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Patent Infringement in the Digital Age: How a Dispute About Tooth Aligners Led to a Fight About the ITC's Jurisdiction over Electronic Transmissions

The International Trade Commission ("ITC") is an "independent nonpartisan agency that investigates and reports to the President and Congress on matters concerning import trade, tariffs and trade agreements." *Shewmaker v. Parker*, 479 F. Supp. 616, 618 (D.D.C. 1979). Established in 1930 as the U.S. Tariff Commission, the ITC has broad investigative authority over matters of international trade, including regulating the importation of goods into the country. Among its responsibilities is to serve as a forum for intellectual property owners to petition to prevent the importation of products that infringe their rights. Last year, the ITC made the following statement:

"'[I]mportation . . . of articles' should be construed to include electronic transmission of digital data because the digital data sets at issue in this investigation are true articles of international commerce that are imported into the United States and their inclusion within the purview of section 337 [of the Tariff Act] would effectuate the central purpose of the statute."—United States International Trade Commission, In re Certain Digital Models, Digital Data, and Treatment Plans for Use in Making Incremental Dental Positioning Adjustment Appliances, the Appliances Made Therefrom, and Methods of Making the Same (Apr. 9, 2014).

This sentence turned an otherwise typical patent infringement dispute about orthodontic appliances into a fierce debate about the authority of the ITC over electronic transmissions of information into the U.S. How did a patent case about tooth aligners turn into a debate that some said called into question the future of an open and free internet, the effectiveness of copyright protection in the film, music and publishing industries and, ultimately, the ITC's authority to prevent transmission into the U.S. of information that infringes, or could be used to infringe, the intellectual property rights of U.S. businesses?

How Did We Get Here?

Align Technology, Inc., ("Align") is a medical device company that that specializes in clear tooth alignment products, including the Invisalign orthodontic system. ClearCorrect Operating LLC ("ClearCorrect") like Align, develops clear, removable alignment devices under the ClearCorrect brand. Align and ClearCorrect's products are quite similar: both reposition teeth

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INSIDE

Quinn Emanuel Named Disputes Firm of the Year at *The Asian Lawyer*'s Asia Legal Awards 2015

On March 3, 2015, *The Asian Lawyer* held its second annual Asia Legal Awards, recognizing the region's foremost law firms. Quinn Emanuel shared the award for Asian Disputes firm of the Year. *The Asian Lawyer* said that the *Apple v. Samsung* litigation was one of the year's "best examples of complex, high-stakes legal work." It concluded that, "[o]n a broader level, the Samsung/Apple litigation continues to be the biggest and most high profile intellectual property dispute in the world, involving multiple jurisdictions across the globe." Q

Quinn Emanuel Win for Viasat Named 2014 Top Verdict by the *Daily Journal*, *The National Law Journal*, and *The Recorder*

In *ViaSat v. Space Systems/Loral*, the firm won a $283 million verdict for its client ViaSat. The case was named a Top 10 Plaintiff Verdict by Dollar by the *Daily Journal*, a Top Verdict of 2014 by *The National Law Journal*, and a Top California Verdict of 2014 by *The Recorder*, achieving the highest dollar amount across all categories. It was also named a "Milestone Case of the Year" at the *Managing IP North America Awards*. Q gradually through a series of aligners that a patient wears in succession until the desired positioning is achieved. Their dispute before the ITC centered on ClearCorrect's use of digital data sets—three-dimensional models of the desired positions of patients' teeth at different stages of orthodontic treatment—to construct the aligners. Specifically, ClearCorrect would scan a physical model of patients' teeth, and send the scan to its overseas affiliate ("CCP") in Pakistan. CCP would then use software to design schematics of the teeth in each incremental stage of the alignment process, and would transmit the data sets for those aligners back into the U.S. to ClearCorrect electronically. ClearCorrect would then 3D-print physical models of the schematics, and aligners would be made by molding plastic over the models. Align petitioned the ITC alleging that the activities of CCP in transmitting the data back to the U.S. violated Section 337 of the Tariff Act of 1930, namely that it led to the infringement of Align's patents.

Before reaching the substance of Align's claims, the administrative law judge ("ALJ") overseeing the dispute was faced with the threshold question of whether the ITC had authority to remedy CCP's allegedly wrongful conduct. Specifically, the ALJ had to determine whether CCP's electronic transmission of the data that ClearCorrect used to build its aligners constituted "importation of . . . articles" within the meaning of Section 337. The ALJ found that digital data was indeed an "article" under Section 337, and found CCP in violation of Section 337 on a subset of the patents at issue, recommending that the ITC issue a cease-and-desist order against further transmission of the data sets.

Following both parties' petitions for review (ClearCorrect was not found to infringe on a number of the patents), the ITC determined to review the ALJ's finding in its entirety, and requested public comment regarding whether "articles" could properly be construed to include the intangible data sets at issue. A number of organizations submitted comments to the ITC, including Google (against such a construction), and the Motion Picture Association of America ("MPAA"), the Association of American Publishers ("AAP"), and Nokia (in favor of such a construction).

Ultimately, the ITC affirmed the ALJ's finding. After considering the Tariff Act's statutory text, legislative history, principles of statutory construction, comparisons to other agencies' treatment of digital data, and policy concerns, it concluded that, although a "difficult question," the term "articles" covers digital data. Commission Opinion at 36. ClearCorrect appealed the ITC's decision to the Court of Appeals for the Federal Circuit. That appeal (Case No. 14-1527) is currently pending and has drawn, in addition to briefing from the parties, *amicus curiae* submissions from a number of organizations, including the Business Software Alliance ("BSA"), the Internet Association, Public Knowledge and the Electronic Frontier Foundation ("EFF") (in opposition to the ITC opinion); and Nokia, the AAP, the MPAA and the Recording Industry Association of America ("RIAA") (in support of the ITC opinion).

The Federal Circuit Appeal

ClearCorrect argued in its brief on appeal that not only was the ITC wrong, but the question of whether "articles" includes digital data had already been decided—in *Bayer AG v. Housey Pharmaceuticals, Inc.*, 340 F.3d 1367 (2003). Dkt. 31, at 9. In *Bayer*, the Federal Circuit considered whether 35 U.S.C. § 271(g)—a companion statute to Section 337—reached non-physical goods. 340 F.3d at 1368. In so doing, the Federal Circuit ruled that "section 271(g) was intended to address the same 'articles' as were addressed by section 1337." *Id.* at 1374. It therefore reviewed the legislative history of Section 1337, and concluded that, "Congress was concerned solely with physical goods that had undergone manufacture," and "nothing in the legislative history [of Section 337] suggest[s] that Congress was concerned that the pre-existing statutory scheme failed to reach intangible information." *Bayer*, 340 F.3d at 1373-74. According to ClearCorrect, *Bayer* was dispositive.

ClearCorrect also noted that none of the dozen amendments to the Tariff Act since 1930 gave any indication that Congress intended to include intangible information within the ITC's authority. *Id.* at 113-14. It also argued that Congress's explicit exclusion of electronic transmissions from the enforcement authority of U.S. Customs and Border Protection ("Customs") meant that Congress could not have meant the ITC to have the same power, since the ITC's primary remedial power was an exclusion order to be enforced by Customs. *Id.* at 15. Further, ClearCorrect argued that, to the extent the ITC's inability to reach electronic transmissions reveals a flaw in the statutory scheme, Congress was in the best position to remedy that flaw. *Id.* at 16.

The Internet Association, whose members include companies such as Amazon, Facebook, Google, Netflix, Twitter and Yahoo!, echoed ClearCorrect's arguments. *See* Dkt. 42. It also argued that the ITC's lack of remedial tools against electronic transmissions meant that Congress could not have intended for the ITC to have authority over them. Dkt. 42 at 9. Specifically, it argued that the ITC's core remedy was an exclusion order which, by definition, could not be enforced against electronic transmissions. Dkt. 42 at 23-25. And because the ITC's other remedy—a cease-and-desist order—was only available as a supplement or alternative where an exclusion order was available, there was no remedy that the ITC could provide against electronic transmissions. *Id.*

The BSA, whose members include major tech companies such as Adobe, Apple, Dell, IBM, Microsoft, Oracle, and others, concurred with ClearCorrect and the Internet Association's arguments. It further argued that Congress knew that electronically transmitted information existed as early as the 1930s, and that Congress entrusted regulation of such information to the Federal Communications Commission, not the ITC. Dkt. 43 at 14. It also argued that, notwithstanding the remedial purpose of Section 337, the ITC has a statutorily limited function—to "deal with unfair competition in the importation of tangible goods, not to prevent all intellectual property violations regardless of origin." *Id.* at 5. That role, BSA argued, is reserved for the district courts, which are perfectly capable of protecting intellectual property rights where the ITC cannot. *Id.* at 5.

Align and the ITC, of course, disagreed. Align argued that that the text of the Tariff Act directly supported the ITC's construction of the term "articles." Dkt. 56 at 7. Looking to the dictionary definition of the term at the time the Tariff Act was passed, and the use of the term in conjunction with other words such as "importation" and "sale," Align argued that "article" included any items that are bought and sold in commerce. *Id.* at 9, 12-13. Align dismissed as irrelevant the existence of electronic transmissions in 1930, as no commercial trade in such transmissions existed at the time. *Id.* at 15. It also rejected the notion that Congress intended to lock the ITC's authority in time, such that it would lose its authority to prevent importation of infringing products based solely on changes in the technology used for importation. *Id.* at 16. Align noted that the ITC's interpretation was in line with the Department of Labor and U.S. Court of International Trade's refusal to read a "tangibility requirement" into other comparable statutes. *Id.* at 19-20. It also distinguished *Bayer* on the grounds that Section 337 was not at issue in the case, that *Bayer* concerned only abstract information, not digital schematics, and that the Federal Circuit noted in a footnote that the language of section 337 "suggests a broader scope for section 337 than for section 271(g)." *Id.* at 28-30. The ITC joined in a number of these arguments and further noted that a broad construction of the term "articles" was consistent with "Congress's declared intention" that section 337 be "broad enough to prevent every type and form of unfair practice." Dkt. 55 at 25.

Does the Copyright Act Necessitate the ITC's Exercise of Authority over Digital Transmissions?

The MPAA and RIAA together, and the AAP separately, submitted briefs in support of the ITC opinion, arguing—in addition principles of statutory construction, legislative history, and deference to the ITC—that there was much more at stake than a simple patent dispute between Align and ClearCorrect. They argued that ruling against the ITC "could effectively read copyright protection out of Section 337 because electronic transmission is the mode by which most unauthorized copyrighted works are imported into the United States." Dkt. 77 at 3. According to the MPAA and RIAA, the term "articles" cannot be interpreted without taking into account the "realities of the marketplace." *Id.* at 13-14. That reality, in the film and music industries, is that "electronic transmission of copyrighted electronic works has become the predominant form of distribution." *Id.* AAP expressed similar concerns with respect to the publishing industry, noting the increasing popularity of eBooks (whose sales increased by almost 4,500% since 2008). Dkt. 73 at 18. As the AAP noted, quoting the U.S. Copyright Office's DMCA Section 104 Report, "time, space, effort and cost no longer act as barriers to the movement of copies [of copyrighted works], since digital copies can be transmitted [via the Internet] nearly instantaneously anywhere in the world with minimal effort and negligible cost." *Id.* at 19. Thus, for the AAP, MPAA and RIAA, the inability of the ITC to restrict the importation of electronic transmissions—which include books, movies, and music—would render Section 337's copyright protections toothless. Dkt. 77 at 3.

The AAP, MPAA and RIAA thus argued for a policy favoring broad ITC authority. But policy considerations do not necessarily dictate statutory interpretation. It may not matter how strong the argument is that the ITC *should* be able to restrict importation of digital transmissions, or how problematic the outcome would be if it could not, if the Federal Circuit finds that the statute, as drafted, places digital data outside of the ITC's reach. In that event, the responsibility for fixing problematic legislation is for Congress, not the courts.

Are Intellectual Property Rights in the United States in Jeopardy if the ITC Lacks Authority over Digital Data?

Nokia also argued in support of the ITC, noting its investment of "EUR 50 billion in research and development relating to mobile communications," and its need for assurance that "past, present and future substantial research and development efforts are fully protected from infringing imports." Dkt. 74 at 1-2. According to Nokia, a finding limiting the ITC's authority to tangible media could "gravely damage the protection of valid patent rights" because many modern patents "require both hardware and software components in order to complete the patented product or a product capable of performing a patented method." *Id.* at 15. If the ITC had no authority over electronic transmissions, Nokia argued, bad actors could simply import hardware without the software installed, and then electronically transmit the software once the hardware is in the U.S. to complete the infringing product.

Id. Nokia argued that would be "wholly contrary to the remedial purpose of Section 337," and therefore Congress could not have intended such a gap in the ITC's authority, because essentially it would render Section 337 meaningless for such patents. *Id.* at 16.

It remains to be seen how persuasive the Federal Circuit will find Nokia's argument, given that any such "gap" in intellectual property enforcement, as Nokia described it, could be dealt with in the U.S. federal courts. Indeed, Align itself pursued a concurrent federal action involving the same patents.

Is ITC Authority over Digital Transmissions a Danger to a Free and Open Internet?

Public Knowledge and EFF together submitted a brief expressing concern that the ITC's opinion left unanswered the question of "whether all transmissions of telecommunications data are within the scope of its authority." Dkt. 43 at 3. In their view, the ITC has no jurisdiction over telecommunications data transmissions and its "manufacturing of new powers over data transmission" was cause for concern because the ITC did not indicate any "limiting principles" on its power. Public Knowledge and EFF therefore argued, in addition to certain historical and statutory arguments also made by others, that Section 337 "*ought not* cover telecommunications." *Id.* at 3-4. First, they argued that counting data transmissions as imported articles could result in "conflicting legal burdens" for internet service providers. *Id.* at 4, 12. Specifically, they raised the specter that internet service providers would be forced into an enforcing role that Congress never intended, noting that the ITC conceivably could require internet and other telecommunications providers to "actively block transmission" of content. *Id.* at 13. This, they argued, conflicted with the Electronic Communications Privacy Act's prohibition on intentional interception of electronic communications and the Digital Millennium Copyright Act's ("DMCA") safe harbor from copyright liability for online service providers. *Id.* at 14. Second, they noted the importance of an open internet to society and argued that mere threat of a cease-and-desist order from the ITC would have a chilling effect, causing "service providers to refuse carriage of new and innovative services, block access to data, and otherwise restrain an open and unfettered arena of technological growth." *Id.* at 17.

For Public Knowledge and EFF, the ITC's "fail[ure] to indicate any outer limit" or any "limiting principles on the scope of the Commission's authority" over digital transmissions required reversal. *Id.* at 18. The dispute between Align and ClearCorrect implicated more than just tooth aligners—"[t]he digital models of patients' teeth at issue were, at base a series of bytes, or numbers, sent over a communications channel to be interpreted by a computer as a three-dimensional model." *Id.* at 19-20. But so are voice-over-IP telephone calls, television transmissions and radio broadcasts, over which, according to Public Knowledge and EFF, Congress never intended the ITC to have jurisdiction. *Id.* at 20. That the ITC's opinion could be read to the contrary, they argued, "necessitates this Court's clarification of the proper scope of the Commission's jurisdiction." *Id.* at 20.

Where Do We Go from Here?

As of the date of this article, the Federal Circuit appeal remains pending. Further briefing is expected from ClearCorrect, and possibly others, with oral argument expected this summer and a decision in the fall. Ultimately, the Federal Circuit will have to decide whether the ITC's authority to issue an exclusionary or cease-and-desist remedy against "importation . . . of articles" includes electronic transmissions of digital data. Its decision could have a significant impact on anyone transmitting data into the United States. Q

Antitrust Lawyer Stephen Neuwirth Named a "Titan of the Plaintiffs Bar" by *Law360*

Stephen Neuwirth, chair of the firm's antitrust and competition litigation practice, has been named a "Titan of the Plaintiffs' Bar" by *Law360*. Steve is recognized for being at the "forefront of some of the major antitrust class actions that have yielded plaintiffs hundreds of millions of dollars in damage awards." The article highlights Steve's roles in the *United States v. Microsoft* antitrust litigation, and his role as court-appointed lead counsel for plaintiffs in significant ongoing antitrust class actions, including against major polyurethane foam manufacturers and rail freight companies. The article praises Steve as "masterful" at leading litigation teams and directing the resources required to successfully litigate large antitrust class actions. Q

Opt-out Collective Actions for Competition Damages Actions—A New Dawn for Litigation in the UK

The *Consumer Rights Act 2015* (UK), enacted on March 26, 2015, heralds a significant development in UK litigation. Following years of debate, and despite the concerns of many that the UK would suffer from the apparent excesses of U.S. class action litigation, the Act introduces opt-out collective actions (the British term for class actions) for competition claims. This new regime should take effect starting October 1, 2015, and significantly raises the stakes for companies found to have infringed competition law, as they potentially face a much larger range of claims.

Background

Over the last five years, there has been a significant increase in private enforcement of competition law. With many decisions being issued by the European Commission and National Competition Authorities, companies have become increasingly aware of the degree to which they may have been impacted by unlawful cartel conduct and the need for them to seek recovery of significant sums for the benefit of shareholders. The English Courts have been at the forefront of this increased focus on private enforcement of competition law. The European Commission's recently adopted Directive on Private Enforcement seeks, in many respects, to bring most European Member States closer to the UK (see our January 2015 Business Litigation Report for details about the Directive). However, a concern has remained in the UK that it is still difficult for companies and consumers to recover the losses caused by cartels and other anti-competitive practices.

Cartel damages claims have typically been pursued by large corporations, which can either fund claims themselves or attract litigation funding. While it is possible to bring collective actions in the UK, the current opt-in regime, which requires individual claimants to positively elect to participate, has meant that only one collective action has been brought—a 2007 claim by the Consumer Association on behalf of 130 purchasers of replica football kits. The claim was settled in 2008 and no further collective actions have been brought since.

Given the lack of an effective collective action regime, the Department of Business Innovation and Skills undertook a number of consultations that culminated in the Consumer Rights Bill 2013. The Bill proposed a range of amendments to consumer and competition law, but one of the most significant was the introduction of an opt-out collective action regime, similar to the U.S. class action regime. Following protracted debate in parliament, the Bill was passed as the Consumer Rights Act 2015. The collective action amendments are set out in Schedule 8, entitled "Private Actions in Competition Law", with relevant provisions being inserted into the Competition Act 1998 and the Enterprise Act 2002.

Where Will Collective Claims Be Heard?

Collective actions will be heard in the Competition Appeal Tribunal (CAT), a specialist competition body that consists of three members: a Chairman who is a judge or senior barrister, and two members who are experienced in business, accountancy, economics, and related fields. The CAT can currently only hear cases that "follow-on" from a decision of the European Commission or the UK Competition and Markets Authority—it cannot hear cases where there has been no finding of infringement. However, the Act will extend the CAT's jurisdiction so that it will be able to hear stand-alone actions where there has been no competition authority investigation or findings.

Who Can Initiate a Claim?

Collective proceedings must be commenced by a person or company that proposes to be the representative who must obtain a collective proceedings order from the CAT.

The intention is that only those with a genuine interest in the case can act as a class representative. In addition to those who have themselves suffered loss, trade associations or consumer groups can also act as a class representative. The Government's policy is that claims should not be brought by law firms, third-party funders, or special purpose vehicles (in contrast to jurisdictions such as the Netherlands and Germany). The CAT must authorize the class representative, and where there is more than one person or company seeking approval, the CAT must determine who would be most appropriate.

Opt-in or Opt-out?

Unlike in the United States, collective actions can be either opt-in or opt-out. An opt-in claim is one where claimants must elect to join the action in order to be considered a member of the class and share in the remedies. An opt-out claim is one where an action can be pursued on behalf of a class of unnamed and, at that point, unidentified claimants. However, the class of persons, rather than the particular members themselves, must be easily identifiable in order for the CAT to make a collective proceedings order. When determining whether an action should be opt-in or opt-out, the CAT can take into account all matters it thinks fit, including (i) the strength of the claims; and (ii) the practicality of bringing the proceedings as opt-in. This second requirement will likely be a matter of much debate in the early cases, as defendants will try to have the claims brought on an opt-in basis to reduce the scope of the suit,

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Bankruptcy & Restructuring Litigation Update

New Bankruptcy Challenges for Secured Creditors. The Bankruptcy Code provides secured creditors with significant advantages over their unsecured counterparts. During the past year, however, courts have chipped away at secured creditors' rights in three important areas: enforcement of "make whole" provisions, protection against "cram downs" under a chapter 11 plan, and credit bidding.

"Make Whole" Payment Risks. Two recent decisions by courts in leading bankruptcy jurisdictions—Delaware and the Southern District of New York—have disallowed "make whole" premiums that otherwise would have been payable to secured noteholders. *In re Energy Future Holdings Corp.*, 527 B.R. 178 (Bankr. D. Del. 2015); *In re MPM Silicones, LLC ("Momentive")*, 2014 Bankr. LEXIS 3926 (Bankr. S.D.N.Y. Sep. 9, 2014), *aff'd* case no. 14 CV 7471 (VB) (S.D.N.Y. May 4, 2015). A "make whole" premium compensates a creditor for the value of future interest income lost when a borrower repays prior to maturity. Typically, the borrower must pay not only all principal and interest then owing, but also a premium based on the net present value of future interest payments that will not be paid as a result of early repayment.

In *Energy Future*, the debtor sought to use debtor in possession financing proceeds to prepay in full a series of 10% first lien secured notes. The debtor stood to benefit from the significantly lower interest rate (4.25%) for the debtor in possession financing, versus the 10% interest rate applicable to the notes' interest. The notes required payment of a "make whole" premium upon an optional prepayment. The debtor, however, claimed that it did not have to pay the "make whole" premium because its bankruptcy filing caused the immediate acceleration of the notes' maturity. The indenture trustee for the noteholders commenced an adversary proceeding asserting that the debtor was liable to pay the "make whole" premium and simultaneously filed a motion seeking a declaration that it could de-accelerate the notes without violating the automatic stay provisions of 11 U.S.C. § 362(a).

The *Energy Future* court held that the indenture trustee could not rescind acceleration without violating the automatic stay. The court indicated, however, that the trustee may be able to seek relief *nunc pro tunc* from the automatic stay "to waive the default and deaccelerate the Notes," which would have the effect of making the payment an optional prepayment—thus causing the "make whole" premium to be due. If the court denied the motion, or granted it without *nunc pro tunc* relief, then at most, the noteholders would have a damage claim for denial of the rescission right. The court determined that material facts needed to be resolved before it could determine whether cause existed to lift the automatic stay.

The Bankruptcy and District Courts in *Momentive* reached a similar result, even though the context was different from *Energy Future*. In *Momentive*, the debtors proposed a reorganization plan under which senior noteholders would be paid in full, but without approximately $200 million in "make whole" compensation for future interest through the original maturity of the notes. The senior noteholders objected, arguing that the plan violated the terms of the applicable indenture. The *Momentive* courts disagreed, holding that the bankruptcy filing resulted in an automatic acceleration of the senior notes. In order for the "make whole" premium to apply, the indenture needed to specifically provide that such a payment was due in the event of automatic acceleration. Absent such specificity, the noteholders had no enforceable claim to the "make whole" premium. Nor did the Bankruptcy Court allow the senior noteholders to rescind the automatic acceleration of the notes that occurred upon the bankruptcy filing, holding that the automatic stay barred de-acceleration.

Cram Down Interest Rates. The same Bankruptcy Court in *Momentive* also confirmed, over the objection of secured creditors, a chapter 11 plan that provided for interest at 2% over the risk-free Treasury rate, even though the debtors were ***not*** able to obtain comparable rates from replacement lenders. The District Court affirmed.

A chapter 11 plan may be confirmed over a secured creditor's objection only if the plan satisfies the "cram down" requirements in Bankruptcy Code section 1129(b)(2)(A). Although the Code provides three alternatives for structuring a cram down, by far the most common is to provide the secured creditor with deferred payments "of at least the value" of the creditor's claim, determined "as of the effective date of the plan." This might suggest that in order to be crammed down, a secured creditor must receive installment payments whose total present value equals or exceeds that of its claim. Indeed, that is precisely what a four-justice plurality of the Supreme Court said in the landmark *Till* decision, which interpreted a similar provision in the Bankruptcy Code governing the confirmation of plans for individual debtors under chapter 13. *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004). The Supreme Court in *Till*, however, also held that "present value" does not include the lenders' transaction costs or profits, but rather only what is required to compensate lenders for the risks of inflation and default. Although the Supreme Court did not specify the precise method for determining the compensation a lender should receive, it noted that courts "generally" had approved an adjustment of 1% to 3% over a comparable risk-free rate (such as prime).

Courts and commentators have pondered whether *Till* should govern cram downs in chapter 11 cases. The Supreme Court left this issue open in a footnote, which stated that "when picking a cram down rate in a Chapter 11 case, it might make sense to ask what rate an efficient market would produce." 541 U.S. at 476 n.14. Relying on this footnote, a number of courts have held that, when considering whether to cram down a secured creditor, a bankruptcy court must first determine whether an efficient market interest rate can be determined. Only in the absence of such an efficient market should the court apply the *Till* approach. *See, e.g.*, *In re Am. Homepatient, Inc.*, 420 F.3d 559 (6th Cir. 2005). The *Momentive* courts disagreed, finding the Supreme Court's footnote to apply only to the appropriate rate for debtor in possession financing, and not to a cram down under a plan. The courts also interpreted the 1% to 3% risk adjustment discussed in *Till* not as simply a general guideline, but rather as a specific range to use in chapter 11 cases "unless there are extreme risks" for the crammed down creditor. The correct cram down rate must be "premised on a base rate that is riskless, or as close to riskless as possible, plus a risk premium in the range of 1 to 3 percent, if at all, depending on the Court's assessment of the debtors' ability to fully perform the replacement notes."

Momentive was not the first case to apply *Till* to a chapter 11 cram down, but it is clearly the most noteworthy. Although *Momentive*'s discussion of cram down interest rates has yet to be cited—favorably or otherwise—by another published decision, it is already having a material effect on how secured creditors and debtors view the threat of a cram down in chapter 11. The decision currently is on appeal to the Second Circuit.

Credit Bidding. Bankruptcy Code section 363 governs the sale of assets in a bankruptcy case. Section 363(k) permits a secured creditor to credit bid in a sale of its collateral, rather than bidding cash, "unless the court for cause orders otherwise." While the Code does not define "cause," courts historically have applied the exception sparingly, and usually only in the face of creditor misconduct, or bona fide disputes concerning the creditor's claims or liens.

The Bankruptcy Court for the District of Delaware has held that "cause" existed to limit a secured creditor's right to credit bid when it was necessary to promote a competitive bidding environment for a debtor's assets. *In re Fisker Automotive Holdings, Inc.*, 510 B.R. 55 (Bankr. D. Del. 2014). The court limited a secured creditor's credit bid based on (i) evidence that "bidding will not only be chilled without the cap; bidding will be frozen" because the only competing bidder would not bid if the full amount of the credit bid was permitted, and (ii) a stipulation between the debtor and the creditors' committee that the secured creditor's claim was "partially secured, partially unsecured and of uncertain status for the remainder." The court found these factors constituted sufficient cause to cap the credit bid at $25,000,000, which coincided with the amount the creditor had paid for the claim in the secondary market. The court noted that it "may deny a lender the right to credit bid in the interest of any policy advanced by the [Bankruptcy] Code, such as to ensure the success of the reorganization or to foster a competitive bidding environment." *Id.* at 60, n.14.

The court in *Free Lance-Star Publishing* also limited credit bidding. 512 B.R. 798 (Bankr. E.D. Va. 2014). Prior to the debtor's bankruptcy filing, a party with a "loan-to-own strategy" ("DSP") acquired secured claims against the debtor. Unbeknownst to the debtor, DSP unilaterally filed liens on additional assets in which it previously did not have a security interest. DSP also aggressively pushed the debtor toward a bankruptcy process in which DSP would acquire the debtor's assets through a credit bid.

In finding cause to limit DSP's credit bid under section 363(k), the court held that "DSP's overly zealous loan-to-own strategy" had "depressed enthusiasm for the sale in the marketplace [because p]otential bidders now perceive the sale of the business to DSP as a *fait accompli*." *Id.* at 807. The court accordingly limited DSP's total credit bid to a fraction of its claim, and did not allow DSP to credit bid on the assets in which DSP had unilaterally filed its lien.

To date, *Fisker* and *Free Lance-Star* do not appear to have resulted in wholesale limitations of a secured creditor's credit bid rights. Nonetheless, both serve as cautionary tales for parties who acquire loans of distressed companies seeking to own the company. Despite section 363(k) generally permitting credit bidding, it is not an absolute right. If a court finds that a credit bid will dampen the likelihood of a robust auction, or that a secured creditor may have engaged in overly aggressive tactics, the court may limit the credit bid, or even potentially eliminate it, in order to advance the objective of fostering a competitive bidding environment.

Securities & Structured Finance Litigation Update

U.S. Supreme Court Clarifies When an Opinion Is Actionable Under the Securities Act. Under Section 11 of the Securities Act of 1933, a securities purchaser may sue for damages if the securities registration statement "contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading." 15 U.S. Code § 77k. On March 24, 2015, the Supreme Court considered the application of Section 11 to statements of opinion, such as statements prefaced by "we believe," that turn out to be incorrect. *See Omnicare, Inc. v. Laborers Dist. Council Const. Industry Pension Fund*, 135 S.Ct. 1318 (2015). The Court held that an opinion may be actionable under Section 11 as an untrue statement of fact if the opinion was not subjectively believed, or may be actionable as a misleading statement if facts were omitted calling into question the basis of the opinion.

Before the U.S. Supreme Court's decision in *Omnicare*, there was a conflict among the federal courts regarding the application of Section 11 of the Securities Act to statements of opinion. Some courts, including courts in the Second, Third, and Ninth Circuits, interpreted liability narrowly based on the U.S. Supreme Court's decision in *Virginia Bankshares v. Sandberg*, 111 S. Ct. 2749 (1991), which addressed liability for statements of opinion under Section 14(a) of the Securities Exchange Act of 1934. Those courts held that only statements of opinion that were not subjectively believed (*i.e.*, the speaker did not, in fact, hold the beliefs or opinions expressed) were actionable under Section 11. Other courts, including courts in the Sixth Circuit, interpreted liability broadly, holding that any opinions ultimately found to be incorrect, regardless of the speaker's belief, were actionable under Section 11 because the statute imposes liability for misrepresentations regardless of the speaker's intent or state of mind. Finally, other courts, such as courts in the First Circuit, fell in the middle, holding that a statement of opinion was actionable if it did not represent the actual belief of the person expressing the opinion, lacked any basis, or knowingly omitted undisclosed facts tending seriously to undermine the accuracy of the statement.

In *Omnicare*, the U.S. Supreme Court adopted a middle ground by parsing the language of Section 11, recognizing that the statute imposes liability for both false statements of fact *and* omissions of facts. The Court set forth one standard for determining when a statement of opinion is as an untrue statement of fact, and another standard for determining when a statement of opinion is misleading because facts relevant to the opinion have been omitted.
The Court held that because every statement of opinion explicitly affirms one fact—that the speaker actually holds the stated belief—a statement of opinion is an untrue statement of fact if the speaker did not, in fact, hold the belief. *Omnicare*, 135 S. Ct. at 1326. The Court also distinguished pure statements of opinion from statements of opinion with embedded facts, such as facts to justify the opinion. The Court noted that if embedded facts are untrue, they are actionable as untrue statements of fact even if included in the context of an opinion. *Id.* at 1327.

The Court then tackled the more complex problem of determining when a statement of opinion is misleading because of the failure to disclose certain facts. The Court recognized that "a reasonable investor may, depending on the circumstances, understand an opinion statement to convey facts about how the speaker has formed the opinion—or, otherwise put, about the speaker's basis for holding that view." *Id.* at 1328. The Court noted that "if the real facts are otherwise, but not provided, the opinion statement will mislead the audience." *Id.* The Court therefore held that if a registration statement omits material facts about the issuer's inquiry into or knowledge concerning a statement of opinion, and if those facts conflict with what a reasonable investor would take from the statement itself, then the statement of opinion may be misleading and actionable under Section 11. *Id.* at 1329.
In holding that a statement of opinion may be misleading based on the omission of certain facts, the Court noted that whether an omission of fact makes a statement of opinion misleading depends on the context, such as the expected level of inquiry into an opinion or the other disclosures surrounding the opinion. *Id.* at 1330. The Court also noted that it is not sufficient for a securities purchaser to make only the conclusory allegation that the opinion had no basis in fact; the purchaser "must identify particular (and material) facts going to the basis for the issuer's opinion—facts about the inquiry the issuer did or did not conduct or the knowledge it did or did not have—whose omission makes the opinion statement at issue misleading to a reasonable person reading the statement fairly and in context." *Id.* at 1332.

Although the standard for false or misleading statements of opinion set forth in *Omnicare* was decided under Section 11 of the Securities Act, the standard likely will be applied to claims under other federal and state securities laws that impose liability for untrue statements of material fact or omissions of material fact required to make the statements not misleading, including Section 12 of the Securities Act, which imposes liability for any misrepresentations (even those outside the registration statement) made in connection with a securities offering, and state securities laws similar to Section 12. In fact, the Southern District of New York recently applied the *Omnicare* standard to the misrepresentation element of claims under Section 10(b) and Rule 10b-5 of the Securities Exchange Act. *See In re BioScrip, Inc. Sec. Litig.*, -- F. Supp. 3d --, 2015 WL 1501620, at *9 (S.D.N.Y. Mar. 31, 2015).

Life Sciences Litigation Update

Trends in Post-grant Review of Orange Book Patents. The America Invents Act's post-grant challenges ("AIA proceedings") continue to grow as an option for companies challenging a patent's validity. In the first full fiscal year that AIA proceedings—*inter partes* review ("IPR"), covered business method review ("CBM"), and post-grant review ("PGR")—were available (FY2013), companies filed 563 petitions. *See* USPTO, AIA Progress Statistics, *available at* http://www.uspto.gov/sites/default/files/documents / aia_statistics_03-26-2015.pdf. ("PTO Stats") In FY2014, the number of petitions ballooned to 1494. *Id.* At the same time, district court patent filings dropped 18%. *See* DocketNavigator, 2014 Year in Review, *available at* http://home.docketnavigator.com/year-review/. Now, halfway through FY2015, the United States Patent & Trademark Office ("PTO") has already received close to 950 fillings. *See* PTO Stats.

Pharmaceutical companies with patents listed in the U.S. Food and Drug Administration's publication entitled, "Approved Drug Products With Therapeutic Equivalence Evaluations," known as the "Orange Book," have not escaped post-grant challenges. Traditionally, generic companies attempting to market a generic version of a patent-covered branded pharmaceutical drug product before patent expiration had no choice but to litigate against the innovator company in district court. Now, generic pharmaceutical companies, like many companies in other technological areas, have chosen to file AIA proceedings with the PTO while district court litigations are pending.

AIA proceedings are attractive to all patent challengers, including generic drug companies for multiple reasons. In general, AIA proceedings proceed more quickly than district court litigations, offer lower burdens of proof and broader claim constructions, and have, thus far, resulted in high success rates for petitioners. Thus, it's understandable that patent challengers are singing the AIA's praises, while patent owners are becoming ever more fearful.

For the PTO to institute an AIA proceeding, the petitioner must show either a reasonable likelihood of success of proving at least one challenged claim invalid (in IPRs) or that the challenged claim is invalid by a preponderance of the evidence (in CBMs and PGRs). As of March 26, 2015, the PTO reported it had issued 1829 Institution Decisions since the inception of AIA proceedings. *See id.* The PTO has instituted trial in 76% of those decisions. *Id.* And once instituted, the challenged claims fair no better. So far, less than 20% of the instituted claims have survived the PTO's Final Written Decisions.

When looking at the trends, however, petitioner success rates are not uniform across all technologies. Patent owners with pharmaceutical patents should be breathing a little easier because the petitioner success rates are noticeably lower for such patents, and the possibility of challenging pharmaceutical patents via a CBM, which offers a broader array of invalidity grounds and less harsh estoppel provisions than an IPR, has been recently rejected.

Specifically, there have been 97 total AIA proceedings filed against Orange Book patents to date: 90 IPRs, 6 CBMs and 1 PGR. Out of the 47 Institution Decisions issued, 18 petitions (over 38%) have been denied. Further, in each of the three Orange Book IPRs decided to date, every claim has been upheld as patentable. *See* IPR2013-00368, -371, -372. The PTO has also rejected generic pharmaceutical companies attempts to shoehorn Orange Book patents into the CBM patent definition. The PTO has been liberal in its interpretation of what is included in a "financial product or service," and therefore eligible for CBM review. But in the first-ever and only CBM attack in the pharmaceutical industry, Quinn Emanuel secured Decisions Not to Institute review of six patents for Jazz Pharmaceuticals. *See* CBM2104-00149, -150, -151, -153, -161, -175. The PTO denied the CBMs, holding that Jazz's patents did not claim a "financial product or service." It was only the second time the PTO had denied institution of CBM review on these grounds, and the first time that the PTO found that the patent owner affirmatively showed its claims did not encompass a "financial product or service."

There are currently sixty-five Orange Book IPRs pending. In seven of those proceedings, Quinn Emanuel represents the patent owner. Five of the sixty-five IPRs have completed oral argument and are slated for Final Written Decisions within the next few months. We will soon know if Orange Book patent owners will continue to experience success in AIA proceedings. Q

VICTORIES

Landmark Environmental Victory

In a case the *New York Times* called "the most ambitious environmental lawsuit ever," the firm helped secure a complete dismissal with prejudice. The historic environmental lawsuit had been filed by the Board of Commissioners of the Southeast Louisiana Flood Protection Authority—East (the "Board") against almost 100 oil and gas companies in Louisiana state court, including two of the Quinn Emanuel's clients. The headline-making complaint named Quinn Emanuel's clients and nearly a hundred other oil and gas companies, and alleged that oil and gas activities (in particular, dredging canals to access oil and gas wells) destroyed Louisiana's coastline and diminished the natural buffer zone that protects against storm surges. The Board also alleged that, as a result, it faced increasing storm surge risk and flood protection costs, and sought damages from the defendants to pay for the restoration of the coastline—an effort it claimed would cost approximately $50 billion. The case was the subject of extensive press coverage, as it touched on national issues like the Keystone Pipeline debate and the federal government's role in encouraging oil and gas exploration, as well as local hot button issues such as wetland loss and hurricane protection.

The first challenge was to get the case out of Louisiana state court where plaintiff initially filed it, and into federal court. The firm worked hand-in-hand with the other key defendants to develop and execute a strategy to remove the case to federal court and keep it there. Faced with a complaint that lacked any basis for diversity jurisdiction and artfully avoided pleading any federal claims, the defense urged the court to look past the labels plaintiff used and instead focus on the test for substantial federal question jurisdiction. In an early victory, Judge Nanette Brown of the U.S. District Court for the Eastern District of Louisiana denied the plaintiff's motion to remand in July 2014.

Having secured a preferred venue in federal court, Quinn Emanuel and the other defendants launched into a coordinated effort to dismiss the case. This included extensive motion to dismiss briefing on issues ranging from whether the Board's claims were adequately stated, preempted by federal law and barred under state law, or non-justiciable and fell within the primary jurisdiction of federal and state agencies, as well as a well-attended and highly-publicized oral argument in New Orleans. Ultimately, Judge Brown rendered a decision that carefully and meticulously addressed each of the Board's six causes of action, and held that each of them failed to state a claim upon which relief could be granted. The victory was sweeping, but of particular lasting significance was the Court's determination that the Board was incapable of making the showing that the defendants owed a specific duty to protect the Board from the results of coastal erosion allegedly caused by oil and gas activities along the coast. Given that several other variations of wetland loss cases are pending against the oil and gas industry in Louisiana and elsewhere, Judge Brown's ruling is likely to become a key precedent in similar cases.

The Board has appealed the decision to the Fifth Circuit.

Victory in Receivership Action Against Caesars Entertainment

The firm obtained a major victory in the Delaware Chancery Court on behalf of the Indenture Trustee for holders of $1.25 billion in notes issued by Caesars Entertainment Operating Company, Inc. ("Caesars"), a leading gaming and resort company. Beginning around 2011, Caesars began transferring billions of dollars in cash, casinos, intellectual property, and other assets to affiliated entities. Caesars was rendered insolvent, and by 2014 was admitting that it would not be able to repay its debts without a major restructuring.

UMB Bank, as Indenture Trustee, retained Quinn Emanuel to vindicate the noteholders' rights to repayment. On November 25, 2014, UMB filed a 200-page, 400-paragraph complaint cataloging the wrongful conduct of Caesars, its affiliates, and their boards of directors. The complaint alleged fraudulent transfers, breaches of fiduciary duty, and other wrongdoing that stripped valuable assets out of Caesars and the reach of its creditors. In order to stop the asset stripping in its tracks, the firm sought to place Caesars into receivership under Section 291 of Delaware's General Corporation Law. On December 17, 2014, after accelerated briefing and a contested hearing, the Court handed the firm a major victory by agreeing to expedite the Complaint's demand for a receiver, effectively giving Caesars a horizon of just a few months before it faced handing over management to court-appointed officials. The pressure exerted by this hard-won ruling paved the way for execution of a Restructuring Support Agreement supported by holders of more than $6 billion

Victory in Patent Action for MicroStrategy

On April 3, 2015, in a precedential opinion, the United States Court of Appeals for the Federal Circuit affirmed a summary judgment ruling from a district court in the Northern District of California in a patent lawsuit brought by Vasudevan Software Inc. ("VSI"), which had found that Quinn Emanuel's client, MicroStrategy, Inc., did not infringe any asserted patents.

All four of the asserted patents related to database and online analytical processing ("OLAP") technology. The patents purported to address the problem of how to merge data from different databases "on the fly" and generate an "OLAP cube," which is a method of storing data in a multidimensional form. Quinn Emanuel attorneys successfully argued to the district court that statements made during prosecution of the asserted patents limited the claimed invention to specialized "disparate" databases that cannot be combined using traditional techniques such as common keys.

The appeal before the Federal Circuit centered on the meaning of these prosecution history statements and whether the patentee was simply listing examples of ways databases could be "disparate" or whether the patentee was actually defining the term "disparate." The Federal Circuit wholly adopted Quinn Emanuel's arguments and determined that the prosecution history statement was definitional and excluded our client's products.

This was an important decision for two reasons. First, the Federal Circuit held that our client's marketing documents, which described its products as being able to join data from "disparate databases" (the exact language in the patent claims), were not substantial evidence of infringement. Second, we believe that this opinion is now the first appellate decision applying the formal logical rule "DeMorgan's Theorem" to interpreting patent claims. Q

(Continued from page 5)

while claimants will want the CAT to allow the claim to proceed on an opt-out basis. The requirement for the CAT to determine whether claims proceed on an opt-in or opt-out basis is said to be a safeguard against the potential excesses of U.S.-style class actions. Where cases proceed on an opt-out basis, the class members are limited to those domiciled in the UK. Any non-UK domiciled individuals or companies must opt-in to the claim.

Certification of Claims to Proceed on a Collective Basis

In light of concerns regarding the potential for the collective action regime to be abused through unmeritorious claims, the Act and the draft CAT Rules provide for a range of matters that the CAT will need to consider before it certifies a claim to proceed as a collective action. This includes an assessment of whether collective proceedings are an appropriate means for the fair and efficient resolution of the issues; the costs and benefits of the proceedings; the size and nature of the class; whether the claims are suitable for an aggregate award of damages; and the availability of alternative dispute resolution. In deciding whether to allow claims to proceed on an opt-in or opt-out basis, it is proposed that the CAT also consider strength of the claims.

It will be important to see how the CAT approaches the certification process given that in most cartel damages cases there is significant information asymmetry, as defendants typically have substantially more information than claimants. This issue is addressed in English litigation at the disclosure stage. However, if the certification stage becomes a mini-trial of the substantive issues, as it has become in the U.S., and the claimants have not had the benefit of disclosure, it will remain to be seen how many cases can meet the merit requirements to be brought as a collective action.

How Will These Cases Be Funded?

In April 2013, contingency fees (known as Damages Based Agreements) were allowed in English litigation. However, as a safeguard against the perceived excesses of U.S. class action litigation, the Act prohibits the use of contingency fee arrangements for opt-out collective actions. In light of this, the Act provides that the CAT can order that any unclaimed damages be used to cover the representative's costs and expenses of bringing the claim. However, the Act also does not remove the UK "loser pays" rule, which means that the class representative is exposed to adverse costs in the event that the claim is unsuccessful. This gives rise to a number of considerations for opt-out claims.

Lawyers for class representatives will need to decide whether they are willing to act under a Conditional Fee Agreement (CFA) with a success fee, or whether the representative will need a litigation funder. For large claims, and given that the experience in the U.S. suggests well in excess of 50% of class damages remain unclaimed, lawyers may be willing to take the risk and act on a CFA with a success fee that can be paid from unclaimed damages. Given the potential adverse costs exposure, class representatives will require "After-the-Event" insurance. It remains to be seen what premiums will be offered by insurers and whether they are willing to defer those and take the risk of whether unclaimed damages are sufficient to cover the premium.

Conclusion

There is much uncertainty in the new collective action regime that will take time to resolve through the early cases, and it remains unclear whether the regime will be expanded in the future to cover claims for breaches of other laws. What is clear, however, is that the new regime both increases the risks and exposure for cartel defendants and presents significant opportunities for claimants to obtain recoveries. Q

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