manufacturer of konjac jelly.

Konjac jelly, also called konnyaku, is refined from konjac, a starchy root, and hardened chemically. The jelly is a popular ingredient in numerous Japanese foods, but owing to its chewy nature, it is a choke risk. Although there have been calls for regulation, this was the first ruling on the liability of a jelly manufacturer under Japanese product liability laws.

The parent of a 1-year-old baby who choked on the jelly sought damages of about 62 million yen (approximately $750,000). The court dismissed the claims, holding there was no design defect, defect in warnings, or inappropriate method of sale, and that the food had the requisite level of safety for its intended use. The parents have now appealed that ruling to the Osaka High Court.

Old Version of Bar Exam Abolished: The traditional version of the Japanese bar examination, which had been in use since 1949 and had achieved international attention for its level of difficulty, has been abolished.

Since 1999, Japan has sought to reform its judicial system to increase the number of legal professionals and encourage specialization. The reforms included the opening of law schools in Japan in 2006. Before the schools were opened, passing the bar exam was the only requirement for becoming an attorney. When the law schools were created, Japan introduced a new bar exam for law school graduates, administered side-by-side with traditional law school exam.

The pass rate on the traditional exam was very low, approximately 3 percent before 2005. Since 2006, when the new system was phased in, the newer exam has had pass rates of 25 percent to 48 percent. The Japanese government touted those higher rates to encourage prospective lawyers to enroll in law schools and take the new exam. It was too successful. The campaign to encourage enrollment in law schools resulted in a flood of students. The government has therefore capped the pass rate on the new examination meaning that once again there will be many failed attempts to become lawyers.

The traditional test has, however, been abolished. Only the persons who failed the oral aspect of the exam in 2010 are allowed to take it in 2011. As in the United States, individuals who wish to become attorneys will have to graduate from law school.

Entertainment Litigation Update

Leaking the Secrets of* Survivor*: "Outwit, outplay and outlast" is the tagline to the popular CBS reality series, *Survivor*. That phrase could apply equally to both the rabid online forum in which the show's fans attempt to "spoil" the plot twists and secrets of the show and to the show's producer, who has attempted to thwart the spoilers. In 2010, DJB Inc., a company owned by *Survivor* executive producer Mark Burnett, filed a federal suit against James Early for violating trade secret laws by disseminating online spoilers for *Survivor*'s 19th and 20th seasons.

California law defines a "trade secret" as information which "derives independent economic value, actual or potential, from not being generally known to the public or to other persons who can obtain economic value from its disclosure or use." *Cal. Civ. Code* § 3426.1(d). Typically, trade secret law has been used to protect company secrets that would be valuable to a competitor. Here, DJB has used trade secret law in a novel manner: it alleges that the production releases information to the public on a periodic basis, but that to protect the value of the business, information concerning what will be released must be kept secret until its scheduled release date.

DJB settled with Early. Although the terms are confidential, Early was reportedly willing to identify his source as Russell Hantz, a popular contestant on *Survivor*. Hantz could be subject to a liquidated damages clause in his *Survivor* cast member's contract of up to $5 million. Viewers of the show may get a sneak peak as Hantz is currently scheduled to be a team captain in the latest season of *Survivor,* which premieres in February 2011. If he departs the island with attorneys by his side, we will know how much the producers of *Survivor* value keeping the secrets of their show.

First Sale Doctrine Protects Distribution of Promotional CDs: UMG Recordings, like many music companies, ships specially produced promotional CDs to select individuals, such as music critics and disc jockeys, who do not solicit the CDs. In *UMG Recordings v. Augusto*, 628 F.3d 1175 (9th Cir. 2011), the Ninth Circuit affirmed summary judgment in favor of defendant Tony Augusto on UMG's claim of copyright infringement after he sold his copies of promotional CDs on eBay.

Augusto argued that the distribution of the CDs by UMG effected a transfer of ownership, rendering them subject to the first sale doctrine (17 U.S.C. § 109(a)), which allows the owner of a copy of a copyrighted work to sell it without permission from the copyright owner. UMG countered that it merely *licensed* the CDs because it included specific language on the CDs stating they were the property of the record company and were licensed to the recipient for personal use only. Although the district court found that UMG established a *prima facie* case of copyright infringement, it held that the first sale doctrine applied, allowing Augusto to sell the copies without authorization from UMG.

At issue on appeal was whether Augusto owned the copies notwithstanding the limiting language on the CDs. The Ninth Circuit determined that there had been a transfer of ownership, not a license, because the CDs were sent to the recipients without any prior agreement. The limiting language was not effective because, under basic contract law, the mere receipt of an unsolicited offer does not impair the recipient's freedom of action. Moreover, UMG had no control over the CDs following their initial distribution. Thus, Augusto owned the CDs and the first sale doctrine applied.

UMG Recordings is distinguishable from *Vernor v. Autodesk*, 621 F.3d 1102 (9th Cir. 2010), in which the Ninth Circuit recently considered the first sale doctrine in the context of software licensing. In *Vernor*, the court held that the first sale doctrine did not apply to a paying licensee of software if the vendor: "(1) specifies that the user is granted a license; (2) significantly restricts the user's ability to transfer the software; and (3) imposes notable use restrictions."

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Quinn Emanuel Wins Summary Judgment for Surety

Quinn Emanuel, acting with co-counsel, recently obtained summary judgment on behalf of American Home Assurance Co. against a plaintiff seeking to recover in excess of $30 million for remediation work allegedly performed for of the New Jersey Meadowlands. The New Jersey Chancery Court (Bergen County) ruled that the bond in issue was not a payment bond insuring the payments to contractors after the original landowner, which had contracted with the plaintiff for the work to be performed, failed to make payment. Instead, the bond was for the sole benefit of the entity overseeing the remediation work, which had conveyed the land in question to the owner. The court held that the owner, now bankrupt, was solely responsible for payment of the plaintiff-contractor.

Quinn Emanuel Wins Trial in Case Alleging that Malicious Conduct Contributed to Woman's Death

Quinn Emanuel obtained an exceptional victory following a bench trial in Los Angeles Superior Court on behalf of its clients, a bereaved family that lost a 24-year-old daughter owing to the negligent and malicious conduct of the defendant. The clients' daughter suffered an accidental drug overdose while in the company of the defendant and other acquaintances. The defendant, who was a convicted felon with a warrant out for his arrest, prevented those present from calling 911 and summoning medical aid because he feared police involvement. After being left unconscious and without medical treatment for more than eight hours, the young woman died. The defendant contributed to the young woman's death just two weeks after he had signed a written contract promising to cease all contact with her.

The young woman's family brought claims for wrongful death, false imprisonment, and breach of contract. The judge found for the plaintiffs on all claims, noting that the court was deeply troubled by the defendant's conduct and the course of events. The court also found that defendant acted with malice, justifying an award of punitive damages. The plaintiffs received the full amount of compensatory damages requested, totaling over $500,000, and the court will set a date to determine the appropriate punitive damages.

Quinn Emanuel Clears the Path for FairPoint Communications to Emerge from Chapter 11

In federal bankruptcy court in the Southern District of New York, the firm recently secured approval of a critical third-party injunction, clearing the way for FairPoint Communications, Inc. to emerge from chapter 11. After being spun-off from its parent, Verizon Communications, Inc., FairPoint entered bankruptcy in late 2009 with an unserviceable debt load in excess of $2.8 billion. In January 2011, FairPoint was set to emerge from bankruptcy with a restructured balance sheet negotiated by lead bankruptcy counsel, Paul, Hastings, Janofsky & Walker.

For the benefit of its creditors, FairPoint agreed to assign to a litigation trust certain claims against Verizon arising out of the spin-off transaction. But to protect reorganized FairPoint from any indemnification "claims over," FairPoint's plan included a third-party injunction that precluded Verizon from asserting any contribution or indemnification claims that could arise out of the assertion of the litigation trust claims against it. Verizon objected strenuously to this effective third-party release.

Controlling case law necessitated that FairPoint establish "truly unusual circumstances" making the injunction critical to the success of its reorganization. See *In re Metromedia Fiber Network, Inc.*, 416 F.3d 136 (2d Cir. 2005). Quinn Emanuel argued that without the injunction, FairPoint would not agree to the assignment of claims to the litigation trust, and without the assignment, the creditors would not support FairPoint's emergence from bankruptcy. The firm also illustrated the potential effect the to-be-enjoined claims could have on FairPoint's estate, thus establishing that the court could fairly exercise jurisdiction to enjoin such claims.

The court adopted Quinn Emanuel's argument, approved the injunction, and confirmed FairPoint's plan, finding that the protection was "essential to the debtors' reorganization and in the best interest of the estate." FairPoint's chapter 11 plan became effective January 24, 2011. Q

Maria Ginzburg Joins Quinn Emanuel's New York Office

Maria Ginzburg has joined the New York office as a partner. Maria is a versatile and seasoned trial lawyer with a wealth of experience in complex commercial disputes in the financial industry and related regulatory matters. She has extensive experience in civil cases involving structured products, accounting and underwriting practices, Ponzi schemes, fraudulent conveyance, consumer fraud, conflict of interest, and employment disputes. She regularly represents clients in investigations before the SEC, FINRA and the New York Attorney General that involve allegations of insider trading, short selling, PIPEs trading, and market timing.

Maria, formerly a partner in the New York office of Kirkland & Ellis, was attracted to Quinn Emanuel in part by our firm's leading position in the litigation of structured products disputes and other complex financial issues. She received her A.B. from Harvard College, *magna cum laude,* and received her J.D. from Stanford Law School, also with honors, where she was an Editor of the *Stanford Law Review*. Maria clerked for the Honorable Ralph K. Winter of the Second Circuit. Prior to attending law school, she was an investment banker at Merrill Lynch. Q

(Practice Area Updates continued from page 9)

Attorney Fee Awards: In Hollywood, it might serve future plaintiffs well to read the screenplay—and the jurisprudence of copyright law—before filing a copyright lawsuit. Just ask Sheri Gilbert.

In March 2009, Gilbert sued Warner Bros. and 33 other defendants for copyright infringement. *Gilbert v. New Line Productions, Inc.*, Case No. CV 09-02231 (C.D. Cal. 2010). Gilbert alleged that the studios, actors and others involved in the movie *Monster-in-Law* stole the idea for the film from a script she penned in 1998. She did not, however, read the screenplay for the movie to verify that it infringed anything she had written. She also apparently failed to read the long established case law holding that copyrights do not protect ideas, but only the expression of ideas. *See*, *e.g.*, *Mazer v. Stein*, 347 U.S. 201, 217 (1954). Nevertheless, Gilbert pressed forward with her suit, naming as defendants virtually everyone involved with *Monster-in-Law* and seeking a portion of the worldwide box office receipts.

It took two years, but the defendants prevailed on summary judgment. The district court then awarded the defendants almost $900,000 in attorneys' fees and costs under the Copyright Act of 1976, 17 U.S.C. § 505. The court considered a number of factors, including the degree of the defendants' success and the "frivolousness" of the claim. All factors weighed heavily against Gilbert, including that Gilbert's claims "were without merit" because "there was an absence of substantial similarity between [Gilbert's] work" and the film. The court found that Gilbert "and those similarly situated" should be deterred from filing frivolous claims.

The court's unequivocal ruling should serve as an admonition to future copyright plaintiffs in Hollywood: read the script, and the law, before you file suit. Q

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WL 3221821 (D. Md. Aug. 13, 2010).

Three other cases have recently applied the *Moench* presumption at the motion to dismiss stage, adopting analyses similar to that followed in *Bear Stearns*. See *In re Bank of America Corp Sec. Derivative and ERISA Litig.*, *In re SLM Corp ERISA Litig.*, 2010 WL 3910566 (S.D.N.Y. Sept. 24, 2010), and *In re American Express Cos. ERISA Litig.*, 2010 WL 4371434 (S.D.N.Y. Nov. 2, 2010).

In *Wright v. Medtronic*, 2011 WL 31501 (D. Minn. Jan. 5, 2011) (granting motion to dismiss), the court held that when alleging misrepresentations concerning company stock, an ERISA plaintiff must also allege actual reliance on the misrepresentation and that the misrepresentation caused the alleged loss. It held that under ERISA, there is no "fraud on the market" presumption of reliance similar to that allowed under the securities laws. See *id.* at *6.

Recent cases holding that public statements in SEC filings, press releases, and other public disclosures are not actionable as against plan fiduciaries include *Bear Stearns, Bank of America, Sallie Mae, Wright*, and *In re RH Donnelley ERISA Litig.*, 2011 WL 86623 (N.D. Ill. Jan. 10, 2011).

Although some recent decisions have not been as favorable to the defendants, it is fair to say that in general the judiciary has been increasingly protective of plan fiduciaries with respect to decisions to include company stock. Q

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business litigation report

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