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## Quinn Emanuel Hosts Chinese Mock Trial Event Amid Changing Patent Landscape

The firm recently hosted a live demonstration of a Chinese patent trial in a first-of-its-kind event in San Francisco. The mock trial, which was conducted by attorneys from the Zhong Lun law firm, showcased a Chinese patent case in which a foreign company sought to enforce its patents in China. Former Judge Yi Zhang of China presided over the mock trial, which was conducted in Mandarin with simultaneous English translation. The demonstration was followed by a discussion among a panel of Quinn Emanuel and Zhong Lun attorneys.

“As far as we know, there has never been an event like this in the United States,” said Quinn

Emanuel partner Mark Tung, who co-hosted the event along with partners from four different offices in the United States and China. “This was a unique opportunity, because United States attorneys are not even allowed into Chinese courtrooms to observe, let alone participate in, legal proceedings in China,” Tung added.

Xiao Liu, who recently joined Quinn Emanuel as a partner in its Shanghai office, also participated. “More and more, companies based in the United States and around the world are looking to China as a critical forum, often as part of an international patent enforcement strategy. We wanted to show them

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## Leading Patent Litigator James Pak Joins Los Angeles Office

James Pak has joined the firm as a partner in the Los Angeles office. Pak is an experienced patent litigator and trial lawyer who has won significant victories in jury trials and U.S. International Trade Commission proceedings. He has represented clients in the wireless telecommunication and automotive industries and in matters relating to Standard Essential Patents and FRAND obligations, earning him a recognition as a leading practitioner in licensing. He is fluent in Korean and works extensively with clients in both Korea and Japan. [Q](#)

## Isabelle Michou Receives Global Arbitration Review Award

Isabelle Michou received the award for the *2018 Most Important Decision* in international arbitration at the Global Arbitration Review (GAR) Live annual awards, in recognition of last year's final ICSID arbitral award in *UP and CD Holding v Hungary*. Isabelle led a team that recovered all claimed damages on behalf of UP and CD Holding, whose investment had been expropriated by Hungary in violation of an intra-EU Bilateral Investment Treaty (BIT). This was a landmark victory because it was the first time an ICSID arbitral tribunal confirmed that the controversial ruling of the European Court of Justice in *Achmea v Slovakia* (that arbitrators should decline jurisdiction over such intra-EU BIT disputes) did not apply to ICSID arbitration. [Q](#)


## The American Lawyer Names Shon Morgan “Litigator of the Week”

Shon Morgan was named the “Litigator of the Week” by *The American Lawyer* after persuading an *en banc* panel of the 9th Circuit to overturn a class action ruling against Hyundai and Kia. The victory stemmed from a settlement resolving more than 50 class actions in a MDL related to errors in the automakers' fuel economy ratings. A Ninth Circuit panel had vacated the settlement, which the *en banc* ruling reinstated. Morgan states that the *en banc* court's decision “provides perhaps the clearest statement from any federal court on how the Rule 23 standards apply differently to a settlement class than a contested litigation class.” [Q](#)

what litigating in China is like, because an improved understanding can help guide strategy in future cases,” Liu added. The event was a novel experience even for lawyers whose practice is based in China. “We often cooperate with Quinn Emanuel in cross-border disputes,” said Ping Gu, a partner at Zhong Lun, “and we were very happy to participate in this event and shed light on the Chinese system for a new audience.”

The mock trial involved a simulated dispute in which a foreign company sought to enforce its Chinese patent for a spindle motor. It was based on an actual case that was recently litigated in China. The demonstration included opening statements, evidence presentation, direct and cross examination of witnesses, and legal argument. The three-judge panel included former Chinese Judge Yi Zhang presiding as Chief Judge, a former Chinese patent examiner, and Quinn Emanuel

partner Mark Tung, whose practice frequently involves China-based companies or disputes. As in Chinese courts, the mock trial featured frequent back-and-forth between the attorneys and the panel of judges as they worked through each side’s claim construction and infringement analysis. Ultimately, the foreign patentee in the mock trial succeeded on its infringement claim, as the foreign patentee had in the real case.

This event was conducted against the backdrop of a quickly changing and drastically expanding patent system in China. As China continues to develop its patent system, companies doing business in China must be aware of how it operates and what remedies are available against infringers. See *Understanding the Unique Features of China’s Rapidly Expanding Patent System*, directly below. 

## Understanding the Unique Features of China’s Rapidly Expanding Patent System

China is probably now the third most important (after the United States and Germany) venue for patent prosecution and enforcement, and it is critical for companies doing business there to understand how the system works. Patent applications in China have exploded in recent years. In 2018, approximately 1.54 million patent applications were filed with the recently renamed and restructured China National Intellectual Property Administration (“CNIPA”), formerly the State Intellectual Property Office. This was a year-over-year increase of 11.6%, and was by far the most applications filed in any country in the world. The United States Patent and Trademark Office, by comparison, received approximately 640,000 applications in 2018. And while the number of patent applications has remained relatively steady in the United States in recent years, China has seen a 50% increase in just the last four years.

A significant increase in patent litigation in China has followed. Civil patent lawsuit filings in China increased 30% between 2016 and 2017 to over 16,000, exceeding United States patent lawsuits by fourfold. And while Chinese patents themselves share many similarities with their U.S. counterparts, the patent litigation systems have a number of important differences.

***There Are Different Processes for Obtaining Different Types of Patents.*** China has a first-to-file system for three types of patents: invention, utility model, and design. An invention patent in China is valid for 20 years from filing; the application and review process typically takes three to five years; and issuance is subject to requirements of novelty, inventiveness, and practical application. Chinese utility model patents, which last ten years, protect new technical solutions

relating to a product’s shape, structure or a combination thereof. But they *are not* substantively examined before issuance, *i.e.*, they are not compared against prior art, and are usually granted within eighteen months of the application. Design patents in China cover the original appearance of a manufactured product and currently last ten years, but this could increase to fifteen years upon the passage of draft amendments to China’s patent laws, which are expected to go into effect by the end of this year. All three types of Chinese patents protect against manufacture, use (not applicable for design), offer for sale, sale, and importation of the patented item.

***Jurisdiction in Patent Litigation Is Based on the Defendant’s Domicile.*** Patent infringement suits must be filed in the court where the infringer is domiciled or where the infringement occurred. Because some courts located outside of major cities are less predictable, plaintiffs often include as defendants distributors and/or other related parties based in major cities. The statute of limitations for an infringement claim in China is two years from when the plaintiff knew of or should have known of the infringement, compared to six years in the United States.

There are four levels of courts in China (in ascending order of authority): the Local People’s Court, the Intermediate People’s Court, the Higher People’s Court, and the Supreme People’s Court. Until a few years ago, most patent infringement suits were heard by the Intermediate and Local People’s Courts. Today, most are heard by specialized intellectual property courts based in major cities like Beijing, Shanghai, and Guangzhou, as well as regional IP tribunals located in cities such as Nanjing, Suzhou, and Chengdu. Similar to Germany,

China has a split patent litigation system in which courts make infringement determinations, but invalidity challenges are heard in the first instance by the CNIPA, often in parallel proceedings with infringement suits.

**Discovery Is Very Limited.** Perhaps the most obvious and significant difference between patent litigation in China as opposed to the U.S. is the near-total absence of compulsory discovery and the narrow rules of admissibility. Courts may, in their discretion, undertake their own evidence collection or order the parties to engage in discovery, though it is uncommon. As a result, plaintiffs often need to build much of their cases on evidence obtained through private investigators, which means they need to be careful not to violate China's data privacy laws—which could render the evidence inadmissible and subject the plaintiffs to criminal liability.

There are signs, though, that courts in China are becoming more willing to order the preservation and disclosure of relevant evidence, though the burden to obtain such an order often remains high and the party seeking the order is typically required to post a bond. Once obtained, an evidence preservation order could allow for a party to be questioned, its premises to be inspected, or the production of documents and samples of the allegedly infringing products.

The use of experts is limited as well. Although courts in some instances may allow the parties to present expert witness testimony at trial, courts more commonly use their own expert witnesses. Even when courts do allow party experts in addition to court-appointed experts, testimony from the court-appointed experts is given far more weight.

**Claim Construction Occurs at Trial.** Unlike United States courts, Chinese courts conduct claim construction at trial rather than in a pretrial hearing. Completely new inventions are entitled to broader interpretation of claims, whereas improvement patent claims are construed more narrowly. Claims are also subject to prosecution history estoppel, whereby any ground surrendered during patent application (prosecution) is completely barred and the patent holder cannot assert that the patent covers the surrendered ground. This is stricter than in the United States, where only those changes linked to patentability are irrevocably surrendered.

**Injunctions Are Common but Monetary Remedies May Be More Limited.** Successful plaintiffs in Chinese patent litigation will normally be awarded a permanent injunction and monetary damages. The relative ease of obtaining an injunction in Chinese patent litigation is a major factor driving patent actions filed against infringers, particularly competitors. However, monetary remedies are typically much less than those in U.S. patent

litigation. Currently, courts award monetary damages based on actual losses to the patent holder, disgorgement of the infringer's profit, the equivalent of a reasonable license fee, or statutory damages at the court's discretion between RMB 10,000 and RMB 1,000,000 (between approximately 1,400 and 140,000 US dollars). In practice, it is often difficult to obtain evidence of actual losses and the infringer's profit, and thus, parties often receive licensing fees or statutory damages that are far less than the damages that could be available in the United States. Successful plaintiffs are sometimes awarded court fees, but attorney's fees are usually only awarded in cases where the defendant's conduct was egregious.

Upcoming expected reforms to China's patent system will significantly increase the amount of monetary damages available to successful plaintiffs by (i) reducing plaintiff's burden of proving damages where the relevant documents and evidence are primarily in the possession of the defendant infringer, (ii) increasing the maximum statutory damage to RMB 5,000,000 (approximately 720,000 US dollars), and (iii) allowing the recovery of punitive damages in exceptional cases.

While Chinese courts are authorized to issue preliminary injunctions in patent infringement cases, in practice these are very difficult to obtain, largely because of the difficulty of obtaining early discovery (including expert discovery) to establish the necessary elements of infringement and irreparable harm. In considering whether to grant a preliminary injunction, Chinese courts weigh four factors that track the factors United States courts consider: (i) the likelihood of the plaintiff proving its patent was infringed, (ii) whether the patent holder will be irreparably harmed in a manner for which monetary damages are inadequate compensation if the infringing act is not enjoined, (iii) whether the patent holder has provided an adequate bond, and (iv) whether issuance of a preliminary injunction would prejudice the public interest.

**Courts Cannot Invalidate Patents.** Unlike in the United States, civil courts in China cannot invalidate a patent. Although patent invalidity is available as a defense in an infringement proceeding, only the CNIPA—the patent-issuing government body—has authority to invalidate a patent. A patent invalidation proceeding may be initiated by any interested party who files a petition to invalidate with the Chinese Patent Reexamination Board (“PRB”) of the CNIPA, including by a defendant after civil patent litigation has commenced.

The PRB can invalidate patents for many reasons, including lack of novelty, lack of inventiveness (similar to obviousness in the United States), insufficient disclosure to the CNIPA during the application process, and indefiniteness of claims. Procedurally, after a party


submits a petition for invalidation, the parties exchange briefing and the PRB decides whether to hold an invalidity proceeding. Oral hearings are typically granted upon either party's request. The PRB ultimately renders a decision of validity, partial-validity, or invalidity. PRB proceedings normally take between six months and two years, and decisions may be appealed to the Beijing IP Court in the first instance and then to an Intellectual Property Rights Court for Appeals, which is akin to the Federal Circuit in the United States.

#### ***Administrative Patent Infringement Proceedings.***

In addition to the infringement suits in civil court summarized above, patent-holders in China can also bring an administrative action before a local Intellectual Property Office ("IPO"). These proceedings have advantages and disadvantages relative to typical civil proceedings. A local IPO can issue fines and permanent injunctions, but damages are rarely available in the proceedings and the fines are usually too small to seriously deter infringement. Local IPOs may also lack the necessary expertise to assess technically complex patents, and thus may be reluctant to find infringement.

On the other hand, these administrative actions are usually much quicker than civil litigation, often reaching completion in three to four months. Even more beneficial to patent-holders, though, is that once the patent-holder initiates a suit with evidence showing likelihood of infringement, the local IPO is empowered to conduct its own investigation, including performing on-site inspections and seizing sample products for technical evaluation. This process can be extremely useful for a plaintiff because the record created by an IPO investigation can be used in later civil litigation, as plaintiffs may file a follow-on civil suit on the same patent regardless whether the local IPO finds infringement.

\* \* \*

Chinese patent law continues to evolve and is becoming an ever more important part of intellectual property litigation. Companies seeking to protect their patent portfolios worldwide, or who have been accused of infringement, are increasingly likely to see Chinese litigation feature prominently in their disputes. 

## NOTED WITH INTEREST

### **Legal Challenges to CFIUS Reviews**

On August 13, 2018, President Trump signed into law the Foreign Investment Risk Review Modernization Act ("FIRRMA"), which had received overwhelming bipartisan support in both houses of Congress. FIRRMA expanded the authority of the Committee on Foreign Investment in the United States, or CFIUS, to review (and potentially block) foreign investments in U.S. companies that are deemed to pose a threat to national security—a standard that remains vaguely defined. Even before FIRRMA, CFIUS had broad powers; its reviews constituted a substantial hurdle for transnational deals in a wide range of industries, such as telecommunications, integrated circuits, and payment systems. Perhaps most notably, on March 12, 2018 President Trump—acting on a recommendation by the CFIUS—prohibited Singapore-based Broadcom's proposed acquisition of U.S.-based Qualcomm on national security grounds. With FIRRMA expanding CFIUS's authority even more, and with the President seeming to take a broader view of what could pose a threat to national security, U.S. companies seeking international investments face an increased risk that potential transactions will be blocked—with limited legal options to challenge those decisions.

***The History and Background of the CFIUS.*** The CFIUS is an interagency committee authorized to review certain transactions involving foreign investment in the United States, in order to determine the effect of such transactions on U.S. national security. This authority is provided under section 721 to the Defense Production Act of 1950, as amended in the Exon-Florio amendment in 1988. Congress passed the Exon-Florio amendment in response to a rise in foreign—in particular, Japanese—acquisitions of U.S. technology companies.

The composition of the CFIUS has changed over time, but it is currently made up of the heads of the Departments of Treasury, Justice, Homeland Security, Commerce, Defense, State, and Energy, along with representatives from the Office of U.S. Trade and the Office of Science & Technology Policy. Other executive branch offices observe and participate in the CFIUS, including the Office of Management & Budget, the Council of Economic Advisors, the National Security Council, the National Economic Council, and the Homeland Security Council.

The Exon-Florio amendment granted the President the authority to block foreign acquisitions of companies engaged "in interstate commerce in the United States" that pose a risk to national security. To block a foreign



acquisition, the President must conclude that other U.S. laws are inadequate to protect national security, and determine that there is “credible evidence” that the foreign acquirer might take action that threatens to impair U.S. national security. Significantly, the statute also states that the President’s decision to suspend or prohibit a transaction is “not subject to judicial review.”

Despite the Exon-Florio amendment’s grant of virtually unchecked power to block foreign acquisitions of U.S. companies, presidents have rarely exercised that power. Until 2011, President George H.W. Bush was the only president to block a deal. However, starting with President Obama, who vetoed two deals involving Chinese acquirers, the CFIUS has not shied away from investigating transactions involving foreign companies and investors—in particular, from China. And in his first two-and-a-half years in office, President Trump has already blocked three deals, two of which involved Chinese firms. With FIRRMA’s enactment last year, CFIUS’s and the President’s power to block investments from foreign investors has expanded even more.

One of the reasons that historically presidents have only rarely used their powers to formally block transactions is that the CFIUS typically enters into mitigation agreements with transacting parties to alleviate potential national security concerns. For instance, the parties may agree to allow foreign persons only limited or no access to sensitive documents or information bearing on national security, or agree to allow the U.S. government the right to review and approve certain business decisions. Thus, historically, even if the CFIUS determined that an acquisition threatened to impair national security, the CFIUS and the parties could usually find a way to mitigate that threat and still close the transaction. But another reason presidents have rarely used their powers is that transacting parties often preemptively withdraw from scrutinized transactions based on feedback they receive from the CFIUS, thus mooted the need for presidential action.

**Challenging CFIUS Determinations.** The Exon-Florio amendment provides that Presidential decisions to suspend or prohibit deals are “not subject to judicial review.” Accordingly, the options to appeal any adverse rulings emerging from a CFIUS review are severely limited. FIRRMA further restricts the ability to challenge CFIUS orders by mandating that any legal challenges be filed in the United States Court of Appeals for the District of Columbia Circuit. To date, no such suits have been initiated under FIRRMA. In fact, since passage of the Exon-Florio amendment, only one company has ever gone to court to challenge a CFIUS review. *See Ralls Corp. v. Comm. on Foreign Inv. in U.S.*, 758 F.3d 296 (D.C. Cir. 2014).

*Ralls* involved a Chinese-owned company, Ralls

Corporation (“Ralls”), that in 2012 sought to acquire a wind-farm project in north-central Oregon. The transaction caught the attention of the CFIUS because the wind-farm was located near a U.S. Navy weapons systems training facility. *Id.* at 304-05. The CFIUS issued orders mandating interim mitigation measures (preventing Ralls from building the wind farms during the pendency of CFIUS review, and ordering the removal of all items from the project sites, including concrete foundations), and President Obama followed up with an executive order formally blocking the deal. *Id.* at 305-06.

Ralls brought suit challenging both the CFIUS order and the Presidential veto. The District Court for the District of Columbia dismissed the case on jurisdictional grounds, but on appeal the D.C. Circuit reversed and remanded. The Court of Appeals confirmed that Ralls could not challenge the merits of the President’s determination that the transaction at issue posed a national security threat. *Id.* at 311. However, the Court did hold that the presidential veto deprived Ralls of constitutionally protected property interests without procedural due process, because the government did not provide Ralls with advance notice, access to the unclassified evidence supporting the decision, and an opportunity to rebut that evidence. *Id.* at 319-21. The Court of Appeals also remanded the matter to the District Court to assess on the merits the lawfulness of the CFIUS’s orders mandating interim mitigation measures. *Id.* at 325. The parties settled before the District Court ruled on whether the CFIUS exceeded its authority and violated Ralls’ due process by “effectively prohibiting” the transaction (which only the President has authority to do).

*Ralls* illustrates that even before FIRRMA, parties to potential international investment transactions faced severe hurdles in challenging an interim CFIUS order, much less a presidential blocking order. Even if a court rules that the CFIUS exceeded its authority in ordering interim mitigation measures (or in recommending that the transaction be prohibited), once the CFIUS refers the matter to the President, he or she can issue an order blocking the deal that is non-appealable.

**Recent Enforcement Trends.** Under the Trump Administration, the CFIUS has stepped up its efforts to scrutinize acquisitions made by Asian companies, and especially Chinese companies, on national security grounds. In 2017, for instance, President Trump blocked the Chinese investment firm Canyon Bridge Capital Partners from acquiring U.S. chipmaker Lattice Semiconductor Corp., finding that the transaction “pose[d] a risk to the national security of the United States that cannot be resolved through mitigation.” A year later, the President blocked Singapore-based Broadcom’s acquisition of Qualcomm over concerns that Broadcom’s influence over Qualcomm’s development of 5G technology posed a risk to U.S.

national security. And earlier this year, President Trump ordered Beijing Kunlun Co. to divest itself of Grindr LLC, an online dating app, over national security concerns based on foreign access to personally identifiable information.

Although transactions in the technology arena are clearly being targeted by the CFIUS, recent statements coming out of the White House in connection with the ongoing trade war with China show that the CFIUS may begin scrutinizing transactions in sectors that are not often associated with national security, such as imported automotive passenger vehicles and auto parts. President Trump's announcement (in May 2019) that "automobiles

and certain automobile parts are being imported into the United States in such quantities and under such circumstances as to threaten to impair the national security of the United States," generated concern from major automobile importers such as Toyota. Whether the President's statement will lead to future CFIUS scrutiny and potential prohibition of transactions in the automotive sector—especially in connection with companies involved in the development and manufacture of electric and autonomous vehicles—or beyond, only time will tell. [Q](#)

## PRACTICE AREA NOTES

### Appellate Practice Update

#### *New Supreme Court Precedent on "Substantial Evidence" Standard of Review*

On April 1, 2019, the Supreme Court decided a case providing a detailed explanation of the meaning of "substantial evidence" when applying that standard of review. In *Biestek v. Berryhill*, 139 S. Ct. 1148 (2019), the Supreme Court addressed whether the Social Security Administration's reliance on expert testimony based on private data, while refusing to provide that data, categorically precluded her testimony from qualifying as substantial evidence. *Id.* at 1152. In a majority opinion by Justice Kagan, the Court held that there was no such categorical preclusion.

In reaching this conclusion, the Court examined the meaning of substantial evidence. The Court first explained that the standard "is not high," but "is more than a mere scintilla." *Id.* at 1154 (quotation marks omitted). "It means—and means only—'such relevant evidence as a reasonable mind might accept as adequate to support a conclusion.'" *Id.* (quoting *Consolidated Edison Co. v. NLRB*, 305 U.S. 197, 229 (1938)). Applying this test, the Court began by stating that a very qualified expert could rely on data not provided if the data was not requested by the other side. *Id.* at 1155. The Court then held that a refusal to provide requested data could undermine "iffy" testimony to render it not substantial evidence, but if the agency "views the expert and her testimony as otherwise trustworthy, and thinks she has good reason to keep her data private, her rejection of an applicant's demand need not make a difference." *Id.* at 1156. Thus, the court concluded that there can be no "categorical rule," and instead the inquiry must be "case-by-case." *Id.* at 1157; *see also id.* at 1156 ("In some cases, the refusal to disclose data, considered along with other shortcomings, will prevent a court from finding that 'a reasonable mind' could accept

the expert's testimony. But in other cases, that refusal will have no such consequence.") (internal citation omitted). Three Justices dissented on the ground that the testimony of the expert at issue did not suffice for substantial evidence—a question the majority did not reach because it believed only the issue of the categorical rule was properly raised—but all agreed that there should be no categorical rule. *Id.* at 1157 (Sotomayor, J., dissenting); *id.* at 1161-62 (Gorsuch, J., joined by Ginsburg, J., dissenting).

The substantial-evidence test is important in administrative law because it is the standard typically applied to a court's review of agency fact-finding, and *Biestek's* analysis of the substantial-evidence test is instructive in two respects. First, as one commentator has noted, the majority's framing of the test—relying on *Consolidated Edison* for a "such relevant evidence as a reasonable mind might accept" standard—is arguably more deferential than the framing the Court has used at other times, which aligned "substantial evidence" with the test for challenging jury fact-finding. *See Biestek v. Berryhill* and *Judicial Review of Agency Factfinding*, Law & Liberty, <https://www.lawliberty.org/2019/04/10/biestek-v-berryhill-and-judicial-review-of-agency-factfinding> (Apr. 10, 2019). Indeed, the majority at one point seemed to suggest that anything more than a mere scintilla of evidence would suffice. *See Biestek*, 139 S. Ct. at 1156 ("[T]he expert's opinion will qualify as 'more than a mere scintilla' of evidence supporting the ALJ's conclusion. Which is to say it will count, contra *Biestek*, as substantial."). Second, *Biestek* also shows the need for litigants to keep in mind that, when challenging agency fact-finding, any attempt to propose categorical rules will be unlikely to succeed. Thus, rather than arguing that evidence should be categorically rejected as insufficient, a case-specific argument—like the one accepted by the dissenting Justices—is generally the more promising approach.

## Arbitration Update

### *Express Consent Required for Class Arbitration*

A recent Supreme Court decision has—for the most part—signaled the end to an era of class arbitration proceedings. In *Lamps Plus, Inc. v. Varela*, 139 S. Ct. 1407 (2019), the Court held that class-wide arbitration can only be compelled if the arbitration agreement expressly authorizes it. *Id.* at 1419. This case bolsters a line of Supreme Court decisions favoring individualized arbitration over the past decade. See *Epic Sys. Corp. v. Lewis*, 138 S. Ct. 1612 (2018) (validating class arbitration waivers regardless of NLRA conflicts); *Am. Exp. Co. v. Italian Colors Rest.*, 570 U.S. 228 (2013) (validating class arbitration waivers irrespective of cost imposed on either party); *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333 (2011) (holding that the FAA preempts state laws prohibiting class arbitration); *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp.*, 559 U.S. 662 (2010) (holding that silence in an arbitration agreement cannot compel class-wide arbitration). In a 5-4 decision authored by Chief Justice Roberts, the Court made it clear that arbitration is “strictly a matter of consent.” *Lamps Plus*, 139 S. Ct. at 1415.

**Background and Procedural History.** In 2016, *Lamps Plus* was hacked. *Id.* at 1407. *Lamps Plus* inadvertently disclosed the tax information of 1,300 company employees. *Id.* After a fraudulent tax return was filed in the name of employee Frank Varela, he filed a putative class action against *Lamps Plus* in Federal District Court on behalf of employees whose information had been compromised. *Id.* *Lamps Plus*, in accordance with its employee arbitration agreement, sought to dismiss the claims and compel individual arbitration. *Id.* The court dismissed the claims but authorized Valera to pursue class arbitration. *Id.*

On appeal, *Lamps Plus* argued that the District Court erred by compelling class arbitration, but the Ninth Circuit affirmed the order. *Id.* The Ninth Circuit concluded the agreement was ambiguous on the issue of class arbitration. *Id.* at 1413. The court resolved this ambiguity by applying the *contra proferentem* doctrine, which requires contractual ambiguities to be construed against the drafter (*Lamps Plus*). *Id.*

**The Supreme Court’s Reversal.** The Court faced the question of, “whether, consistent with the [Federal Arbitration Act], an ambiguous agreement can provide the necessary ‘contractual basis’ for compelling class arbitration.” *Id.* at 1415. The majority held that it “cannot.” *Id.*

The FAA has a fundamental rule—arbitration is a creature of “consent, not coercion.” *Id.* Consent is essential under the FAA because arbitrators wield only the authority they are given. *Id.* at 1416. That is, they derive

their powers from the parties’ agreement to forgo the legal process and submit their disputes to private dispute resolution. *Id.* At issue here was the interaction between the FAA’s fundamental rule and the *contra proferentem* rule applied to address the agreement’s ambiguity. *Id.* at 1415. Under the FAA, state contract law is applied to interpret the intent of the parties to an arbitration agreement—to the extent it does not preempt the FAA. *Id.* at 1415. But here, the majority found the application of *contra proferentem* to the agreement preempted the FAA. The Court explained that the *contra proferentem* doctrine applied by the Ninth Circuit is a rule of “last resort,” and it is only used when the intent of the parties cannot be deciphered. *Id.* at 1417. But if the parties’ intent is undecipherable, they will surely fail to conform with the FAA’s fundamental rule of consent—this logical barrier was the crux of the Court’s opinion. The Court saw the Ninth Circuit’s holding as an effort to “reshape” individualized arbitration in a manner that was inconsistent with the FAA. *Id.* at 1418.

Chief Justice Roberts emphasized the importance of consent by “recognizing the ‘fundamental’ difference between class arbitration and the individualized form of arbitration envisioned by the FAA.” *Id.* at 1416. Class arbitration sacrifices the traditional benefits of informality, cost, and efficiency. *Id.* Instead, the aggregate process looks like “the litigation it was meant to displace.” *Id.* Further, “it also raises serious due process concerns by adjudicating the rights of absent members of the plaintiff class” with limited judicial review. *Id.*

**Client Impact.** *Lamps Plus* is a major win for employers. The Court’s ruling was immediately echoed just one day later in *Herrington v. Waterstone Mortg. Corp.*, No. 11-CV-779-BBC, 2019 WL 1866314 (W.D. Wis. Apr. 25, 2019). In the case, a \$10 million class arbitration award was vacated when a class arbitration waiver was in conflict with the agreement’s incorporation of the American Arbitration Association (AAA) rules, which authorized class arbitration. *Id.* at \*1. The court held that, even if this conflict created an ambiguity, the award would still be vacated because *Lamps Plus* confirmed that class arbitration would be improper. *Id.* at \*5.

Employers who wish to avoid class-wide arbitration should still include explicit waivers in their arbitration agreements. However, *Lamps Plus* will offer additional protection against class arbitration for slow-moving employers and those sued on old contracts without a waiver. As it stands today—silence, ambiguity, and explicit waivers are all valid defenses to class arbitration.

Employers should also be aware of what the court *did not* decide—the question of “arbitrability.” *Lamps Plus*, 139 S. Ct. at 1417 n.4. If the wording of an arbitration agreement is not precise, the decision of class-wide arbitration could be left to the arbitrator, not the court.



Depending on the agreement, the arbitrator may authorize class arbitration; a ruling the court would have to respect “however good, bad, or ugly.” *Oxford Health Plans LLC v. Sutter*, 569 U.S. 564, 573 (2013).

## White Collar Litigation Update

### *Information Advantage? Foreign Nationals’ and Companies’ Challenges in Navigating U.S. Criminal Prosecutions While Subject to the Fugitive Disentitlement Doctrine*

Non-U.S. individuals and companies face an initial critical question when summoned to face criminal charges in U.S. courts: should they immediately surrender to the U.S. government’s authority, or fight to gain more information, protect assets from seizure, and/or potentially challenge extradition? With little access to relevant information at the outset, and often a limited understanding of applicable U.S. laws, the individual or company should attempt to gain as much information as possible about the strength of the government’s case before proceeding.

A typical defendant has at its disposal several methods to gather information, including various forms of discovery, a written bail demand that may trigger disclosures, or conducting its own internal investigation. These processes are severely hampered by the “fugitive disentitlement doctrine,” however, which limits the recourse available to defendants who remain beyond the reach of the U.S. courts.

The nearly 150-year old fugitive entitlement doctrine was initially created by an appellate court to “dismiss an appeal or writ in a criminal matter when the party seeking relief becomes a fugitive.” *Degen v. United States*, 517 U.S. 820, 823 (1996) (citing *Ortega-Rodriguez v. United States*, 507 U.S. 234, 239 (1993)); *Smith v. United States*, 94 U.S. 97, 24 (1876)). The doctrine developed to respond to two concerns—first, that a decision by a U.S. appellate court would be unenforceable against the fugitive because of due process concerns; and second, that a “fugitive” from justice should not be able to avail himself or herself of the benefits of the same system he or she sought to avoid. Over time, the doctrine has expanded beyond criminal cases to civil cases including, in particular, those involving foreign defendants.

Once a court concludes that a party is a fugitive, the doctrine permits a court to deny that party’s request to make *any* use of the judicial system. The doctrine promotes the federal courts’ power “to protect their proceedings and judgments in the course of discharging their traditional responsibilities” and promote the “dignity of the judiciary.” *Degen*, 517 U.S. at 823.

Contrary to the popular understanding of a “fugitive” as a defendant who, after being charged with a crime, hides or flees the jurisdiction to avoid imprisonment,

the doctrine also applies to non-U.S. citizens who are considered “fugitives” due to their failure to surrender to U.S. authorities upon learning of the charges against them. *See, e.g., United States v. Nabepanha*, 200 F.R.D. 480, 482 (S.D. Fla. 2001) (noting the “critical element” is “knowledge of a pending charge” and that a defendant’s knowledge “can be inferred from his failure to surrender to authorities once he learns of the charges while outside of the jurisdiction”). Failing to surrender does not mean, of course, that a non-U.S. national can count on safely remaining beyond the United States’ jurisdiction. The U.S. Department of Justice (“DOJ”) may commence extradition proceedings against a foreign national if that individual’s home country is a party to an extradition treaty with the United States. It can also pursue an INTERPOL Red Notice requesting that participating countries arrest the named individual for possible extradition to the United States, which effectively prevents the foreign national from traveling.

Once triggered, the fugitive disentitlement doctrine limits a foreign defendant’s defensive and information-gathering options in three important ways. First, the doctrine can defeat a foreign defendant’s motion to dismiss the indictment, a typical first parry for foreign nationals facing charges. Courts have routinely refused to entertain motions to dismiss brought by foreign nationals based on the fugitive disentitlement doctrine alone. *See, e.g., United States v. Kashamu*, 656 F. Supp. 2d 863, 868 (N.D. Ill. 2009) (denying motion to dismiss under fugitive disentitlement doctrine); *United States v. Stanzione*, 391 F. Supp. 1201, 1202 (S.D.N.Y. 1975) (same).

Second, the doctrine can prevent the foreign national defendant from obtaining discovery into the charges, another common and important strategy pursued by defendants. U.S. courts consistently deny such requests when the foreign national is considered a fugitive. *Nabepanha*, 200 F.R.D. at 482-84 (denying a discovery request by defendant who moved to Israel prior to his indictment and who refused to return to the United States for trial); *see also S.E.C. v. Roman*, 1996 WL 34146, \*2 (S.D.N.Y. Jan. 30, 1996) (holding that plaintiffs were barred from obtaining discovery while they were fugitives because “one who has removed himself from the jurisdiction of the courts has no claim upon them which would require the delivery of the files of the United States government to his hiding place”). In a recent and high-profile example, the U.S. District Court for the District of Columbia restricted access into the government investigative file by absent foreign entities in the Special Counsel’s investigation into alleged Russian involvement in the 2016 U.S. election. *See United States v. Concord Mgmt. & Consulting LLC*, Case No. 1:18-cr-00032-DLF, Dkt. No. 42 at 3-4 (D.D.C. June 29, 2018) (ordering that “all sensitive discovery materials must be




stored in a U.S. office of [defendant's counsel's firm] and shall not be disclosed, transported, or transmitted outside of the United States").

Third, the doctrine also has been extended to bar foreign nationals who are alleged fugitives from contesting the seizure of their assets. The Civil Asset Forfeiture Reform Act of 2000 ("CAFRA") codified the fugitive disentitlement statute, allowing courts to prohibit fugitives from contesting forfeiture claims. 28 U.S.C. § 2466.

Given these procedural impediments to those deemed fugitives, it is important to understand the applicable law relevant to the doctrine. The U.S. Courts of Appeals are currently split over the issue of the requisite intent "to avoid criminal prosecution" that triggers application of the doctrine. The D.C. Circuit has adopted the most favorable position to foreign nationals, holding that the government must prove "that avoiding prosecution is the reason [an alleged fugitive] has failed to enter the United States." *United States v. 6,976,934.65, Plus Interest Deposited into Royal Bank of Scot. Int'l, Account No. XXXX-XXXXXXXX, Held in Name of Soulbury Ltd.* ("Soulbury"), 554 F.3d 123, 132 (D.C. Cir. 2009). The Second Circuit has rejected the D.C. Circuit's approach, concluding that "[t]o the extent that the D.C. Circuit's opinion in [Soulbury] was intended to mean that when a claimant declines to enter or reenter the United States the government is required to prove that avoidance of criminal prosecution is his *sole* purpose, we respectfully disagree." *United States v. Technodyne LLC*, 753 F.3d 368, 384-85 (2d Cir. 2014) (emphasis added). The Second Circuit ruled that the correct standard is instead "specific intent" to avoid prosecution, a lower threshold. *Id.* "[S]pecific intent need not be the actor's sole, or even

primary, purpose." *Id.* Rather, in the Second Circuit, individuals can be deemed fugitives under § 2466 so long as "any of their motivations for declining to reenter the United States was avoidance of criminal prosecution." *Id.* at 386.

The Fifth and Ninth Circuits have adopted yet a third standard by requiring that intent to avoid prosecution be proven by a totality of the circumstances. *See United States v. 2005 Pilatus Aircraft, Bearing Tail No. N679PE*, 838 F.3d 662, 664 (5th Cir. 2016) (approving fugitive disentitlement of a defendant who suddenly avoided any travel following his criminal indictment, after previously taking more than 100 trips to the United States); *United States v. \$671,160.00 in U.S. Currency*, 730 F.3d 1051, 1056-57 (9th Cir. 2013) (claimant's changed travel plans coupled with statements that he remained in Canada due to the criminal matter demonstrated that totality of the circumstances showed he deliberately remained away from the United States to avoid criminal prosecution).

Given the impediments posed by the fugitive disentitlement doctrine, a foreign national may determine it best to travel to the United States to challenge criminal proceedings, but that strategy comes with serious risks of its own. Upon arrival, he or she faces arrest and may be detained pending trial or required to post a significant bond. The foreign national could also be forced to remain in the United States for a significant time prior to trial. These competing considerations complicate the defense strategy for foreign individuals facing U.S.-based criminal prosecutions and require careful analysis. 

## VICTORIES

### Second Circuit Victory for Indonesian Bank

The firm recently won an important victory in the Second Circuit for the former Bank Mutiara, an Indonesian bank which emerged from receivership after the financial crisis. In 2013, a purported hedge fund called Weston International Capital Limited, through one of its affiliates, obtained judgments against Bank Mutiara in Mauritius, which it then sought to enforce on Bank Mutiara's correspondent bank accounts in New York. Before Quinn Emanuel was retained, Judge Crotty of the Southern District of New York entered judgment for Weston, then vacated the judgment within three weeks of our appearing and defending Bank Mutiara. But in the meantime, Weston had obtained more than \$3.6 million, which it steadfastly refused to return after the court vacated the judgments and ordered Weston to return the money.

The firm persuaded the court to hold each of the Weston entities and its principal in contempt and impose monetary fines that ultimately reached more than \$400 million. But Weston still refused to comply. In response to this, Quinn Emanuel then asked the court to transfer ownership of the Weston entities to Bank Mutiara, since it was clear that Weston and its principal would never comply with the court's orders. This was an extraordinary and apparently unprecedented order, but QE persuaded the district court to grant the motion and the Court of Appeals to affirm.

Following that order, Weston's former management commenced an action in the Delaware Court of Chancery that was designed to oust the director that Bank Mutiara appointed to the board of one of the entities and to retake control of the entities. The firm swiftly obtained an

# VICTORIES

injunction against that suit, which the Court of Appeals affirmed. The order leaves Weston's former management with no viable means to continue to harass Bank Mutiara in federal or state courts in the United States or anywhere else, and it will bring to an end Weston's years-long global litigation and harassment campaign against Bank Mutiara.

## Preliminary Injunction Victory for Lockton Companies

The firm recently achieved a broad preliminary injunction for Lockton Companies in a case arising out of a corporate raid engineered by competitor Alliant and its outside counsel.

Our clients, the Mountain West Series of Lockton Companies, LLC, and Lockton Partners, LLC, are commercial insurance brokers based in Denver and Kansas City, respectively. Defendant Alliant Insurance Services, Inc., headquartered in Newport Beach, sought to gain a foothold in the Denver market by inducing seven of Lockton's revenue-generating "Producer Members" and 19 additional employees to resign *en masse* from Lockton to join Alliant. Immediately upon joining Alliant, they began to solicit Lockton's clients to move their business to Alliant, in violation of post-termination non-solicitation obligations contained in their respective agreements with Lockton. Within a matter of days, more than 50 Lockton customers had moved their business in response to the improper solicitation.

After Lockton's Kansas City-based counsel were denied a temporary restraining order against the defecting Producer Members in Missouri state court, QE filed an action directly against Alliant in Delaware Chancery Court, alleging tortious interference with contract and business expectancy; misappropriation of trade secret, confidential, and proprietary information; and aiding and abetting breaches of fiduciary duty. In a critical move during expedited discovery, the Delaware Vice Chancellor granted Quinn Emanuel's motion to compel Alliant to produce the more than 1000 documents listed on its privilege log on the grounds that the log was grossly deficient and therefore did not adequately claim privilege under Delaware rules. The production of these documents revealed that Alliant and its outside counsel sought to conceal evidence, in one case sought to destroy evidence, and that they intentionally induced Lockton's former Producer Members and employees to breach various obligations to Lockton, knowing full well the legal risks inherent to its raid on Lockton. In another strategic victory, a subpoena to Lockton's landlord for security tapes yielded footage of a former Lockton employee taking armloads of documents from Lockton's offices during the weekend before the raid, which was used by Quinn Emanuel to impeach this former employee's inconsistent testimony during his deposition

and served as a key fact in motion practice.

After extensive expedited briefing, the Court held a one-day preliminary injunction hearing where Quinn Emanuel presented additional evidence of similar misconduct by Alliant, including evidence that Alliant had made misrepresentations in its answer to Lockton's complaint and in its interrogatory responses and that certain of the former Producer Members and Alliant's own executives had made numerous representations in sworn statements that they later had to recant or modify in the face of contradictory evidence. In light of this evidence, Lockton argued that it had a reasonable likelihood of prevailing on its claims and that Lockton would face irreparable harm in the absence of an injunction against Alliant's further solicitation of Lockton's employees and customers. The Court agreed and granted a temporary restraining order from the bench, finding "an absolute threat of irreparable harm" to Lockton. Later, in its comprehensive 57-page opinion, the Court found that Alliant "engineered" and "coordinated" the raid that "induced" the former employees to "breach" their Lockton contracts and begin a "full-court press" to solicit Lockton's customers. Notably, the Court found Alliant and its outside counsel responsible for "secretive and underhanded behavior in violation of contractual obligations and legal requirements." Until a trial on the merits, likely later this year, Alliant and its affiliated entities are enjoined from soliciting or servicing many of Lockton's customers and prospects, including those who had already switched brokers, and from soliciting any Lockton employee, member, or consultant.

## Appellate Victory for KKR

The firm recently secured an important appellate victory for KKR in a case in which the Plaintiff, Atlas, sought to unwind a multimillion dollar sale of properties to KKR affiliates at a UCC auction. See *Atlas MF Mezz. Borrower, LLC v. Macquarie Tex. Loan Holder, LLC*, --- N.Y.S.3d ---, 2019 WL 2374960, \*1 (1st Dep't June 6, 2019). The First Department of the New York Appellate Division held that Atlas was not entitled to unwind the sale after closing, and dismissed Atlas's damages claims against KKR. This was not only a win for KKR, but it also brought much-needed certainty to the law governing UCC foreclosure sales in New York. Bidders at foreclosure sales can now rest assured that their sales cannot be undone after closing, which is a significant and positive development for New York commercial transactions.

The case arose from Atlas's default on a \$71 million mezzanine loan extended by Macquarie, its secured creditor. The loan was secured by Atlas's equity interests in a holding company that indirectly owned eleven apartment complexes in Texas. After Atlas defaulted, Macquarie announced its intention to sell the holding company at an

auction. Atlas attempted to halt the auction by seeking a preliminary injunction in the Southern District of New York, but Atlas's motion was denied. The auction proceeded as scheduled, and KKR was declared the winning bidder due to its demonstrated financial ability to close on the purchase. Atlas also attempted to bid at the auction, but its bids were rejected because Atlas failed to meet the auction's requirements.

After losing the auction, Atlas added KKR as a defendant to its lawsuit, which was remanded to New York Supreme Court. Atlas ultimately filed an amended complaint that alleged (without any factual basis) that KKR and Macquarie had conspired to rig the auction. The primary relief Atlas sought was a declaratory judgment claim seeking to unwind the sale. Atlas also sought \$30 million in damages based on allegations that KKR had induced Macquarie to breach its mezzanine loan agreement with Atlas. Prior to retaining Quinn Emanuel, KKR's prior counsel moved to dismiss, but the Court (Ramos, J.) denied the motion at a hearing. KKR then hired Quinn Emanuel.

Quinn Emanuel appealed the Court's order denying KKR's motion to dismiss even while aggressively litigating the case at the trial court level. The primary issue on appeal was whether Atlas was entitled to unwind the sale of the holding company to KKR under Article 9 of the UCC. Surprisingly, no New York court had ever definitively addressed the issue, and the few courts in other jurisdictions to have considered it had reached differing (and often cryptic) conclusions. The case thus presented an issue of first impression.

Last month, the First Department validated Quinn Emanuel's position in a comprehensive, twenty-six page opinion that often adopted Quinn Emanuel's arguments wholesale and unequivocally held that Atlas was not entitled to unwind the sale. The First Department also emphatically rejected Atlas's arguments. The First Department began its decision by stating that: "if UCC sales could be unwound, it would only serve to muddy the waters surrounding nonjudicial sales conducted pursuant to article 9 of the UCC, and to deter potential buyers from bidding in nonjudicial sales, which would, in turn, harm the debtor and the secured party attempting to collect after a default." *Id.* at \*1. The First Department further reasoned that Atlas's requested relief (unwinding the sale) was at odds with the plain language of the UCC, which allows an aggrieved debtor to seek injunctive relief *before* a sale has closed, but limits the debtor to seeking damages after closing. *Id.* at \*8. Finally, the First Department held that Atlas's damages claims against KKR failed because Atlas had defaulted on its mezzanine loan agreement with Macquarie, and thus could not hold KKR liable for inducing Macquarie to breach that agreement (since Atlas

had failed to perform under the agreement). Thus, all of Atlas's claims against KKR were dismissed.

## Victory for The Andy Warhol Foundation for the Visual Arts, Inc.

The firm recently achieved a complete victory for The Andy Warhol Foundation for the Visual Arts, Inc., obtaining a ruling from the district court that Andy Warhol's series of celebrity portraits of Prince is protected by fair use.

Warhol regularly used source images, such as photographs of celebrities like Marilyn Monroe, as part of his artistic process. Even though Warhol transformed the underlying source material in his art, it has been the subject of accusations of copyright infringement.

In 2017, the Foundation was threatened with suit by rock-and-roll photographer Lynn Goldsmith. She had taken photographs of Prince in 1981, and later licensed one of the photographs to Vanity Fair for use as an "artist reference." Andy Warhol used Goldsmith's photograph as a reference for sixteen famous portraits of Prince. Vanity Fair published one of Warhol's portraits in its November 1984 issue, accompanying an article about Prince's rising fame entitled "Purple Fame."

After Prince died in 2015, Condé Nast published a commemorative magazine celebrating the musician's life and work. It obtained a license from the Foundation to publish one of Warhol's Prince works on the cover of the magazine. Goldsmith then threatened to sue the Foundation for copyright infringement. The Foundation sued Goldsmith first in the U.S. District Court for the Southern District of New York, seeking declaratory judgments that, among other things, Warhol's Prince works made fair use of Goldsmith's photograph. Goldsmith counterclaimed for copyright infringement.

The parties engaged in discovery and filed summary judgment motions on their respective claims. After oral argument, the district court ruled in favor of the Foundation, granting its motion for summary judgment and dismissing Goldsmith's counterclaim. The court held that Warhol's sixteen Prince works are transformative—the most important of the statutory factors considered by courts in determining whether the "fair use" defense applies. The court explained that Warhol's alterations to the source material "result in an aesthetic and character different from the original." The court further recognized that Warhol's Prince works "add something new to the world of art and the public would be deprived of this contribution if the works could not be distributed."

The importance of this ruling to Warhol's legacy cannot be overstated: finding that Warhol's Prince works are transformative protects against further claims of infringement and preserves Warhol's legal reputation as one of the most influential artists of the 20th century. Q



**business litigation report****quinn emanuel urquhart & sullivan, llp**

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