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Renegotiation of, or Withdrawal from, NAFTA: Context and Possible Consequences

Introduction

The North American Free Trade Agreement ("NAFTA") is a trade agreement signed by Canada, Mexico, and the United States that came into force on January 1, 1994. Its goal was to eliminate barriers to trade and investment, creating one of the largest free trade zones. Since NAFTA came into effect, trade among the NAFTA countries has more than tripled, reaching US $1.1 trillion in 2016 (James McBride and Mohammed Aly Sergie, NAFTA's Economic Impact, The Council on Foreign Relations, January 24, 2017, available at http://www.cfr.org/trade/naftas-economic-impact/p15790). NAFTA also provided a mechanism for investor-state dispute resolution, which led to a proliferation of investments in all three countries (NAFTA Investment Law and Arbitration, xxiv (Todd Weiler ed. 2004)). Indeed, the record shows that NAFTA has led to at least 80 investment arbitrations against NAFTA Parties and has resulted in a perfect win-loss record for the United States (Todd Weiler, naftaclaims.com (March 12, 2017), http://www.naftaclaims.com/).

NAFTA has not been without critics, however. Most recently and perhaps most critical for NAFTA's longevity, President Trump has pledged to renegotiate NAFTA, and if renegotiation is not possible, then to withdraw from NAFTA altogether. Modification of or withdrawal from NAFTA could have a number of serious consequences for investments and investors. For example, Mexico already has experienced a

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INSIDE

Law360 Names Three Quinn Emanuel Groups as "Practice Groups of the Year"

Law360 named Quinn Emanuel's Banking, Intellectual Property, and White Collar Practice Groups to its listing of 2016 "Practice Groups of the Year." The groups were identified based on the importance and size of the matters the firm worked on and the excellence of the results. Q

Firm Retained in the Top Two Most Significant Cases in the UK for 2017

Two of the firm's cases, *Walter Hugh Merricks CBE v. MasterCard Inc & Ors* and *Law Debenture Trust Corporation plc v. Ukraine*, were named as the top two cases in *The Lawyer*'s list of "Top 20 Cases of 2017" in the UK. Seen as cases "which will become the most high-value and explosive claims of the next 12 months"—*The Lawyer* acknowledged both the valuation and importance of these matters. The firm's settlement of the claims of a number of the largest institutional claimants in the RBS Rights Issue litigation is also listed in the Top 20, as well as the firm's work on behalf of Eurasian Natural Resources Corporation (ENRC) in respect of a Serious Fraud Office investigation. Q

Lazar Raynal Joins Chicago Office

Lazar P. Raynal has joined Quinn Emanuel as a partner based in the Chicago office. Lazar was formerly a partner at McDermott Will & Emery where he was global chair of the firm's litigation practice and co-chair of the Trust & Estate Controversy Practice. Lazar is an experienced trial lawyer who tries high-stakes cases in state and federal courts and in domestic and international arbitrations around the world. He has also represented clients in numerous internal investigations in response to governmental investigations and civil suits. Lazar received his J.D. from University of Notre Dame Law School *cum laude* and is admitted to practice in Illinois. Q chilling of investment by U.S. investors in light of the prospect of NAFTA's coming changes. Additionally, although Canada seems amenable to the prospect of renegotiating NAFTA, Mexico has hinted that it will not sit down with the United States to renegotiate the agreement.

"America First"

Within days of taking office, President Trump formally withdrew from the Trans-Pacific Partnership, another free trade deal, highlighting a significant policy shift under his administration. In tune with what he has dubbed his "America First" policy, President Trump's White House has said, "[i]f our partners refuse a renegotiation that gives American workers a fair deal, then the President will give notice of the United States' intent to withdraw from NAFTA" (*America First Foreign Policy*, (March 10, 2017) https://www.whitehouse.gov/america-first-foreign-policy).

President Trump's policy towards NAFTA has already had repercussions in the investment community, particularly with respect to investor-state disputes. In what would seem like an unrelated matter, President Trump recently invited TransCanada to reapply for a permit to construct the Keystone XL Pipeline, a pipeline that would bring more than 800,000 barrels per day of heavy crude to the Gulf Coast from Canada (*America First Foreign Policy*, (March 10, 2017) https://www.whitehouse.gov/america-first-foreign-policy). The Obama Administration had previously denied TransCanada's permit, causing TransCanada to initiate arbitration against the United States under Chapter 11 of NAFTA, arguing that the refusal to allow the project violated the substantive protections that NAFTA affords investors of the other member states. (TransCanada Corporation & TransCanada Pipelines Limited Request for Arbitration, June 24 2016 para. 1, available at https://www.keystone-xl.com/wp-content/uploads/2016/06/TransCanada-Request-for-Arbitratio-2n.pdf).

In light of President Trump's executive order allowing TransCanada to reapply for a permit, TransCanada has suspended the NAFTA arbitration. If the State Department approves the project, the NAFTA claim likely will be rendered moot. And while the status of Keystone is not yet certain, President Trump's decision to allow TransCanada to re-apply for a permit has had the effect of cooling tensions for the time being.

TransCanada's example, however, seems to be isolated. President Trump's broader posture on NAFTA could well have the opposite effect in the investment community, as it could lead to uncertainty as to the fate of investor-state disputes under NAFTA's dispute settlement provisions.

Trade Agreements Under U.S. Law

Under U.S. law, trade agreements are not treaties. This means that, unlike a treaty, a trade agreement: (1) is not "self-executing"; (2) does not require two-thirds approval by the Senate; and (3) does not have the force of law upon ratification. Instead, trade agreements are considered "congressional-executive agreements" that are easier to enact than a formal treaty since they do not require a supermajority from the Senate. Instead, the President typically signs a "congressional-executive agreement," which Congress then puts into effect through implementing legislation, which finally is signed into law by the President. A "congressional-executive agreement" also is limited in scope, as it can deal only with matters that are reserved for Congress and the President under the U.S. Constitution, specifically the powers of Congress under Article 1, Section 8 and the powers of the President under Article II, Section 2. Congress, however, has delegated certain powers to the President dealing with commerce with foreign nations, including the President's power to enact trade agreements on his own. Given that the NAFTA is one of these congressional-executive agreements (it was implemented by legislation—the North American Free Trade Implementation Act ("NAFTA Act")) President Trump's new policy may have far-reaching implications on the modification of and/or the United States' withdrawal from NAFTA.

Modification of NAFTA: Possible Areas of Negotiation

The NAFTA Act arguably gives President Trump the authority to raise tariffs on imports from the NAFTA countries to pre-NAFTA levels. Tariff reductions under NAFTA were implemented via presidential proclamation pursuant to Section 201(a) of the NAFTA Act. Outside of raising tariffs, President Trump also could seek to enter into negotiations to amend NAFTA pursuant to NAFTA Article 2202, which provides:

1. *The Parties may agree on any modification of or addition to this Agreement.*
2. *When so agreed, and approved in accordance with the applicable legal procedures of each Party, a modification or addition shall constitute an integral part of this Agreement.*

NAFTA Article 2202 is silent on whether congressional approval would be required for any such amendment in order to be "in accordance with applicable legal procedures." Since its inception, there have been no amendments to NAFTA. Generally, the negotiation of executive agreements is considered within the exclusive purview of the Executive (John C. Yoo, *Laws as Treaties: The Constitutionality of Congressional-Executive Agreements*, 99 Mich. L. Rev. 757, 758 (2000)). In the case of NAFTA, however, since it is a "congressional executive agreement," Congress likely must approve any proposed modifications before they enter into force (*Id*. at 759).

Some have posited that, in addition to raising tariffs, the President could focus on the "rules of origin" that govern what constitutes a finished good produced within the free trade area (Neil Irwin, *What is NAFTA and How Might Trump Change It?*, N.Y. Times, Jan. 25, 2017, available at https://www.nytimes.com/interactive/2017/upshot/what-is-nafta.html; *See also* Christopher Wilson, Five Ways Trump Could Improve NAFTA, January 23, 2017, available at https://www.forbes.com/sites/themexicoinstitute/2017/01/23/trump-to-announce-plans-for-renegotiation-of-nafta-five-ways-to-improve-the-agreement/#1afcbdea5562). The President could seek to decrease the components of a finished good that can originate in a non-NAFTA country (*Id*.). Currently, a certain percentage of component parts of a finished good may originate in non-NAFTA countries, like China (*Id*.). Requiring more constituent parts of a finished good to originate in NAFTA countries could provide advantages to U.S. manufacturers, but may result in disadvantages to Mexican and/or Canadian manufacturers seeking to export goods to the U.S. (*Id*.).

The U.S. may also ask Canada and Mexico to expand the definition of a "*de minimis*" shipment, allowing more goods to be shipped to their countries without taxes (*Id*.). In 2016, Congress passed legislation to raise the U.S. *de minimis* value to $800 (Trade Facilitation and Trade Enforcement Act of 2015, Pub. L. No. 114–125 (2016)). Small shipments to the U.S. under $800 are considered *de minimis,* escaping customs revisions. Canada and Mexico, however, have a much lower *de minimis* threshold. Encouraging Canada and Mexico to reciprocally expand the *de minimis* definition would encourage smaller U.S. companies looking to sell their goods abroad.

Modifications also could impact the scope of the investor-state dispute resolution mechanism under NAFTA Chapter 11. The President, for example, could seek to limit the ability of Canadian or Mexican companies to sue the U.S. government under Chapter 11 of NAFTA, although there is no express indication at this time that President Trump is considering renegotiating the dispute settlement provisions of the agreement. The President also could seek renegotiation of the substantive protections afforded under NAFTA, but again there is no express indication from President Trump in this regard.

Withdrawal from NAFTA

As mentioned, President Trump could (and has threatened to) opt for the more radical option of withdrawing from NAFTA if his oft-touted negotiation skills don't yield the deal he wants. Withdrawal from NAFTA is quite straightforward. NAFTA Article 2205 requires only written notice to the other Parties,. Withdrawal will become effective six months after the notice.

Because trade agreements are not treaties in the traditional sense, however, some might argue that withdrawal is not as simple as Article 2205 provides. Specifically, it is worth considering whether President Trump has a unilateral right to withdraw from NAFTA without Congressional approval, or whether withdrawal from NAFTA under Article 2205 results in an automatic termination of the NAFTA Act.

As to the first issue, the majority consensus appears to be that President Trump has the power to withdraw the U.S. from NAFTA without Congressional approval. This position finds support in the U.S. Constitution as well as in the Trade Act of 1974, which is the prevailing U.S. law governing trade agreements. On the one hand, under Article 1, Section 8 of the U.S. Constitution, Congress has delegated certain powers related to commerce with foreign nations to the President, thereby allowing the President to execute domestic trade policies with foreign nations by way of trade agreements in accordance with his foreign affair powers under Article II of the U.S. Constitution. Section 125 of the Trade Act of 1974, on the other hand, allows the President to withdraw from any trade agreement made under that Act, which will become effective at the end of the period specified in the relevant agreement. Thus, taking into account the clear wording of NAFTA Article 2205, President Trump may very well unilaterally withdraw from NAFTA by following the procedure set out in the Agreement.

With respect to the second issue, it is quite likely that withdrawal from NAFTA under Article 2205 also will lead to the repeal of the NAFTA Act. Section 109(b) of the NAFTA Act, which governs the termination of the NAFTA status, states that:

> *During any period in which a country ceases to be a NAFTA country, sections 101 through 106 shall cease to have effect with respect to such country.*

Accordingly, it could be argued that the NAFTA Act provides for automatic termination in the event that the U.S. withdraws under NAFTA Article 2205.

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Second Circuit Clarifies Process for Enforcement of Nondomestic Arbitral Awards Against Alter Egos of Award Debtor

In a recent pair of opinions, the United States Court of Appeals for the Second Circuit clarified that the procedure for enforcing a nondomestic arbitration award does not require a separate "confirmation" step. *CBF Indústria de Gusa S/A v. AMCI Holdings, Inc.*, 846 F.3d 35 (2d Cir. Jan. 18, 2017) (the "initial opinion"); *CBF Industria de Gusa v. AMCI Holdings, Inc.*, Nos. 15-1133-cv(L), 15-1146-cv(CON), 2017 U.S. App. LEXIS 3815 (2d Cir. Mar. 2, 2017) (the "revised opinion"). The Second Circuit also held that enforcement of the award against third parties is a matter of local law (in this case, the law of the Southern District of New York), not a matter of the scope of the parties' arbitration agreement.

Background

In *CBF v. AMCI*, a producer of pig iron (a type of metal) had entered into a series of sales contracts with a purchaser. When the price of pig iron crashed, the purchaser failed to perform under the contracts. The producer initiated an ICC arbitration against the purchaser and obtained an award for approximately $48 million. However, the purchaser had transferred its assets to other companies and, following Swiss bankruptcy proceedings, stopped existing under Swiss law. During the arbitration, the producer claimed that the purchaser had committed fraud by through secret asset transfers, but the tribunal did not allow the producer to proceed against any third parties for lack of evidence of fraud in the Swiss bankruptcy proceedings.

Nonetheless, with the award in hand, the producer initiated enforcement proceedings in the Southern District of New York against alleged alter egos and successors-in-interest of the purchaser. In April 2014, the Southern District of New York dismissed the enforcement proceedings because the producer had not "confirmed" the award at the seat of the arbitration (i.e., Switzerland). Citing a 1963 Second Circuit decision, *Orion Shipping & Trading Co.*, 312 F.2d 299, 301 ("*Orion*"), the court held that the producer could not pursue enforcement of the "unconfirmed" award. The court also dismissed the producer's fraud claims because the producer had raised similar claims in the arbitration.

In response to the dismissal, the producer then initiated new proceedings to "confirm" the award in the Southern District of New York. By that time, however, the purchaser had ceased to exist, and the court dismissed the confirmation proceedings on that basis. The producer appealed both of the district court's dismissals.

No Separate "Confirmation" Step Is Required Before Recognition and Enforcement of Award

In the first of two opinions, on January 18, 2017, the Second Circuit reversed the district court. The Second Circuit held that the producer was not required to "confirm" the award in a step separate from enforcement proceedings. In doing so, the Second Circuit provided important clarification on the process for confirming arbitration awards under the Federal Arbitration Act ("FAA") and the Convention for the Enforcement and Recognition of Foreign Arbitral Awards ("New York Convention"). The Second Circuit's opinion largely tracked the United States' *amicus* brief, whose stated interest was in "ensuring the proper interpretation and implementation" of the New York Convention and "encouraging the reliable and efficient enforcement of international arbitral awards in aid of international commerce." U.S. *amicus* br. at 1.

The Second Circuit explained the nature of the confusion over "confirmation" versus "recognition and enforcement" of awards. Before 1970, when the United States ratified the New York Convention and added Chapter 2 to the FAA to implement the New York Convention, the 1927 Geneva Convention provided the framework for enforcing arbitration awards. Under the Geneva Convention, an award creditor was required to obtain recognition of the award in the state where it was rendered before he could attempt to enforce it abroad. This enforcement regime, known as "double *exequatur*," governed when the Second Circuit issued its 1963 *Orion* decision, on which the district court relied in dismissing the producer's enforcement proceedings.

The addition of Chapter 2 to the FAA in 1970 did not eliminate the confusion over whether double *exequatur* was still required. In fact, as the Second Circuit noted, Chapter 2 of the FAA uses the word "confirm," allowing a party to an arbitration to apply for "an order *confirming* the award." 9 U.S.C. § 207 (emphasis added). And in the same section, the FAA also refers to "recognition" and "enforcement" of awards. *Id.* This may have led to confusion, including in the district court, over the difference between "confirmation," "recognition," and "enforcement" of arbitration awards.

The Second Circuit clarified this situation, holding that the New York Convention, as implemented by Chapter 2 of the FAA, envisions a "single-step process for reducing a foreign arbitral award to a domestic judgment." *CBF v. AMCI*, 2017 U.S. App. LEXIS 3815, at *31 (citation omitted). According to the

Second Circuit, the word "confirm" in Chapter 2 of the FAA should be understood as a synonym of "recognition and enforcement" under the New York Convention. *Id.* at *32. And although "recognition" and "enforcement" are distinct concepts, they "occur together, as one process" under the New York Convention. *Id.* at *31.

This decision is significant because it reduces uncertainty in the enforcement of arbitration awards in the United States (or at least before the courts of the Second Circuit) and allows award creditors to rely on the simpler, single-step procedure under the New York Convention and the FAA. Though the award debtor can still bring a set-aside challenge in the jurisdiction where the award is rendered, the Second Circuit has made clear that confirmation of the award at the seat is not required to recognize and enforce the award under the FAA and the NY Convention.

For the producer, however, this decision did not resolve everything. Though the Second Circuit eliminated any need for pre-enforcement "confirmation," the text of the FAA only provides for enforcement of awards "against any other party to the arbitration." 9 U.S.C. § 207. Since the purchaser—the only "other party to the arbitration"—was bankrupt and nonexistent, the producer wished to enforce the award against third parties, which the bare text of the FAA does not address.

Enforcement of Awards Against Third Parties Is a Matter of Local Law, Not Arbitrability

Having found that separate "confirmation" proceedings were not required, the Second Circuit turned to whether the producer could enforce the award against entities that were not parties to the arbitration agreement or the arbitration award. In its initial opinion, the Second Circuit held that issue preclusion did not apply to the producer's fraud claims, which underpinned its alter ego theories. However, this led to some difficult questions. Was the joining of third parties an issue subject to the parties' arbitration agreement? Or could the producer attempt to enforce the arbitration award against third parties, regardless of the scope of the arbitration agreement?

In its initial opinion, the Second Circuit characterized the question as one of "arbitrability" under the *First Options* line of cases (*First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938 (1995)). The concept of "arbitrability"—and even more so the "arbitrability of arbitrability"—is an especially confusing one, as the Second Circuit framed the inquiry as whether the parties "*agreed to have an arbitrator decide whether they decided to arbitrate* the question of whether a nonsignatory could be bound to an award under the Contracts." *CBF v. AMCI*, 846 F.3d at 54. This left open the possibility that "the district court must refuse to decide the issue" or that "the question must go to the arbitrator," which could have been the end of the case or at least very burdensome for the producer. *Id.*

The Second Circuit cleared up this confusion and uncertainty in a rehearing. Leading up to the rehearing, the New York City Bar Association ("NYC Bar") submitted an *amicus* brief, citing the importance of avoiding confusion or impeding award enforcement "in what may be the United States' most significant enforcement jurisdiction." NYC Bar *amicus* br. at 1. The NYC Bar contended that the *First Options* line of cases, which concerns the intent of an arbitration *agreement*, did not apply to the enforcement of an arbitration *award* that "does not by its terms purport to bind non-signatories to the arbitration agreement." *Id.* at 2. Instead, the NYC Bar contended that the enforceability of an *award* (as opposed to an *agreement*) against third parties "should be determined by legal principles concerning enforcement of awards or judgments under applicable state law, not by New York Convention and Federal Arbitration Act principles concerning the ambit of an arbitration agreement." *Id.* at 3. The NYC Bar also explained that restricting an award creditor's enforcement options according to the arbitration agreement "could invite an award debtor to engage in improper activity with impunity—such as transferring its assets and striking itself from the corporate registry," which was what the purchaser was alleged to have done in this case. *Id.* at 9–10.

The Second Circuit issued a revised opinion, which no longer cites *First Options* or mentions "arbitrability." Instead, the revised opinion provides, simply, that the "sole issue" for the district court on remand is the producer's alter ego theory, to be evaluated under "applicable law in the Southern District of New York." *CBF v. AMCI*, 2017 U.S. App. LEXIS 3815, at *43. The revised opinion is otherwise identical to the initial opinion.

This revised opinion represents an important clarification and simplification of the process for enforcing arbitration awards against third parties. It is now clear that, at least in the courts of the Second Circuit, not only is "confirmation" unnecessary, but once the award is in hand, there is no need to engage in confusing and uncertain analyses of arbitrability in order to determine the targets of all-important enforcement proceedings. Q

Regulatory Litigation Update

Insider Trading in the E.U. and U.S. Markets—An Ocean Apart? With increasing momentum towards global regulatory convergence—driven predominantly by G20 commitments—it is noteworthy that some important (and practically significant) distinctions remain between the market conduct regimes in the U.S. and the E.U.

This article should be of particular interest to those institutions and individuals transacting on U.S. and E.U. listed securities markets—regardless of their physical trading location.

Einhorn/Greenlight. Much has already been written on the *Einhorn/Greenlight* case, which served to highlight certain key differences between the U.S. and E.U. regimes; not to mention the extra-territorial reach of the U.K. regulatory authorities. To briefly re-cap, U.S.-based David Einhorn and his fund, Greenlight, were each convicted of (civil) insider dealing in the shares of Punch Taverns Plc (a UK-listed stock), notwithstanding that all trading was directed from the U.S.. In summary, Einhorn had failed to appreciate that information he had received during a call with Punch and its advisors, in the lead up to an imminent share issuance by the company, amounted to 'inside information.' Greenlight began to dispose of its entire Punch stake only a few minutes following this call. The equity issuance was announced to the market around a week later, whereupon the price of Punch shares fell by almost 30%. Perhaps unsurprisingly, this particular sequence of events prompted a formal regulatory investigation, which culminated in fines exceeding £3.5m for each of Einhorn and Greenlight.

Among other things, Einhorn argued in his defence that the call had been conducted on the express basis and understanding by all concerned that no inside information was to be divulged—a point repeatedly affirmed before and during the call. However, the U.K regulator—adopting a "substance over form"approach—contended that the totality of information provided to Einhorn, when taken in context, in fact amounted to inside information—in particular, the purpose, anticipated size and timing of the proposed issuance; and the fact that other shareholders were broadly supportive, on which Greenlight subsequently traded.

Significantly, despite the Regulator's acceptance that Einhorn did not act deliberately or recklessly, he was nevertheless held to be an "insider" (and therefore culpable) because he *ought to have recognized* his receipt of inside information (even if, in actuality, he did not believe it to be).

Level Informational Playing-Field? The U.S. courts have repeatedly rejected the 'parity of information' doctrine, maintaining that there is *no "general duty between all participants in market transactions to forego actions based on material, non-public information"* (*Chiarella v. United States,* 445 U.S. 222, 233 (1980)). Instead, the scope of the U.S. insider trading offence is limited to situations where the insider had "a duty to disclose arising from a relationship of trust and confidence between the parties to a transaction … A relationship of trust and confidence [exists] between the shareholders of a corporation and those insiders who have obtained confidential information by reason of their position with that corporation. This relationship gives rise to a duty to disclose because of the necessity of preventing a corporate insider from…taking *unfair advantage of the uninformed minority of stockholders*." {our emphasis}

Similarly, a corporate "outsider" can only be liable for insider dealing where (s)he trades in breach of a fiduciary duty—but, importantly, only where such duty is owed to the source of the information. By necessary implication, no duty is considered to be owed to those persons with whom (s)he transacts.

In stark contrast, the E.U. Market Abuse Regulation is fundamentally underpinned by a notion of *information parity and fairness across <u>all</u> market participants*.

In essence, this approach is akin to a general duty between all market participants—of the type expressly rejected by the U.S. courts. Put another way, in the E.U., there is no restrictive pre-condition for the existence and breach of a specific duty—whether owed by the insider to: (i) the issuer or its shareholders; or (ii) the tipper/source of the inside information. This distinction is significant as the U.S. authorities are often faced with an insurmountable hurdle when pursuing alleged market miscreants.

"Personal Benefit" Requirement. The U.S. specific duty requirement has been the subject of numerous *tipper/tippee* cases, in which the issue of *personal benefit* to the tipper was a central consideration in the breach determination. In the seminal *Dirks v. SEC* case, the court held that the "test" for determining whether a breach of duty has occurred is "whether the insider personally will benefit, directly or indirectly, from his disclosure." "Absent some personal gain" by the insider, there has been no breach and thus no duty to refrain from trading.

Exactly what will qualify as a "personal benefit" remains somewhat unclear. Most recently, in December 2016, the Supreme Court (in *Salman v. United* Sates) clarified that a gift to a trading relative or friend may satisfy the "personal benefit" requirement, even if the tipper had no expectation of personal *pecuniary* benefit. Interestingly, however, the Court limited its finding to disclosures to trading friends and relatives, and expressly refused to adopt the Government's contention that a gift to "anyone" should suffice to meet the test—a stance which, had it been upheld, would have served to bring the U.S. regime into closer alignment with that of the E.U..

Other Key Differentials Between the U.S. and U.K. Regimes. There are some other important (and practically significant) distinctions between the U.S. and E.U. insider trading regimes. In summary:

- *Tippee Knowledge.*
  - In the U.S., it is necessary for the authorities to establish that a tippee knew of the tipper's breach: that is, the tippee knew that the information was obtained (by the tipper) in confidence and divulged for personal benefit. In practice, this can prove to be a challenging, if not prohibitive, obstacle for the authorities
  - There is no such positive knowledge requirement in the E.U.. Simply, a tippee who knew or ought to have known that s(he) possessed inside information, and who goes on to use that information, will have committed a *prima facie* offence. The relative ease with which a regulator can assert that a defendant ought to have recognized their receipt of inside information was clearly illustrated in *Einhorn/Greenlight*—highlighting the need for investors to remain constantly vigilant when, for example, interacting directly with listed issuers or receiving market soundings.
- *Insider—Circumstances.*
  - As discussed above, an insider in the U.S. must have acquired the inside information in particular circumstances for liability to attach.
  - There is no equivalent requirement in the E.U.—it is irrelevant how the insider came into possession of the inside information.
- *Insider Knowledge More Generally.*
  - Under the U.S. regime, a defendant can only be liable for insider trading if (s)he acted with a culpable state of mind, commonly referred to as "scienter." The level of scienter required is the only legal difference between a civil and criminal insider trading violation. Broadly, the civil liability standard is a "reckless disregard" / "highly unreasonable" conduct; while under the criminal regime, the defendant must act willfully.
  - There is no equivalent "intent" requirement under the civil regime in the E.U.. Therefore, a genuinely ignorant defendant or one who failed to apply his mind can still have committed an offence in the E.U..
- *Liability for Improper Disclosure of Inside Information.*
  - In the E.U., it is an offence to unlawfully disclose inside information other than in the normal course of the exercise of a person's employment, profession or duties. In contrast to the U.S. position, there is no need for the recipient to have traded following receipt of the inside information. Nor is there a requirement for the insider to have received a personal benefit in order to be liable for unlawful disclosure.
- *Encouraging Offence:*
  - The recommendation or inducement of another to engage in insider dealing will, in and of itself, constitute market abuse in the E.U.—irrespective of whether the other person follows through. There is no direct U.S. equivalent.

Conclusion. As illustrated, the E.U. market conduct regime is, in various respects, markedly broader in scope and application (and commensurately easier to violate) than the U.S. equivalent. US-based investment professionals and other market participants transacting on E.U. securities markets must remain continually alert to these differences. Ignorance will not afford a defense under the E.U. regime—as David Einhorn famously discovered to his considerable cost.

International Trade Update

Quinn Emanuel Introduces Programs to Assist Clients with International Regulatory Matters

Conducting business internationally is as rewarding as it is complex. Utilizing *Complementarity Analysis*™, members of Quinn Emanuel's International Trade Litigation and Policy Practice Group help clients navigate the myriad obstacles facing global operations by providing expert, discrete counsel on how to harmonize business models with local regulations, politics, customs, and traditions to leverage economic, supply chain and regulatory policy efficiencies. Companies which can benefit from these services include those that source, grow or produce products subject to international trade agreement protocols like SPS (Sanitary & Phyto-Sanitary), IPR (Intellectual Property), Trade in Services, ROO (Rules of Origin) and the valuation methodologies related to the ROO; manufacture products with inputs subject to export or import control requirements; and, companies that operate in restricted technology or defense related industries.

For example, an unforeseen change in the regulatory classification of certain fungicides used in leather treatment surfaced in sideline discussions during bilateral trade meetings between the US and a trading partner. The cost to a leather manufacturing company and the timing of the reclassification could have had a negative impact on the company's to meet customer requirements and the company's bottom line. Since the issue was flagged early in bilateral trade discussions, there was time to explore formal trade dispute remedies with government officials as well as identify alternatives and substitutes, request public comment periods, and require a reasonable implementation period of new regulations to accommodate alternative solutions. Leveraging our experienced as trade litigators, senior trade officials and political advisors, we are able to anticipate issues, provide clients with diverse options and craft solutions.

We work successfully across multiple disciplines including legal, regulatory and diplomatic to protect client's interests. Recently, we quickly worked to confront and reverse a foreign government sponsored legal action that targeted an affiliate of a US-based parent corporation. We uncovered the underlying motivation for the initiation of a baseless action whilst simultaneously protecting the client's affiliate in the court. Working through our diplomatic channels and with local legal partners, we ensured that the case was withdrawn. In another part of the world, working with our local staff and through legal and diplomatic channels, without incident or media attention, we secured and protected a client's critical database servers from extraction by local state-owned ventures. Our decades of legal experience inform the design and implementation of these programs to ensure our clients' interests are aligned not only with US law but also with local and international institutions.

Our system of Complementarity Analysis™ begins where the numbers end, defining and analyzing observable criteria and critical intangibles. These necessary but distinct disciplines help to insure alignment between our clients' strategic goals and the means implemented to achieve them.

Comprehensive International Trade and Customs Assessments and Audits. Our international trade and customs lawyers conduct thorough review and efficiency assessments of company internal protocols, policies and practices relating to the flow of trade, movement of capital, and the protection of intellectual property. We review and assess client operations worldwide for compliance with local, regional and international customs practices and regulations and to increase efficiencies with respect to customs valuation, world customs classification and current and projected rate of duties. We review production and/or sourcing origin and anticipate any alteration to existing bilateral, regional or plurilateral trade agreements that could impact where a client sources or produces product. For example, this process has successfully produced for clients streamlined supply chain logistics that saved millions of dollars each year by identifying new beneficial changes in trade arrangements and free trade agreements, identified valuation issues, and the created and integrated a international trade tracking system into a client's business dashboard to monitor real-time fluctuations and ratios of imports to monitor and respond to pricing changes.

Our lawyers possess the experience, judgment and skill to develop multi-disciplined, company-specific *PAIR™ Programs - Plan Anticipate Integrate Respond*—our global life, safety, property preservation and business continuity programs for international operations are launched in close cooperation with internal personnel and external interlocutors. While these strategies and programs ideally should be designed with clients well before an unforeseen lawsuit or crisis unfolds, we are experienced in addressing and solving the immediate challenge. In emerging economies, under exigent circumstances, working with strategic local assets, our lawyers have designed and executed local programs and strategies to protect personnel, mission critical data systems and the client's global brand as the crisis manifests itself.

In addition to assessing and remediating clients' systems and internal protocols, our lawyers support clients to generate sustainable stakeholder engagement, utilizing proven advocacy and communications techniques that result in durable strategic alliances. We have prepared senior executives for congressional hearings and investigations, drafted testimony and corporate press statements, interfaced with local regulators and the diplomatic corps to extricate a client from retaliatory and politically motivated trade litigation, and designed and successfully implemented legislative strategies, creating unconventional political alliances to produce the first change in US trade remedies and enforcement laws in nearly forty years. Our lawyers are not only litigators, they have served in senior posts in government, the political arena, NGOs and international trade and economic organizations and possess multi-disciplined skillsets to deliver results inside and outside the courtroom.

While well-respected and feared for our litigation prowess, our lawyers are also trusted advisors who protect a client's bottom line.

Entertainment Litigation Update

Ninth Circuit Confirms That "Volitional Conduct" Is Still Required for Direct Copyright Infringement Post-**Aereo.** Earlier this year, in *Perfect 10, Inc. v. Giganews, Inc.*, 847 F.3d 657 (2017), the Ninth Circuit re-affirmed that a defendant must engage in "volitional conduct" in order to be liable for direct copyright infringement. The Supreme Court's decision in *American Broadcasting Companies, Inc. v. Aereo, Inc.*, 134 S.Ct. 2498 (2014), had cast considerable doubt whether volitional conduct was still required, raising questions concerning potential copyright liability for emerging technologies such as cloud computing.

In *Aereo*, the Supreme Court considered whether Aereo "performed" television broadcasters' copyrighted works when it streamed television programs to its subscribers over the Internet, and was thus subject to liability for direct copyright infringement. Even though Aereo's streaming system was "inert until a subscriber indicates that she wants to watch a program," and its "equipment simply respond[ed] to its subscribers' directives,"—suggesting the absence of volitional conduct—the Court nonetheless held that Aereo "performed" the copyrighted works within the meaning of the Copyright Act's Transmit Clause. 17 U.S.C. § 101; *Aereo*, 134 S. Ct. at 2507. In dissent, Justice Scalia argued that the majority's holding was inconsistent with the volitional-conduct requirement—a requirement adopted by "[e]very Court of Appeals to have considered an automated-service provider's direct liability for copyright infringement"—and that this requirement "demands conduct directed to the plaintiff's copyrighted material." 134 S.Ct. at 2512-13 (Scalia, J., dissenting). Justice Scalia maintained that "Aereo does not 'perform' for the sole and simple reason that it does not make the choice of content," and noted the possibility that the Court's holding could "imperil billions of dollars of investments in cloud-storage services." *Id.* at 2514, 2518.

Against this backdrop, the Ninth Circuit decided *Perfect 10*. Perfect 10 owns copyrights in several thousand adult images shared over the Usenet, a collection of online bulletin boards (called "newsgroups") that allow users to post and respond to messages and share content. Giganews provides users with access to the Usenet, and owns and operates Usenet servers, which store the content uploaded by users. Perfect 10 brought several claims against Giganews, including direct copyright infringement on the theories that 1) Giganews displayed Perfect 10's images to users through its browser application; 2) Giganews distributed Perfect 10's images by delivering downloadable content to users; and 3) Giganews directly copied and stored Perfect 10's images. The district court dismissed the first two theories at the pleadings stage, and the third at summary judgment, all on the ground that Perfect 10 failed to allege (or prove) that Giganews engaged in any volitional conduct directed towards Perfect 10's copyrighted images. The district court also awarded Giganews $5.6 million in attorney's fees.

On appeal, the Ninth Circuit first held that the volitional conduct requirement remains an element of a direct copyright infringement claim post-*Aereo*, clarifying that "volitional conduct" is "a basic requirement of causation" such that "direct liability must be premised on conduct that can reasonably be described as the direct cause of the infringement." 847 F.3d at 666. The court reasoned, *first*, that *Aereo* did not expressly address the volitional conduct requirement, and that the Supreme Court was unlikely to have abandoned by implication a requirement that had been adopted by several Courts of Appeals. The Ninth Circuit reasoned, *second*, that the Supreme Court's analysis in *Aereo* was actually consistent with the volitional conduct requirement, because the Supreme Court had distinguished Aereo's conduct from conduct of an entity that "merely supplies equipment that allows others' to perform or transmit."

After concluding that the volitional conduct requirement is consistent with *Aereo*, the Ninth Circuit affirmed the district court's determination that Perfect 10 had not established volitional conduct with respect to any theory of direct copyright infringement it advanced against Giganews. The court held that 1) Giganews' display and storage of Perfect 10's copyrighted images was passive; 2) Giganews' "distribution" of Perfect 10's images was automatic and thus attributable to the user, not any active conduct by Giganews; and 3) Perfect 10 failed to present evidence that Giganews exercised control over Usenet content, actively chose any material for transmission, "or instigated any copying, storage, or distribution." 847 F.3d at 670.

In the context of business litigation, the Ninth Circuit's determination in *Perfect 10* that volitional conduct is still required and that Giganews had not engaged in any volitional conduct as a passive provider, should offer some clarity for online service providers generally, whose liability for copyright infringement was called into question by *Aereo*. In particular, *Perfect 10* seems to make it less likely that, cloud computing network providers and businesses generally reliant on cloud data storage will be subject to liability for direct copyright infringement. However, because the *Aereo*-majority declined to address the volitional conduct requirement (notwithstanding the dissent's claim that the volitional conduct requirement mandated a contrary result), it is possible that the panel's conclusion in *Perfect 10* will be tested. Indeed, as of this writing, Perfect 10 petitioned the Ninth Circuit for rehearing *en banc*, arguing, among other things, that the panel's opinion conflicts with *Aereo*. Whether Perfect 10 will continue to pursue its appeal is unclear—after Perfect 10's rehearing petition was filed, the district court granted Giganews' motion for appointment of a receiver. The receiver will begin the process of liquidating Perfect 10's intellectual property in order to satisfy Giganews' attorney's fee award.

Structured Finance Victory

On March 9, 2017, in matter of first impression, New York's First Department appellate court ruled that Quinn Emanuel's client Computershare Trust Company had standing to bring suit on behalf of a residential mortgage-backed securitization trust, even though Computershare is not the trustee. Computershare, acting as the trust's separate Securities Administrator had filed a complaint in New York's Supreme Court against the trust's sponsor, Natixis Real Estate Capital, for breaches of representations and warranties relating to the quality of the mortgage loans Natixis sold to the trust. Natixis moved to dismiss the complaint, arguing that Computershare lacked standing to sue and only a trustee could bring suit on behalf of a trust. Natixis also sought to dismiss on other grounds, including that the complaint was not timely and that the claims were not ripe. Justice Friedman of the Supreme Court denied Natixis's motion to dismiss, holding the Securities Administrator had standing and rejecting Natixis's timeliness and ripeness arguments.

The New York Appellate Division, First Department, affirmed Justice Friedman's ruling, holding that entities other than trustees may bring breach of warranty claims on behalf of a securitization trust, hence the Securities Administrator had standing. The court rejected Natixis's argument that only a trustee may bring suit on behalf of a securitization trust, and held that, under New York law, the Securities Administrator did not need to have been delegated the power to bring suit by the trustee because the operative trust document gave the Securities Administrator that power directly. The Court also rejected Natixis's argument that a contractual provision requiring the Securities Administrator to act when so directed by the trust's depositor deprived the Administrator of the power to act on its own initiative under a separate provision. The First Department also affirmed the court's decisions that the complaint was timely and the claims were ripe.

This decision created valuable new precedent in the First Department that mortgage securitization trust documents granting enforcement powers to non-trustees are valid, and that such non-trustees may enforce the contractual rights of securitization trusts. This ruling should give parties creating mortgage securitization trusts more flexibility in allocating power to enforce the trust's legal rights in court and streamline the ability of appropriate non-trustees to bring such enforcement actions.

ITC Victory for SawStop

The firm recently secured a complete victory in the U.S. International Trade Commission on behalf of our client, SawStop, LLC, in a bet-the-company case.

In 1999, Dr. Stephen Gass, a physicist and IP lawyer, patented a revolutionary active safety technology for use in table saws. Using electronics and software to detect contact between a user and the spinning saw blade, the invention quickly fires a brake that stops the blade's rotation within milliseconds, leaving the user with at most a superficial scratch. The reaction to his invention was phenomenal; woodworking groups, trade shows, safety advocates, and even the Consumer Product Safety Commission praised Dr. Gass's invention.

Dr. Gass sought to license his technology to existing power tool manufacturers, but each declined because of product liability concerns. Still believing in the promise of the technology, Dr. Gass and colleagues raised money from friends and family and designed and built their own table saws under the SawStop brand. Between 2005 and 2015, SawStop grew from five employees working out of a barn in Oregon to become the leading cabinet saw manufacturer in the United States. Throughout, SawStop offered the only saw on the market with active safety technology.

In March 2015, however, Robert Bosch Tool Corporation and Robert Bosch GmbH ("Bosch") announced plans to bring its own version of the technology to market. Prior to Bosch's launch, SawStop turned to Quinn Emanuel to file a complaint for patent infringement in the ITC, with the hope of securing an exclusion order barring imports of Bosch's infringing table saw. Quinn Emanuel ensured that our client's hope was fulfilled.

Using press releases and cell phone videos shot at trade-show demonstrations of Bosch's prototype, Quinn Emanuel pieced together enough evidence about Bosch's new product to draft a complaint months before Bosch's product was publicly released. As soon as the ITC instituted the investigation, Quinn Emanuel took targeted discovery and depositions to prove up its infringement case, and gathered the evidence of "secondary considerations"—that SawStop's patented technology was groundbreaking, unbelievably effective, and a huge commercial success—that would help SawStop show that its patents were valid and infringed. Quinn Emanuel then litigated its way through the initial claim construction hearing and two rounds of supplemental claim construction briefing, after which the ITC's judge settled on proposed constructions of disputed claim terms that were highly favorable to

SawStop.

After a one-week trial, the ALJ ruled in SawStop's favor, issuing a 150-page opinion that Bosch had infringed two of SawStop's patents, and that SawStop's patents were not invalid. The ALJ recommended that the Commission issue an order excluding Bosch's active safety technology from the U.S. market. On January 27, 2017, the Commission agreed with the ALJ, issuing an exclusion order blocking Bosch from importing the infringing products, and a cease and desist order preventing Bosch from selling any infringing products it had already imported into the U.S.

As a result of Quinn Emanuel's work, Bosch's rollout of infringing products has been halted, SawStop will maintain its strong market position, and power tool users nationwide will continue to benefit from SawStop's active safety technology. Q

(lead article continued from page 9)

Additionally, Section 101(a) of the NAFTA Act, which deals with Congress's approval of NAFTA, would cease to operate as a result of Section 109(b) of the NAFTA Act and, as a result, Congress's approval over NAFTA would no longer have any legal effect.

Withdrawal from NAFTA could have significant consequences for U.S. investors with investment disputes against Mexico/Canada or vice versa. In addition to doing away with the substantive protections and the dispute resolution mechanism afforded to investors under Chapter 11, withdrawal from NAFTA also would have practical implications for investors who have live disputes against one of the member states. Specifically, U.S. withdrawal would create serious time constraints for investors wishing to submit investment disputes to arbitration. A plain reading of NAFTA Article 2205 suggests that investors could bring new claims only during the six months between the notice of withdrawal and the date it becomes effective. NAFTA Article 1119, further complicates an investor's right to submit claims to arbitration, as it requires submission of written notice of intent to submit a claim to arbitration at least 90 days before the claim is presented. This considerable time crunch is further complicated by NAFTA Article 1137, which provides that a claim formally is submitted to arbitration when the request for arbitration (a document more complex than the notice of intent and akin to a complaint) has been *received* by the Secretary-General under the ICSID Convention or the ICSID Additional Facility Rules, or when the notice of arbitration (the analogue to the request for arbitration) has been *received* by the disputing party under the UNCITRAL Arbitration Rules.

The importance of the foregoing is enhanced by the fact that, unlike most other investment protection agreements that typically guarantee investment protections for 10 to 15 years after the instrument has been terminated, NAFTA does not include any such provision. Thus, once the six month period is up, an investor who relied on the dispute settlement provisions and the substantive protections of NAFTA may be left without recourse other than suing the host country in domestic courts, with the usual sovereign immunity and other complications that usually come with suing a sovereign in its own courts.

Investors with already pending claims, however, should not be concerned about the possibility of the United States' withdrawal, since their claims have already been perfected. It is a well-established principle of international law and treaty interpretation that withdrawal from an international instrument cannot have retroactive effects on pending proceedings. For example, cases initiated against Ecuador before the notice of denunciation of the ICSID Convention continued even after Ecuador's denunciation had taken effect (*Occidental Petroleum Corporation and Occidental Exploration and Production Company v. Republic of Ecuador,* ICSID Case No. ARB/06/11, Decision on Jurisdiction, (Sep. 9, 2008); *Burlington Resources, Inc. v. Republic of Ecuador*, ICSID Case No. ARB/08/5; *Corporación Quiport S.A. and others v. Republic of Ecuador*, ICSID Case No. ARB/09/2; *Murphy Exploration and Production Company International v. Republic of Ecuador,* ICSID Case No. ARB/08/4; *Repsol YPF Ecuador, S.A. and others v. Republic of Ecuador and Empresa Estatal Petróleos del Ecuador (PetroEcuador),* ICSID Case No. ARB/08/10). Likewise, cases brought against Venezuela following its denunciation of the ICSID Convention also continued after the denunciation had taken effect (*Venoklim Holding B.V. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/12/22)). Q

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business litigation report

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