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Predictive Coding Comes of Age

So-called "predictive coding"—using a small number of manually-coded documents to analyze and predict appropriate coding for a much larger set of documents—has become a hot topic in e-discovery. This past year brought the first reported judicial decisions explicitly authorizing the practice. 2012 also saw some of the first disputes concerning the appropriate methodologies for this technique.

In coming years, the use of predictive coding will continue to grow as litigants seek to limit discovery costs. Judges may also continue to endorse the practice, even incorporating it into model e-discovery orders. But early adopters should proceed with caution; the practice is likely to generate many disputes as acceptable methodologies and best practices are established.

The Evolution of Computer-Assisted Document Review

As companies have moved away from paper file systems and toward electronically stored information (ESI), the number of documents that must be collected and reviewed in civil litigation has skyrocketed. A number of technologies have been used to handle this explosion in discoverable information. Predictive coding is the latest technical evolution for reviewing and producing large data sets.

Manual Review: Not long ago, manual, linear, "eyes-on-the-page" analysis was the predominant method of document review. The process started with collecting documents that were potentially responsive to formal requests for production. The data collections, especially in complex civil litigation, often contained millions of pages. A small army of junior associates, contract attorneys, and even paralegals would then mobilize to manually review the documents for responsiveness, privilege, and confidentiality.

Although many still consider manual review to be the "gold standard," it is rife with performance

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Quinn Emanuel Adds More International Arbitration Stars

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Amy Candido, Diane Doolittle and Susan Estrich Recognized as "Top Women Lawyers"

Quinn Emanuel partners Amy Candido, Diane Doolittle and Susan Estrich have been named "Top Women Lawyers" by *The Daily Journal.* This list honored leading female attorneys in various practice areas whose accomplishments made a significant impact.

Intellectual property litigator Amy Candido was recognized for her work successfully defending Google Inc. in two patent jury trials in the Eastern District of Texas. Candido also represented HTC Corp. in a proceeding before the International Trade Commission in which HTC Corp. obtained a final determination of non-infringement and invalidity for several Apple Inc. patents.

Diane Doolittle, Co-Chair of Quinn Emanuel's National Trial Practice, was recognized for her successful representation of Southern California real estate developer Donald Bren in a jury trial against his children and their mother who accused Bren of cheating them out of child support payments. The jury verdict was recently affirmed by the California Court of Appeal.

Susan Estrich, Chair of the firm's Public Strategy Practice, legal and political analyst for Fox News, and Robert Kingsley Professor of Law and Political Science at the USC Gould School of Law, was selected for her trial and public communications strategy work on behalf of both TCW Group Inc. and Mattel Inc. Q

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and quality shortcomings. Analysts estimate that when operating at a maximum review speed of about 100 documents per hour, a decision on relevance, responsiveness, privilege, or confidentiality would need to be made in an average of 36 seconds. *See* Nicholas M. Pace and Laura Zakaras, *Where the Money Goes; Understanding Litigant Expenditures for Producing Electronic Discovery* (RAND Corporation 2012) (hereafter "Pace & Zakaras"). As a result, the document review in a large case could take thousands of man-hours. This significant expenditure of time and money does not come with a guarantee of accuracy; studies suggest that up to 95% of reviewer disagreement is the result of human error and not simply close questions of relevance. *See* Maura R. Grossman & Gordon v. Cormack, *Inconsistent Assessment of Responsiveness in E-Discovery: Difference of Opinion or Human Error?* 9 (ICAIL 2011 / DESI IV: Workshop on Setting Standards for Searching Elec. Stored Info. in Discovery, Research Paper).

***Keyword Search*:** Keyword searching is a rudimentary form of computer assistance that narrows the scope and number of documents for further manual review. In a typical keyword search, the producing party runs a set of keywords against emails and other electronic documents to identify a smaller set of documents to be manually reviewed for responsiveness. Typically, multiple keywords and Boolean relationships among them can be utilized. Keyword searching offers performance improvements over manual searching, and is highly common in modern e-discovery. Courts have explicitly endorsed the practice and have even incorporated keyword restrictions and search terms into model orders for e-discovery. *See, e.g.*, Federal Circuit's Model E-Discovery Order for Patent Cases, *available online at* www.cafc.uscourts.gov/images/stories/announcements/Ediscovery_Model_Order.pdf (proposing that email productions occur using "five search terms per custodian").

Yet keyword searching is also rife with shortcomings. Keyword searches are frequently overinclusive and underinclusive; search terms fail to capture many relevant documents, while simultaneously generating many false positives. When search terms turn out to be more common than expected in a document set, keyword searching will return a high number of documents that contain the keyword but have no possible relevance to the case—forcing the producing party to use expensive manual review to find truly relevant documents. A poorly chosen keyword often returns more "junk" than responsive documents. For that reason, great care must be taken by the producing party to identify appropriate keywords, often with the assistance of the document custodians themselves. Creativity must be employed to ensure that common synonyms, misspellings, acronyms, and abbreviations are included and keywords likely to generate false positives are excluded.

***Predictive Coding*:** Predictive coding is the latest evolution of computer-assisted document searching. As with manual and keyword searching, the process begins by collecting a corpus of potentially responsive documents from the client. Next, attorneys review a small set of randomly selected documents to identify a "seed set" of documents that are clearly fitting, or not fitting, the desired document categories. Then, the predictive coding software uses the "seed" documents to create a template to use when screening new documents. Some systems produce a simple yes/no, while others assign a score (for example, on a 0 to 100 basis) relating to responsiveness or privilege. Attorneys then audit the identified documents to validate their relevance, responsiveness, or privilege. The computer uses the attorneys' audit results to modify its search algorithm. The search algorithm is repeatedly audited and rerun until the system's predictions and the reviewer's audits sufficiently coincide. Typically, the senior lawyer (or team) needs to review only a few thousand documents to train the computer, at which point the system has learned enough to make confident predictions on a much larger data set—relevance of millions of documents.

Once a predictive model is generated, there are several ways the review might proceed. In the context of a review for relevance and responsiveness, one option might be to assume that all documents with scores above a particular threshold can be classified safely as responsive, while all those with scores below a particular threshold can be safely classified as not responsive. Only those documents with scores in the middle would require eyes-on review. Another option would be to perform eyes-on review of only those documents exceeding a particular score in order to confirm the application's decisions, while dropping the remainder from all further work. Foregoing all manual review altogether is also a possibility, though likely not advisable, given the potential for unexpected error. As these examples illustrate, the umbrella term "predictive coding" can be used to describe a number of different ways that predictions are used and applied. The individuals supervising the review must pick appropriate cut-off points and use their best judgment as to whether and how humans will review and refine codes that are automatically applied.

Used carefully, predictive coding has the potential to offer significant performance and cost benefits, without compromising accuracy. Litigants are already touting the cost-saving potential; some defendants have claimed predictive coding would reduce time for production and review from ten man-years to less than two man-weeks, and would cost roughly 1% of the cost of human review. *See Global Aerospace, Inc. v. Landow Aviation,* 2012 WL 1431215 (Cir. Ct. Loudoun Cty. Va. 2012). As to accuracy, predictive coding has not been shown to be any less accurate than traditional manual review. (Pace & Zakaras, pp. 61-66.) Some studies suggest that predictive coding identifies at least as many documents of interest as traditional eyes-on review, with about the same level of inconsistency, and may in fact offer more accurate review for responsiveness than most manual reviews. (Pace & Zakaras, p. xviii) Actual cost savings will depend on a number of factors, including the size of the document set, challenges to the predictive coding methodology, and the document review methodology against which predictive coding is compared—but used in the right circumstances, the cost-saving potential of predictive coding is obvious.

Recent Decisions

While keyword searching has been the most frequently used choice of computer-assisted document review and searching, a small handful of recent cases have considered the use of predictive coding. As courts become more familiar with the practice, some are explicitly endorsing and recommending the practice.

Global Aerospace may be the first case actually ordering the use of predictive coding. *Global Aerospace, Inc. v. Landow Aviation,* 2012 WL 1431215 (Cir. Ct. Loudoun Cty. Va. 2012). The defendants argued that, with more than 2 million documents to review, it would take reviewers more than 20,000 hours to perform the task—10 man-years of billable time. 2012 *Global Aerospace, Inc. v. Landow Aviation*, 2012 WL 1419842 (Va. Cir. Ct. April 9, 2012). But with predictive coding, it would take less than two weeks at a cost of roughly 1/100 that of manual, human-review. *Id.* Having heard arguments, the Court ordered that Defendants could proceed with the use of predictive coding for processing and production of ESI. *Global Aerospace, Inc. v. Landow Aviation,* 2012 WL 1431215 (Va. Cir. Ct. April 23, 2012).

Global Aerospace stopped short of an unqualified approval of predictive coding. For example, predictive coding cannot work effectively if a representative corpus is not used for the initial training. The *Global Aerospace* court noted that the receiving party was free to challenge the completeness of the contents of the production and the manner in which predictive coding was used for new documents. *Id.*

In *Moore v. Publicis*, perhaps the most significant judicial decision on predictive coding to date, the Southern District of New York (Magistrate Judge Peck) held that "computer-assisted review is an acceptable way to search for relevant ESI in appropriate cases." *Moore v. Publicis Groupe*, 2012 U.S. Dist. LEXIS 23350, 2012 WL 607412 (S.D.N.Y. 2012). The Court reasoned that computer-assisted review complied with the doctrine of proportionality of Federal Rule of Civil Procedure 26(b)(2)(C), and that predictive coding was an acceptable form of computer-assisted review. *Id.* at *12 ("…computer-assisted review is an available tool and should be seriously considered for use in large-data-volume cases where it may save the producing party (or both parties) significant amounts of legal fees in document review.")

As courts have endorsed the voluntary use of predictive coding, parties have also sought to compel their adversaries to use the technique. In *Kleen Products*, Defendants sought to use keyword search-term processing, in which they had already invested much time and effort; but Plaintiffs moved to compel the use of predictive coding, arguing that keyword search methods were inadequate and flawed. *Kleen Products, LLC v. Packaging Corp. of America*, No. 10-C5711, Dkt. 412 (N.D. Ill. Sept. 28, 2012). The Court held evidentiary hearings in February and March 2012, during which it urged the parties to reach a compromise—for example, adopting Defendants' keyword-based approach, but refining or supplementing terms and review procedures to meet Plaintiffs' concerns. Ultimately, the parties reached agreement before a ruling on the motion to compel was reached. But *Kleen* illustrates that disputes over keyword search-terms may extend far beyond the sufficiency of specific terms going forward. Parties may challenge the notion of keyword searching itself—perhaps using the availability of predictive coding as leverage to obtain significant concessions on proposed keywords.

A recent case management order in *In re: Actos* provides further insight into the predictive coding processes that parties are likely to agree to and courts to sanction. *In re: Actos (Pioglitazone) Products Liability Litigation*, MDL No. 6:11-md-2299, Dkt. 1539 (W.D. La. July 27, 2012). The agreed-upon order in *Actos* allows each side to nominate three reviewers to work collaboratively to code the seed set of documents. The extremely detailed protocol contains numerous levels of sampling and review, as well as meet-and-confer check points throughout the procedure, including regarding the relevance threshold that would trigger manual review by the producing party.

Predictive Coding Done with Care

Litigants interested in utilizing predictive coding should keep several principles from these cases in mind. First and foremost, the producing party should attempt to gain the receiving party's consent to use of predictive coding. The greater transparency offered into the procedure, the less likely that the receiving party will successfully move to compel an alternative document production methodology later in the case. An agreement regarding the basic methodology and the custodians from whom documents will be collected is recommended. Moreover, using jointly-appointed reviewers for the document training set may ease concerns with the process.

Second, the producing party should negotiate a "claw-back provision" that will allow recovery of documents that are improperly produced as a result of the predictive coding methodology. These could include documents that are irrelevant, privileged, or that should be, but were not, marked as confidential under a protective order. Such a provision is especially important if any portion of the documents marked responsive by the predictive coding methodology will not be manually reviewed.

Third, great care should be taken in preparing the initial "seed set" of documents that will be used to program the predictive coding algorithm. If the producing party does not actually involve the receiving party in the selection of the seed set, the producing party should be prepared to disclose the entire seed set to the receiving party and the court, which may raise work-product protection concerns. It is also important that the persons reviewing the initial seed set have a strong grasp of the issues in the case. Because of the importance of the initial seed set, it is critical that persons reviewing the seed set make accurate decisions; any errors in the seed set will become systemic throughout the larger review.

Fourth, the producing party should consider whether it is appropriate to use different seed sets for different custodians. For example, in a patent case, responsive documents that are held by an engineer may look very different than responsive documents held by an employee in the marketing or finance departments.

Fifth, the producing party should work closely with its e-vendor to ensure that the methodology is statistically justifiable. This includes ensuring that the documents from which the seed set is drawn is random, that the seed set is sufficiently large, and that the confidence interval and confidence level are either agreed upon between the parties or statistically justifiable.

Potential Stumbling Blocks and Pitfalls of Predictive Coding

Litigants planning to use predictive coding should be aware of potential pitfalls that could render the practice either more costly or inappropriate than manual review or keyword-driven review. For example, predictive coding may be inappropriate in a case that does not involve a sufficiently large body of documents. If the receiving party is dissatisfied with the results of the predictive coding, the producing party may face a motion to compel a more traditional document review methodology—thereby eliminating any cost savings. The danger of such a motion is especially high now, when predictive coding is in its earliest stages and best practices have not yet been developed. Where the corpus of documents contains highly sensitive information, a full manual review of any documents automatically selected for production may also be required to reduce the likelihood of damaging disclosure. This may entail significantly greater expense than keyword-driven reviews. Finally, predictive coding is not presently suitable for files that are not primarily text-based, such as video or audio files, necessitating the continued manual review of those materials.

Conclusion

As the amount of electronically stored information held by companies continues to grow at an exponential pace, widespread dissatisfaction with traditional manual and keyword review will likely lead to even greater use of predictive coding in 2013. This transition will offer cost savings for some, and headaches for others. As predictive coding grows, so too will litigation concerning predictive coding's appropriate use and methodology. But the potential for significant cost savings is undeniable for large-scale reviews. Cost-conscious litigants in document-intensive cases would be wise to consider predictive coding as one tool to reign in growing e-discovery costs. Q

Copyright Litigation Update

***European Court Holds Computer Programming Languages and Functionality Unprotectable*:** The European Court of Justice in Luxembourg recently held in *SAS Institute Inc. v. World Programming Ltd.*, No. C-406/10 (May 2, 2012) that under the laws of the European Union, the functionality of computer programs and computer programming languages is not subject to copyright protection. SAS developed a scripting language and application for its Base SAS database program to extract data. Using commercially available SAS products, the defendant developed software capable of running scripts written in that language. The Court of Justice held that this was not copyright infringement: the European software copyright directive excludes from protection "ideas and principles which underlie any element of a computer program, including those which underlie its interfaces," and Defendant's effort to replicate the functionality of a computer program or the use of a programming language, did not infringe a form of protected expression.

This decision has received international attention, reflecting widespread desire for harmonization of copyright laws for protection of computer software. For example, in *Oracle America, Inc. v. Google Inc.*, No. C 10-03561 WHA (N.D. Cal. May 31, 2012), the Northern District of California asked the parties to brief the European Court of Justice's *SAS Institute* decision before ruling that the structure, sequence and organization of a Java Application Programming Interface ("API") were not subject to copyright protection. After Oracle acquired Sun Microsystems, which owned Java-related copyrights and patents, Oracle sued Google alleging patent and copyright infringement by the Android platform. In ruling for Google, Judge Alsup held that as long as "the specific code used to implement a method is different, anyone is free under the Copyright Act to write his or her own code to carry out exactly the same function or specification of any methods used in the Java API." Further, it was irrelevant that Google had not chosen to use different method header lines and class names: "copyright protection never extends to names or short phrases as a matter of law." Finally, the Court expressed its view that when the principles underlying patent law and copyright law clash, the patent laws should prevail; thus, even if the structure, sequence and organization of the API were the product of creative endeavor—and arguably entitled to copyright protection—providing copyright protection to these allegedly patented APIs would defeat the 20-year limitation on patent claims.

Bankruptcy Litigation Update

***Jefferson County Section 928 Decision*:** In a matter of first impression and potential importance in the municipal bond market, the Bankruptcy Court for the Northern District of Alabama held in *Bank of New York Mellon v. Jefferson County, Alabama*, 474 B.R. 725, 763-64 (Bankr. N.D. Ala. 2012), that where a trust indenture provides sufficient funding for operating expenses, the "minimal standard" of "necessary operating expenses" imposed by Bankruptcy Code section 928(b) is inapplicable. Section 928(b) provides that "[a]ny [ ] lien on special revenues, other than municipal betterment assessments, derived from a project or system shall be subject to the necessary operating expenses of such project or system, as the case may be." 11 U.S.C. § 928(b). The Bankruptcy Court rejected Jefferson County's contention that section 928(b) overrode the provisions of the parties' trust indenture and permitted it to characterize depreciation, amortization, capital expenditures, reserves for any of the same, or reserves for professional fees and expenses, as operating expenses that it could deduct prior to funding debt service. The Bankruptcy Court agreed with the plaintiffs that "a pledge of special revenues [is] unaffected unless it is at odds with the policies incorporated in 928." *Id.* at 756. It found that "unbridled inclusion of costs that under generally accepted accounting principles are capitalized, whether in the context of a gross revenue or a net revenue pledge, is capable of undoing what the 1988 Amendments were designed to [achieve]," i.e., the post-petition preservation of special revenue liens, protecting the benefits of parties' bargains, and ensuring continued municipal access to capital markets. *Id.* at 760-61. Finally, the Bankruptcy Court concluded that the parties' "mutual exercise of business judgment ... incorporated into a special revenue financing transaction [ ] should not be second guessed in a municipal bankruptcy absent clear evidence of an unreasonable exercise or that it is a certainty that 928(b) is not met. In other words, for pledges that are not gross revenues, a court should defer to the agreed pledge and distributive design representing the business judgments of the parties that is expressed in the contract between them." *Id.* at 763.

***CIT Section 510(b) Decision*:** The Second Circuit recently held that mandatory subordination under section 510(b) of the Bankruptcy Code must be interpreted narrowly in accordance with its underlying purpose. *In re CIT Group Inc.*, 2012 WL 3854887, at *2 (2d Cir. Sept. 6, 2012). The underlying Bankruptcy Court (*In re CIT Group Inc.*, 460 B.R. 633 (Bankr. S.D.N.Y. 2011)) had clarified the scope of section

510(b), which requires the subordination of a claim "arising from rescission of a purchase or sale of a security of the debtor or of an affiliate of the debtor, [or] for damages arising from the purchase or sale of such a security . . . ." The debtor and its former parent, in connection with the debtor's pre-petition initial public offering, had entered into a tax sharing agreement whereby the debtor agreed to pay its former parent any tax benefits resulting from the debtor's use of certain net operating losses (the "NOLs"). The Bankruptcy Court rejected the debtor's attempt to subordinate the former parent's claim, which arose from the debtor's rejection of the tax sharing agreement, concluding that Congress had enacted section 510(b) to prevent equity claims in bankruptcy from being disguised as higher-priority creditor claims. The court reasoned that subordination is appropriate only if the claimant "'(1) took on the risk and return expectations of a shareholder, rather than a creditor, or (2) seeks to recover a contribution to the equity pool presumably relied upon by creditors in deciding whether to extend credit to the debtor.'" *Id.* at 638 (citation omitted). Tax sharing agreements generally create only contractual debtor-creditor relationships. Even though the debtor's ability to use the NOLs depends upon its future revenues, the former parent does not have an interest in the debtor's future equity value, and thus has no expectation of sharing in the debtor's profits without limitation. Thus, the court concluded, and the Second Circuit has now affirmed, subordination is not warranted.

***Sentinel Fraudulent Transfer Decision*:** In *In re Sentinel Management Group*, the Seventh Circuit affirmed that a debtor's repayment of debt owed to creditors with funds taken from the debtor's own customers' accounts was not made with an intent to hinder, delay, or defraud the customers (who became creditors of the debtor by virtue of this comingling of funds) and thus was not an intentional fraudulent conveyance under section 548(a)(1)(A) of the Bankruptcy Code. 689 F.3d 855, 861-64 (7th Cir. 2012). The Sentinel Court explained that "fraudulent conveyance law exists for very different purposes that does not include attempts to choose among creditors as contrasted with restitution and preferences." *Id.* at 862-63. Based on this principle, the Court held that the debtor's "preference of one of set of creditors . . . to another . . . is properly reserved for [the plaintiff]'s preferential transfer claims[.]" *Id*. at 863. The Court further stated that "a debtor's 'genuine belief that' he could repay all his debts if only he could 'weather a financial storm' won't 'clothe him with a privilege to build up obstructions' against his creditors . . . but that does not mean that actions taken to survive a financial storm require a legal finding that the debtor intended to hinder, delay, or defraud[.]" *Id.* (quoting *Shapiro v. Wilgus*, 287 U.S. 348, 354 (1932)).

Class Action Litigation Update

***Defending False Advertising Claims*:** If you thought a false advertising lawsuit based on ads that cats "like" or "choose" one brand of kitty litter over another was going too far, you were not alone. Judge Samuel Conti of the Northern District of California recently dismissed that aspect of a class action against Clorox, pointing out what seems perfectly obvious: that no reasonable consumer could be deceived by depictions of cats appearing to "choose" one litter box over another and that such statements are "puffery." *See In re Clorox Consumer Litigation*, 12-00280, 2012 WL 3642263 (N. D. Cal. Aug. 24, 2012). It is still safe to show our furry friends engaging in human-like behavior without fear of being sued by someone who thinks it should be taken literally.

The *Clorox* case, which moves forward on other claims, is one of the scores of new false advertising lawsuits that have become the suit *du jour* in the class action world. Every label, print, internet, and TV ad is being carefully scrutinized for any transgression from 100% accuracy, no matter how obvious it is that the license taken with a claim is poetic. Even where the plaintiffs concede product ingredient levels and nutritional information are accurately disclosed on the label, they have still launched class actions—and gotten past the pleading stage—by contending consumers should not be expected to read labels provided for their benefit. Indeed, because consumer protection claims are broad in their coverage and claims of violations are fact-intensive, it is difficult to dismiss even seemingly frivolous cases with an early motion. But there are defenses that have had some measure of success and merit considering in the proper case.

First, if the claim is pled generally in a Federal Court complaint, it may be possible to argue it should be considered a fraud claim, subject to Fed. R. Civ. P. 9(b), requiring plaintiff to plead the "who, what, when, where, and how" of the charged misconduct. Federal Courts have required state-law consumer claims to be pled with particularity, including the commonly-asserted trio in California of the Unfair Competition Law (UCL), the Consumer Legal Remedies Act (CLRA), and the False Advertising Law (FAL). *See Yumul v. Smart Balance, Inc.*, 733 F. Supp. 2d 1117, 1122 (C.D. Cal. 2010). This rule will rarely lead to dismissal with prejudice, but it is always worthwhile to know from the start what specific facts plaintiffs believe support their claim.

Second, and potentially more powerful, is a preemption defense, particularly for claims involving federally-regulated labels. This could include FDA-regulated packaging for foods and nonalcoholic beverages, *see, e.g.*, *Chacanaca v. Quaker Oats Co.*, 752 F. Supp. 2d 1111, 1116 (N.D. Cal. 2010), as well as USDA-regulated labeling of meat, poultry, and liquid egg products. For example, The 2012 Nutrition Labeling and Educational Act ("NLEA"), 104 Stat. 2353, 21 U.S.C. §§ 341, et. seq. (2012), requires certain nutritional and ingredient information to be disclosed on the labels of nearly all FDA-regulated food items. *Peviani v. Hostess Brands, Inc.*, 750 F. Supp. 2d 1111, 1118 (C.D. Cal. 2010). The Act expressly prohibits States from imposing "any requirement respecting any claim of the type described in section 343(r)(l) of this title made in the label or labeling of food that is not identical to the requirement of Section 343(r) of this title." 21 U.S.C. §§ 343-1(a); *see also Yumul v. Smart Balance, Inc.*, No. 10-00927, 2011 WL 1045555 (C.D. Cal. Mar. 14, 2011) (finding more restrictive "no cholesterol" labels required by California law preempted by the NLEA); *Chacanaca*, 752 F. Supp. 2d at 1116-17 (finding consumers' action to prohibit "0 grams trans fat" labeling preempted by NLEA).

In California, in particular, many UCL/FAL/CLRA claims against food and drink manufacturers have been held preempted by federal labeling requirements under the NLEA when plaintiffs seek to impose a burden on food manufacturers that is not identical to what the NLEA requires. *See Charles Hairston v. South Beach Beverage Co., Inc.*, No. 12-1429, 2012 WL 1893818 (C.D. Cal. May 18, 2012) (finding preemption of claim that it was improper to refer to fruits in describing flavors when beverage did not contain actual fruit or fruit juice).

Identifying specific provisions of the NLEA or FDA rules will increase the odds of succeeding on a preemption defense. For instance, in *Lam v. General Mills, Inc.*, No. 11-5056, 2012 WL 1656731 (N.D. Cal. May 10, 2012), plaintiffs argued that packaging of Fruit Roll-Ups misled consumers into thinking they were healthy. The packaging contained statements such as "fruit flavored snack" and "strawberry natural flavored," although the side panel had an accurate list of ingredients. Defendants presented a specific rule that permitted a producer to label a product as "natural strawberry flavored" even if that product contained no strawberries. The District Court held the claim was preempted. *See also Carrea v. Dreyer's Grand Ice Cream, Inc.*¸ 475 F. App'x 113 (9th Cir. Apr. 5, 2012) (claim "0g Trans Fat" statement on drumstick's packaging misled consumers into believing Dreyer's ice cream was healthy were preempted by NELA rules on nutritional labeling).

Despite these cases, there is little help for claims against an advertiser who contends that a product is "all natural." The FDA has not defined what is "natural," and as a result, such claims are not preempted. *See e.g.*, *Wright v. Gen. Mills, Inc.*, No. 08-cv-1532, 2009 WL 3247148 (S.D. Cal. Sept. 30, 2009) (rejecting preemption defense to an assertion that a granola bar containing high fructose corn syrup is misleadingly labeled "all natural"); *Astiana v. Ben & Jerry's Homemade, Inc.*, No. 10-4387, 2011 WL 2111796 (N.D. Cal. May 26, 2011) (claim that ice cream containing alkalized cocoa was improperly labeled "all natural" not preempted).

If pleading defenses fail and a class is certified, under most consumer protection statutes, the challenged advertising claim will be judged from the perspective of the "reasonable consumer." Even where common sense compels success under this standard, the litigation costs required to obtain that result in a class action can be significant. Whether courts like the *Clorox* court will become more active in shutting down suits that defy common sense at the pleadings stage remains unclear.

Appellate Litigation Update

***Quinn Emanuel Opens Supreme Court's October 2012 Term*:** On Monday, October 1, 2012, the Supreme Court reconvened for its first oral arguments after the summer recess. Quinn Emanuel's Kathleen Sullivan argued in the very first case of the new Term, *Kiobel v. Royal Dutch Petroleum Co.*, No. 10-1491, on behalf of the respondents, the Dutch and English corporations Royal Dutch Petroleum Company and Shell Transport and Trading Company (collectively, "Shell"). This is the second time the case was argued, after the Court took the unusual step of ordering re-argument after Shell's argument last Term.

At issue is the scope of the Alien Tort Statute ("ATS"), 28 U.S.C. § 1350, which the First Congress enacted in 1789. The Act was motivated by concern that international law violations, like assaults on foreign ambassadors on U.S. soil, required redress in the nation's nascent Federal Courts lest State-Court indifference to such violations lead to international conflict. The ATS accordingly provides: "The district courts shall have original jurisdiction of any civil action by an alien for a tort only, committed in violation of the law of nations or a treaty of the United States."

The ATS was rarely invoked until 1980, when the U.S. Court of Appeals for the Second Circuit gave it new life in *Filartiga v. Pena-Irala*, 630 F.2d 876 (2d

Cir. 1980). Filartiga allowed an ATS suit alleging that a former Paraguayan government official had tortured the plaintiff in Paraguay in violation of international human rights norms. Filartiga opened the door to numerous other ATS cases for conduct on foreign soil—including many naming corporations as defendants.

In 2004, in *Sosa v. Alvarez-Machain*, 542 U.S. 692 (2004), the Supreme Court kept the door open for such ATS actions, if only just ajar. Sosa held that, while the ATS provides only jurisdiction, federal common law provides a cause of action for offenses against the law of nations so long as they have no "less definite content and acceptance among civilized nations than the historical paradigms familiar when [the ATS] was enacted"—namely, violation of safe conducts, infringement of the rights of ambassadors, and piracy. *Id.* at 732. Sosa imposed a second screen on ATS actions as well, requiring that Federal Courts exercise their "judgment about the practical consequences of making [a new ATS] cause available to litigants in the federal courts." *Id.* at 732-33.

Kiobel raises the question whether an ATS suit may proceed against a foreign corporation for alleged conduct aiding and abetting a foreign government on foreign soil. It involves a suit by Nigerian citizens alleging that Shell aided and abetted human rights violations in Nigeria by a prior Nigerian government. In 2010, the Second Circuit, in a divided opinion, held that international law does not recognize liability for corporations (as opposed to natural persons) for the violations alleged, and thus dismissed the case. The Supreme Court granted review in October 2011, and Shell retained Quinn Emanuel to represent it in the Court.

The Court granted review on the question whether international law holds a corporation (as opposed to a natural person) responsible for the violations alleged. Shell argued that it does not, but also argued, in the alternative, that the ATS and federal common law do not apply at all to conduct within the territory of a foreign sovereign. During oral argument on February 28, 2012, several Justices posed questions concerning that extraterritoriality issue, asking what the case had to do with the United States. The following week, the Court issued an unusual order asking the parties to prepare briefs on that issue over the summer and setting the case for re-argument this Term.

Kiobel in its two rounds has attracted over 85 amicus briefs from the U.S. and international business communities, human rights organizations, and governments, including the United States, which argued on the first Monday in October, in support of Shell, that the ATS cannot apply to a "foreign-cubed" action involving foreign conduct by a foreign corporation alleged to have aided and abetted a foreign government. Numerous other corporations and groups filed amicus briefs agreeing with Shell that the ATS equally cannot apply to "foreign-squared" actions against U.S. corporations alleged to have aided and abetted foreign government conduct on foreign soil. A decision is expected by June 2013.

London Litigation Update

***State Immunity*:** In *SerVaas Incorporated v. Rafidain Bank and others [2012] 3 WLR 545*, the UK Supreme Court considered the scope of a state's immunity from execution of a judgment and provided helpful guidance in relation to the "commercial purpose" exception provided for in section 13(4) of the State Immunity Act 1978 ("the Act").

SerVaas sought enforcement of a judgment by applying for a Third Party Debt Order in relation to dividends payable to Iraq by Rafidain under a Scheme of Arrangement. Iraq resisted this on the grounds that the money due to the state was immune from execution by virtue of section 13(4) of the Act as the funds were not property "for the time being in use or intended for use for commercial purposes". The application was dismissed at first instance and an appeal by SerVaas was also dismissed by the Court of Appeal. Undeterred, SerVaas then mounted a further appeal to the Supreme Court.

The Supreme Court unanimously dismissed the appeal and confirmed that the nature of the property against which execution was sought was irrelevant to the "commercial purpose" analysis. Parliament did not intend a retrospective analysis of all the circumstances which gave rise to the property, but an assessment of the use to which the state had chosen to put the property. Unhelpfully for SerVaas, a certificate was signed by the Iraqi Ambassador in London stating the dividend payments would not be used for any commercial purpose. The Supreme Court noted that this certificate created a presumption that SerVaas had no real prospect of rebutting.

This decision demonstrates the considerable limitations of the "commercial purpose" exception. This development may create challenges in enforcing judgments against states in the United Kingdom and, therefore, any party contracting with a state should carefully consider insisting upon an express waiver of immunity from execution when drafting contractual dispute resolution clauses.

***Determining a Debtor's COMI*:** Should a German national (B) who owed a German Bank (the Bank) more than €3 million be allowed to take advantage of England's debtor-friendly bankruptcy regime to erase his liabilities to the bank? This was what the Court had to decide in *Sparkasse Hilden Ratingen Velbert v. Benk and another* [2012] EWHC 2432. B, who had been declared bankrupt in England, owed the Bank more than €3 million. The bankruptcy had run its course and B had been discharged, erasing his liabilities to the Bank. The Bank argued that the English Court should not have made the bankruptcy order because B's COMI had been in Germany at all relevant times and that his presence in England was only temporary. For the Bank to succeed, they had to establish that B's COMI was not in England at the time the petition was presented.

The Court held that B's COMI was in Germany at the time the second petition was presented and when the bankruptcy order was made. It found that B was habitually resident in Germany but only lived in England temporarily. Habitual residence did not require presence at any particular time, only habit: B's professional domicile was in Germany. B was a notary in Germany at all material times and even though he was suspended from practice at the time of the second petition, he had lodged numerous appeals in Germany to resume his practice. This Court found that this showed B's motive to resume professional activities in Germany once discharged and his purported job in England as a professional sports photographer was mere "window dressing". The Court also found that B's only economic activity since relocating to England (i.e. the appeals he had lodged to revive his notary practice) took place in Germany which also pointed to a German COMI. B's partner, E, on whom he was dependent, financed B through her German bank accounts and maintained a German residence despite B's tenancy agreement in Birmingham, England being in their joint names. E's residence was deemed to be in Germany, and the Court found that the mutual emotional dependence of B and E as a couple made it unrealistic that they would have separate COMIs.

Most of B's creditors were also located in Germany and B had not taken steps to inform them of his change in COMI. The Court held that even though the creditors would have known of his change of COMI by way of an earlier unsuccessful bankruptcy petition, this was insufficient to establish a change in COMI. The Court noted that a debtor should not normally need to notify his creditors of a change in COMI, but he should not hide his COMI from them either. B's subjective intent was also a factor in the Court's decision. The judge found that his evidence as a witness pointed to his presence in England as a short-term arrangement. B's ultimate objective was to return to Germany free of his debt and resume his practice as a notary. Lastly, the fact that he had been untruthful in the past and openly used a company which advertised services aimed at helping German debtors relocate to England to work around German bankruptcy law, showed that he had made no real effort to settle in England.

Countries such as Ireland and Germany have much stricter bankruptcy laws than England, and debtors often try to establish England as their COMI to take advantage of the more relaxed laws there. While this decision does not affect the requirements for the establishment of COMI, it certainly shows the English Court's sympathy for the anti-forum-shopping arguments which creditors frequently raise against their debtors when seeking to set aside English Bankruptcy petitions.

Causation in Financial Services Cases**:** Section 150 of the UK's Financial Services and Markets Act creates a cause of action for private persons who have suffered loss as a result of a financial institution's breach of a rule contained in the FSA's Conduct of Business Sourcebook (COBS). Case law (e.g. *Camerata v. Credit Suisse* [2012] PNLR 15) had suggested that where a breach of COBS led a Claimant to make an investment they would not have made but for the breach, but Claimant went on to suffer loss as a result of unforeseeable market events (e.g. the collapse of Lehman Bros), then such loss was not recoverable under section 150. In *Rubenstein v. HSBC* [2012] EWCA 1184, the Court of Appeal departed from that principle. Rix LJ held that *"It was the bank's duty to protect Mr Rubenstein from exposure to market forces when he made clear that he wanted an investment which was without any risk (and when the bank told him that his investment was the same as a cash deposit)... [A] bank must reasonably contemplate that, if it misleads its client as to the nature of its recommended investment, and thereby puts its client into an investment which is unsuitable for him, when it could just as easily have recommended something more suitable which would have avoided the loss in question, then it may well be liable for that loss."* This approach recognizes that the tort created by section 150 is intended to protect investors, and that questions of causation and foreseeability must be understood in that context. This is a welcome development in an area of the law where English claimants have historically faced severe challenges in holding financial institutions to account for their wrongdoing.

Victory for Vermillion Inc. and Bio-Rad in High-Stakes Arbitration

The firm recently obtained an arbitration victory for its clients Vermillion, Inc. (f/k/a Ciphergen Biosystems, Inc.) and Bio-Rad Laboratories, Inc. The case, originally filed in Santa Clara County Superior Court, involved surface enhanced laser desorption ionization ("SELDI") technology—a protein separation and characterization technology with potential applications in the fields of proteomics, drug discovery, diagnostics, and disease treatment. The case was heard by a single arbitrator at JAMS after QE successfully convinced a panel of the California Court of Appeal, Sixth District, to reverse the Superior Court's denial of Vermillion's and Bio-Rad's petition to compel arbitration.

Vermillion recently launched its first diagnostic product, OVA1 (the first blood test to evaluate ovarian masses for malignancies prior to surgery). The plaintiff sought compensatory damages, punitive damages, and injunctive relief. After a five-day trial, the Arbitrator found in favor of Bio-Rad on all causes of action alleged against it (i.e., no liability). The Arbitrator also found in favor of Vermillion on all causes of action alleged against it (i.e., no liability), with the exception that the Arbitrator found that Vermillion should provide a verification that its past royalty payments to the plaintiff had been correctly calculated. As a result of these rulings and pre-trial Section 998 offers, the plaintiff agreed to a Settlement and Consent Judgment in favor of Defendants, in which the plaintiff agreed not seek to vacate the Arbitration Award or otherwise exercise any right to appeal, and further agreed to relieve Vermillion of its contractual obligation to pay royalties on its future revenues.

Victory for Broadcom Founder

The firm recently won a wrongful termination trial brought against our client The Management Company ("TMC"), an organizational entity that provided various services to Dr. Henry T. Nicholas, III, the founder of the Broadcom Corporation.

Following her termination in June 2008, Plaintiff, Dr. Nicholas's former senior executive assistant, brought a number of employment-related claims against TMC and Dr. Nicholas. Through motions practice, Dr. Nicholas was quickly dismissed from the lawsuit, as were the majority of claims against TMC. In March 2010, Quinn Emanuel tried the surviving two claims against TMC: wrongful termination and failure to pay overtime compensation. We obtained a complete defense verdict on both counts.

Plaintiff appealed both verdicts. Although the judgment on the overtime claim was upheld on appeal, the California Court of Appeal reversed the judgment on the wrongful termination claim. In that claim, Plaintiff alleged that she was tortiously terminated in violation of public policy in retaliation for testifying before a federal grand jury and for cooperating with the FBI in an investigation of Dr. Nicholas.

On retrial, the parties waived a jury and tried the wrongful termination claim to the Court. After presenting ten witnesses over five days of trial Plaintiff rested her case and Dr. Nicholas moved for judgment. The Court allowed Plaintiff to present additional evidence in response to our motion and then invited the parties to make arguments on whether the evidence supported a defense verdict.

Quinn Emanuel successfully persuaded the Court that Plaintiff's termination had nothing to do with her grand jury appearance or her communications with the FBI. We demonstrated that Plaintiff's tales of retaliation were not credible by highlighting significant falsehoods and inconsistencies in Plaintiff's testimony. We also established that Plaintiff was lawfully terminated from her position as senior executive assistant with TMC for refusing to report to work. In ruling for our client, the Court ultimately found that Plaintiff's termination was in no way motivated by her grand jury testimony or cooperation with the federal investigation.

Important International Arbitration Victory for DP World

The firm recently achieved a significant victory through a favorable settlement for client Dubai Ports World ("DPW") in a dispute involving an investment treaty arbitration and two contract arbitrations with the Republic of Yemen and the state-owned Yemen Gulf of Aden Ports Corporation ("YGAPC"). The U.A.E.-based port operator entered into a joint venture with YGAPC and concluded a series of agreements to develop, manage and operate two container terminals in Aden, Yemen. Various disputes arose between the parties in relation to their port agreements and Yemen's obligations to DPW pursuant to the bilateral investment treaty between the Republic of Yemen and the U.A.E. ("Yemen/U.A.E. BIT"). Quinn Emanuel assisted DPW with developing its contract and treaty claims against Yemen and YGAPC, and then negotiated an optimal settlement whereby the world-class port operator divested its entire ownership interests in the troubled venture and recouped a lump sum payment of approximately eighty percent of the value of its claims.

To achieve this result, Quinn Emanuel's international arbitration team, working seamlessly across multiple time zones, employed a winning strategy that took the offensive and put the Republic of Yemen on notice of its violations to DPW under the Yemen/U.A.E. BIT. Our team also fashioned compelling arguments and counterclaims when Yemen responded to the BIT dispute notice by terminating the project agreements and threatening to file two separate contract arbitrations pursuant to LCIA and UNCITRAL rules.

The parties agreed to a global settlement of all claims under the BIT and project agreements. Under the settlement agreement, DPW also ceased its management of Aden Container Terminal on September 20th, 2012, when the Aden Port Development Company, a wholly owned subsidiary of YGAPC, took full responsibility of the port's operations.

The global settlement was seen favorably by both parties. YGAPC stated that it was "pleased" to have reached the agreement on an amicable basis and that the agreement "protects the interests of the Republic of Yemen and YGAPC and secures the future for this strategically located terminal." DPW observed that it was "very satisfied" with the agreement and that its "investment in the Aden facility was recognized by [its] joint venture partner, YGAPC, through the agreement reached[.]" Q

Quinn Emanuel Adds More International Arbitration Stars

Quinn Emanuel is pleased to announce that Anthony Sinclair, formerly a partner in the London office of Allen & Overy LLP, and Epaminontas Triantafilou, formerly Legal Counsel at the Permanent Court of Arbitration in The Hague, have joined the firm as partner and of counsel, respectively. Both are based in the London office.

Sinclair, who specializes in International Arbitration and Public International Law, is widely recognized as one of the rising stars in the area. He is highly ranked by many legal publications, including *Chambers* and *Legal 500* for both international arbitration and public international law. Sinclair is co-author of the second edition of *The ICSID Convention: A Commentary* (Cambridge University Press, 2009) and widely published in the field of international investment law and public international law. In 2011, he was named one of *Global Arbitration Review*'s "45 under 45" of the world's leading arbitration practitioners.

Sinclair's experience includes disputes under ICC, LCIA, ICSID and UNCITRAL arbitration rules arising out of concession agreements, licences, production sharing and operating agreements, joint ventures, EPC and other construction agreements, host government and inter-governmental agreements, management and service agreements, distributorships, investment agreements, financing agreements and derivatives and post-M&A matters.

Triantafilou's broad international arbitration experience includes roles as counsel to private corporations and sovereign governments, as well as secretary to several international arbitral tribunals and legal assistant to a leading arbitrator. He has participated in arbitrations concerning power projects, water concessions, construction, shipping, aviation, financial instruments, pharmaceuticals, mining, and oil and mineral exploration in several regions around the world, including Europe, the Middle East, Central Asia, Southeast Asia, and Latin America. He has experience in disputes arising under ICC, VIAC, LCIA, AAA, SCC, UNCITRAL and ICSID arbitration rules and concerning a broad array of government contracts and concessions, joint ventures, construction agreements, and financial instrument covenants. Q

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