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Supreme Court Limits SEC Disgorgement to Five Years

by Alan D. Albert, Esq.

In a unanimous decision handed down on June 5, 2017, the U.S. Supreme Court has imposed what in many cases may be a substantial limitation on the amount of disgorgement the Securities and Exchange Commission (SEC) may seek as part of a securities civil enforcement action.

Justice Sonia Sotomayor's succinct opinion applies a general statute establishing a five-year statute of limitations on any "action, suit or proceeding" that seeks to impose a "civil fine, penalty, or forfeiture, pecuniary or otherwise," 28 U.S.C. § 2462, to SEC actions seeking disgorgement. The effect of the holding is to limit the SEC's disgorgement claims to wrongful gains arising during the five years immediately preceding the filing of the civil enforcement action.

Disgorgement is often sought by the SEC as part of civil enforcement proceedings against individuals and entities that the Commission asserts have profited from violations of the securities laws. Disgorgement seeks to deprive an alleged wrongdoer of the profits earned, often not only by the target of the action her *or* himself, but also those "downstream" of the target; an action seeking disgorgement of profits arising from insider trading, for example, may seek from the "tipper" profits earned by the "tippee" as well as the tipper. As a result, disgorgement remedies often require the wrongdoer to give up substantially more than she or he took in through the challenged conduct.

There is no explicit statutory authority for the SEC to pursue disgorgement as part of the remedy in a civil enforcement action; the Commission persuaded courts, beginning in the 1970s, to impose disgorgement remedies as an exercise of its inherent equitable powers. In 1990, Congress granted the SEC explicit authority to seek civil monetary penalties (CMPs) as part of the Securities Enforcement Remedies and Penny Stock Reform Act, 15 U.S.C. § 77t(d). Armed with this authority, the Commission added CMPs to its toolbox of remedies regularly sought in civil enforcement actions – but did not stop seeking disgorgement, as a separate and distinct remedy in addition to any CMP.

In defending the practice of seeking disgorgement stretching back in time substantially more than five years, the SEC maintained that disgorgement is remedial, rather than punitive, in nature, and thus not subject to the five-year statute prescribed for any action seeking a "penalty" or forfeiture."

The Court, however, decisively rejected this position, holding that disgorgement bears the hallmarks of a penalty: it is a remedy sought to redress a "wrong to the public," rather than a "wrong to [an] individual," and it is sought for the purpose of punishing wrongful conduct and deterring similar future conduct, rather than compensating losses incurred by an individual. Disgorgement, explained the Court, is sought to combat violations of public law and in furtherance of the public interest, not to compensate an aggrieved individual, is clearly punitive in nature, seeking primarily to deter violations of securities laws by clawing back ill-gotten gains; and, because paid into the court with no requirement for restitution (and often no practical means of effecting restitution), and often imposed at levels that exceed gains ill-gotten by the defendant, is not compensatory. Invoking its recent decision (*Gabelli v. SEC*, 568 U.S. 442 (2013)) applying the five-year statute of limitations to CMPs, the Court held that disgorgement orders, like CMPs, "go beyond compensation, are intended to punish, and label defendants wrongdoers' as a result of violating public laws," and thus constitute penalties subject to the five-year statute.

The facts of the case before the Court illustrate the potentially far-reaching practical impact of the decision in many securities enforcement actions. The defendant, Charles Kokesh, was determined by a jury to have violated various securities laws by misappropriating a total of $34.9 million in funds from four business development companies that were clients of Kokesh's investment advisory firms over the 15-year period preceding the filing of the SEC's civil enforcement action. The Court imposed a civil monetary penalty of slightly less than $2.4 million, representing Kokesh's personal gains during the five years preceding the SEC's filing of suit. But the Court, reasoning that disgorgement was not a "penalty," granted the SEC's request to impose a disgorgement obligation of the full $34.9 million diverted over 15 years – almost $30 million of which arose more than five years prior to the filing of suit. The Supreme Court's decision invalidates that nearly $30 million component of the disgorgement order, trimming the total to be disgorged by 85 percent.

The decision will with certainty affect pending actions for disgorgement, limiting the amount recoverable in those actions. It is likely that the decision also will give rise to efforts to reduce recent disgorgement awards to the extent that they are based upon more than five years of wrongful conduct.

The opinion is *Kokesh v. SEC*, No. 16-529, slip. op. June 5, 2017.

Contact the author at alan.albert@leclairryan.com.

Revised Form I-9 Released; Mandatory Use By Mid-September *by Lauren M. Hopwood, Esq.*

The U.S. Citizenship and Immigration Services (USCIS) released a revised version of Form I-9, Employment Eligibility Verification on July 17, 2017. Employers can use this revised version, or continue using the prior Form I-9 with a revision date of 11/14/16N, through September 17, 2017. However, employers must begin using the revised form with a revision date of 07/17/17N on September 18, 2017.

The following revisions have been made to the updated form:

- USCIS added the Consular Report of Birth Abroad (Form FS-240) to List C. Employers completing Form I-9 on a computer will be able to select Form FS-240 from the drop-down menus available in List C of Sections 2 and 3. E-Verify users will also be able to select Form FS-240 when creating a case for an employee who has presented this document for Form I-9.
- USCIS combined all the certifications of report of birth issued by the Department of State (Form FS-545, Form DS-1350, and Form FS-240) into selection C #2 in List C.
- USCIS renumbered all List C documents except the Social Security card. For example, the employment authorization document issued by the Department of Homeland Security on List C changed from List C #8 to List C #7.

USCIS has included these changes in the revised Handbook for Employers: Guidance for Completing Form I-9 (M-274).
https://www.uscis.gov/i-9

Members of LeClairRyan's immigration law team handle a full spectrum of immigration and naturalization issues for clients across industries and are available to answer employers' questions and help them become familiar with the form's updates.

Contact the author at lauren.hopwood@leclairryan.com.

Medical Marijuana – Now a Potential "Reasonable Accommodation" in Massachusetts
by Thomas K. McCraw, Jr. Esq.

The Supreme Judicial Court of Massachusetts (the "SJC") recently held that medical marijuana may constitute a "reasonable accommodation" for employees. As a result, employers may not terminate employees for failing drug tests if the employees fall within that protection – provided the accommodation does not pose an undue hardship for the employer.

Factual Background

In *Barbuto v. Advantage Sales & Marketing, LLC* (Massachusetts Supreme Judicial Court, July 17, 2017), SJC considered whether an employer had violated the Massachusetts anti-discrimination statute, M.G.L. c. § 151B, by terminating an employee who had failed a drug test for using marijuana at her home to ease her symptoms of Crohn's disease and irritable bowel syndrome. The employee had a duly-issued certificate from

her physician authorizing the use of marijuana for those purposes. Upon receiving the positive drug test, the employer terminated the employee over her protests that she was medically authorized to use marijuana, which was legal in Massachusetts. The employer responded that it followed the federal law on the issue, rather than state law.

The employee filed suit for discrimination on the basis of physical handicap, alleging violation of privacy, wrongful termination in light of her medically authorized use of marijuana, and violation of public policy. The trial court dismissed her complaint, and the employee appealed directly to the Supreme Judicial Court.

Legal Analysis

Massachusetts' anti-discrimination statute, M.G.L. c. 151B, § 4, requires employers to provide "a qualified handicapped person" with a "reasonable accommodation" if necessary to enable the employee to perform the essential job functions of her position, unless doing so would impose an "undue hardship" on the employer (usually in the form of a disparate economic impact, or employee safety risks).

The SJC held that allowing a qualified handicapped employee to use medical marijuana to alleviate or manage a medical condition is not unreasonable on its face. The court was unpersuaded by the employer's argument that permitting its employees to use medical marijuana – while permitted by state law – nonetheless would expose the employer to criminal liability under federal law (which does not provide for legal use of marijuana). The court disagreed, noting that the only potentially criminally liable offender would be the employee herself.

The court's ruling, however, does not constitute a blanket allowance for use of medical marijuana. The employer and employee must still engage in the "interactive process" between them to identify and determine an appropriate "reasonable accommodation" to allow the employee to perform her job functions. If an equally effective medication exists, the employer may allow the employee to use that medication as a reasonable accommodation – even if the employee would prefer medical marijuana. If the employer proved medical marijuana posed an unreasonable safety risk to its employees, it could also prohibit medical marijuana use as a reasonable accommodation.

Finally, if the employer is required to follow federal law, or has other "contractual or statutory obligations" obviating the Massachusetts state law allowance of medical marijuana, the employer may be able to terminate the employee without penalty. As the SJC's ruling was made very early in the litigation of the underlying case, following the trial court's grant of the employer's motion to dismiss the complaint, the employer may yet bring these arguments on grounds that it poses an undue hardship.

We will follow the case on remand to the trial court from the Supreme Judicial Court, and provide an update as appropriate.

Contact the author at thomas.mccraw@leclairryan.com.

Massachusetts Appeals Court Concluded LLC's Attorneys May Be Held Liable for Alleged Breach of Fiduciary Duty to Minority Members *by Ben N. Dunlap, Esq.*

The Massachusetts Appeals Court has held minority members of a limited liability company may seek to hold the company's attorneys liable for their involvement in an alleged "freeze-out" orchestrated by the majority members. In *Baker, et al. v. Wilmer Cutler Pickering Hale and Dorr, LLP, et al.*, No. 16-P-639 (July 21, 2017), the plaintiffs alleged the majority members of the company secretly retained counsel, ostensibly to represent the company, and the attorneys "worked behind the scenes" to assist the majority in eliminating the rights and interests of the minority members. The plaintiffs further alleged the majority members, with the help of counsel, created a new operating agreement extinguishing the minority members' rights to participate in management, access the company's records, and prevent dilution of their interests. The complaint asserted claims against the company's attorneys including breach of fiduciary duty, aiding and abetting tortious conduct, civil conspiracy, and violation of G.L. c. 93A.

The defendant attorneys filed a motion to dismiss the claims against them, arguing they had no fiduciary duty to the minority members of the company; they could not be liable for aiding and abetting, because the complaint alleged only that they provided legal advice that turned out to be wrong; and the Chapter 93A claim should be dismissed because they were not involved in "trade or commerce." The trial court allowed the motion, and the plaintiffs appealed.

The Appeals Court noted the existence of a fiduciary duty is "fact specific" and concluded the company's attorneys may have a fiduciary duty to the minority members where, as alleged in the complaint, the operating agreement contained express protections for the minority members, and the attorneys allegedly acted, in secret, to eliminate those protections. With respect to the aiding and abetting claim, the Appeals Court determined the complaint alleged more than merely providing legal advice, and the allegations of devising a covert plan to circumvent and evade the minority members' rights, without ever communicating with them, was sufficient to state a claim.

As to the Chapter 93A claim, the Appeals Court concluded the attorneys' alleged fiduciary duty to the minority members was close enough to an "attorney-client relationship" to satisfy the "trade or commerce" requirement of Chapter 93A. The Appeals Court considered the "intra-enterprise" exception to the application of Chapter 93A (according to which Chapter 93A liability does not attach to "intra-enterprise disputes) but determined it did not apply, because the attorneys were not members of the entity at issue.

Contact the author at ben.dunlap@leclairryan.com.

A Well Drafted Contract Could Have Controlled which State's Statute Of Limitations Applied to Disputes Between the Parties *by Eric Martignetti, Esq.*

In *Petrucci v. Esdaile*, the Suffolk Superior Court dismissed part of the contract claim, the breach of fiduciary duty claims, and the Chapter 93A claim brought by Plaintiff Daniel Petrucci, who alleged he was frozen out of a company he started with the three individual defendants. Specifically, Petrucci alleged that Charles Esdaile, Christopher Hayes, and Daniel McIntyre froze him out of Market Maker Solutions LLC ("MMS") by claiming its assets were worthless, transferred MMS's assets to a new entity, and leveraged Petrucci's contributions to MMS to develop a new profitable company in the same line of business. Petrucci, Esdaile, and Hayes each owned 30 percent of MMS, and McIntyre owned 10 percent.

Esdaile, Hayes, and McIntyre all moved to dismiss for failure to state a claim pursuant to Rule 12(b)(6) on the grounds that Petruuci's claims were barred by the statute of limitations. To decide that issue, the Court first had to determine which state's law to apply. The MMS operating agreement provided that the agreement and the interpretation of it were governed by Delaware law. The defendants argued that this choice-of-law provision required that the breach of contract, breach of fiduciary duty, and unjust enrichment claims—which arose under the MMS operating agreement—be governed by the three-year Delaware statute of limitations. The defendants conceded that the fraud and conspiracy claims were governed by the three-year Massachusetts statute of limitations, and the Chapter 93A claim was governed by the four-year Massachusetts statute of limitations because those claims did not arise under the operating agreement.

Siding with Petrucci, the Court held that Massachusetts statutes of limitations governed all of the claims despite the choice-of-law provision in the MMS operating agreement. The Court stated: "Although the parties agreed by contract that any disputes arising under the MMS operating agreement would be governed by Delaware law, their choice-of-law provision does not expressly address limitations periods, and, for that reason, does not control which State's statute of limitations applies here."

The parties agreed that the contract claims would be timely if the Massachusetts six-year statute of limitations applied, but would be time-barred if the Delaware three-year statute of limitations applied. Because the results would be different depending on which state's law applied, the Court conducted a choice-of-law analysis pursuant to the principles set forth in the Restatement § 142(2). The Court concluded that Massachusetts statutes of limitations governed the contract claim because "Massachusetts has a substantial interest in the maintenance and resolution of the claims and a more significant relationship to the parties and the facts giving rise to this dispute." The parties all lived in Massachusetts, they executed the MMS operating agreement in Massachusetts, and the conduct was allegedly breached through conduct in Massachusetts.

Petrucci alleged the defendants breached the MMS operating agreement in two ways: (1) they breached a duty not to transfer assets out of MMS and not to dissolve it; and (2) they breached a duty not to compete with MMS. The Court held that these claims were not time-barred because even assuming the transfer of assets occurred in 2011, Petrucci filed his action on December 30, 2016, within the six-year limitations period. The Court held the second part of this claim failed to state a claim because the MMS operating agreement expressly permitted each member to "conduct or participate in any business or activity whatsoever" and expressly waived any liability for engaging in a competing business.

The Court held that Petrucci's claim for unjust enrichment was not time-barred because it was a quasi-contract claim, and therefore was governed by a six-year limitations period. The Court further held that the unjust enrichment claim was not barred by the fact that the parties entered into an express agreement. The MMS operating agreement addressed only Petrucci's right to share profits generated by MMS; it did not address the defendants' freezing Petrucci out of sharing in future profits generated by the new entity. The Court concluded: "Since the complaint alleges facts plausibly suggesting that Petrucci is entitled to quasi-contractual compensation based in circumstances not addressed or contemplated in the parties' contract, it states a viable claim for unjust enrichment."

The Court held that the breach of fiduciary duty claim, based on the defendants' alleged misappropriating of corporate opportunities belonging to MMS, should be dismissed under Delaware law. Delaware law governed this claim because MMS was a Delaware LLC. Unlike Massachusetts law, Delaware law does not impose a heightened fiduciary duty on shareholders in a close corporation. Because the MMS operating agreement expressly allowed the individual defendants to engage in any business or activity, Petrucci could not sue them for a breach of fiduciary duty he expressly disclaimed when he signed the operating agreement.

Finally, the Court dismissed the Chapter 93A claim because the alleged misconduct of the individual defendants did not take place in "trade or commerce," but rather was part of a purely private, intra-business dispute.

This decision underscores the importance of well-drafted contracts. Parties to a contract that wish to apply a certain state's statute of limitations should expressly state so in the contract. Further, where appropriate, parties to a contract should avoid using words such as "any" and "whatsoever," as such words will likely be interpreted broadly by the court and will likely allow one party to have a lopsided advantage over the other.

Contact the author at eric.martignetti@leclairryan.com.

Assignment of Unsatisfied Judgment Against Former Client Held Enforceable *by David A. Slocum, Esq.*

Massachusetts attorneys should take note of a recent decision of the Massachusetts Superior Court (Hon. Kaplan, J.) holding that the Rules of Professional Conduct did not prohibit a lawyer from receiving an assignment of an unsatisfied judgment against a former client where no confidential information was used to the former client's disadvantage.

The Massachusetts Superior Court's recent decision in *Spinazola v. Mass. Environmental Associates, Inc., et al.*, (Lawyers Weekly No. 12-078-17) (May 9, 2017) arises out of an underlying lawsuit filed over a decade ago by plaintiff, Rosemary Spinazola against defendant, Patrick Hannon. Final judgment was entered in that case in Spinazola's favor in 2007, ordering Hannon to pay Spinazola over $980,000 with post-judgment interest accruing on that amount. Although attorney George McLaughlin did not represent Hannon in the underlying lawsuit with Spinazola, after final judgment was entered in that case, McLaughlin represented Hannon in connection with the negotiation and execution of a settlement agreement between Spinazola and Hannon pursuant to which the judgment would be satisfied by payment of $400,000 according to a payment schedule.

After initially making periodic payments under that settlement agreement, Hannon defaulted while a sizable balance remained outstanding. Under the terms of the settlement agreement, if Hannon defaulted Spinazola would be entitled to enforce the judgment minus the amounts Hannon had paid pursuant to the agreement.

In July 2011, McLaughlin loaned Hannon over $200,000 to purchase an interest in a company unrelated to the Spinazola litigation and settlement agreement. Hannon was represented by competent, independent legal counsel in connection with those loans, which therefore were enforceable. Less than a year later, Hannon filed for bankruptcy. McLaughlin and Spinazola each filed proofs of claims as creditors in the bankruptcy proceedings. McLaughlin filed an adversary complaint in the bankruptcy proceedings challenging Hannon's right to a discharge based upon allegedly false income statements Hannon had filed with the Bankruptcy Court. The Bankruptcy Court found for McLaughlin, and denied Hannon a discharge.

Thereafter, McLaughlin filed a collection action against Hannon and sought to enjoin Hannon from encumbering or disposing of any of his assets or income, except to satisfy ordinary living or business expenses. Because McLaughlin was not at that time a judgment creditor of Hannon, the Superior Court denied McLaughlin's request for an injunction. Soon thereafter, Spinazola, having heard of the Superior Court's denial of McLaughlin's request for an injunction, contacted McLaughlin and offered to sell him her interest in the unsatisfied judgment against Hannon. Following arm's-length negotiation between McLaughlin and Spinazola's attorney, Spinazola assigned her rights under the judgment to McLaughlin.

McLaughlin then filed a motion with the Court seeking an order for execution on the unpaid judgment. Hannon opposed that motion, arguing that the assignment was void as a matter of public policy. Specifically, Hannon argued the assignment violated Massachusetts Rules of Professional Conduct: (1) prohibiting lawyers from representing a party who is materially adverse to a former client in the same or a substantially related matter in which the lawyer has formally represented the former client (Rule 1.9(a)); and (2) prohibiting lawyers from using a former client's confidential information to the former client's disadvantage (Rule 1.9(c)).

Although the Superior Court acknowledged "there is something unseemly" about McLaughlin's purchasing a judgment against Hannon where McLaughlin previously had represented Hannon in negotiating an arrangement for its payment with the original judgment creditor, the Court upheld the assignment as enforceable. With regard to the first of Hannon's arguments, the Court found that Rule 1.9(a) did not apply under the circumstances because McLaughlin was acting as a principal, not as an attorney representing another party adverse to Hannon.

Similarly, the Court found that the particular circumstances of the case brought the assignment beyond the reach of Rule 1.9(c)'s prohibition against using a former client's confidential information to the former client's disadvantage. The Court acknowledged that under many circumstances, it would run afoul of Rule 1.9(c) for a lawyer who previously represented a client in negotiating an agreement with a judgment creditor to then purchase the judgment and seek its enforcement against the former client. As the Court explained:

> For example, if, as a result of a prior representation, the lawyer knew that the full amount of the judgment was still outstanding because the former client/debtor had breached the payment agreement and then sought out the judgment creditor some time later for purpose of purchasing it, this might well constitute a misuse of confidential client information.

In this case, however, there was no evidence to suggest that McLaughlin had any confidential information concerning Hannon's assets. As the Court noted, Spinazola's judgment against Hannon, the settlement agreement, and McLaughlin's loan to Hannon all became matters of public record during the bankruptcy proceedings. Thus, they were not "confidential information" for purposes of Rule 1.9(c). Further, the Court noted Hannon - - who sought to declare invalid an assignment making McLaughlin his creditor - - had long ago consented to making McLaughlin his creditor when he borrowed money from him. The Court also noted it was Hannon who, by filing for bankruptcy and defaulting on his loans, had caused McLaughlin's interests to become adverse to him. Thus, under the circumstances presented in this case, the Court held the assignment of the unsatisfied judgment against Hannon was enforceable as it did not

violate either of the Rules of Professional Conduct cited by Hannon.

The decision in *Spinazola* should not be misinterpreted as establishing a bright line rule that attorneys may in all cases validly acquire an interest in an unsatisfied judgment against a former client. Where it would involve the use of confidential client information to the former client's disadvantage, doing so is prohibited by the Rules of Professional Conduct. However, if no confidential information is used to disadvantage the former client, the *Spinazola* decision recognizes that this practice may be upheld. Thus, at least under circumstances similar to those presented in *Spinazola*, receiving an assignment of an unsatisfied judgment against a former client may be appropriate and helpful to protect an attorney's interest in seeking to collect amounts owed to the attorney by a former client.

Contact the author at david.slocum@leclairryan.com.

One Racial Slur is One Too Many, Rules Third Circuit *by Brandon R. Sher, Esq.*

Is a single racial slur by an employee's supervisor enough to create a hostile work environment under § 1981 of the Civil Rights Act of 1866? The answer is yes according to the Third Circuit Court of Appeal's decision in *Castleberry v. STI Group*, No. 16-3131 (3d Cir. July 14, 2017).

In *Castleberry*, two African American males were employed as general laborers. They claimed that while working on a fence-removal project, their supervisor threatened to fire them if they "n[****]r-rigged" the fence. The incident was confirmed by their coworkers and reported thereafter by the employees to a superior. Two weeks later, they were fired without explanation (and they were subsequently rehired, only to be fired again for "lack of work").

The employees filed suit alleging harassment, discrimination, and retaliation in violation of 42 U.S.C. § 1981. The trial court dismissed the employees' harassment claim because it determined the facts as pleaded did not support a finding that the harassment was pervasive and regular.

A claim under § 1981 involves the same analysis as an employment discrimination case under Title VII of the Civil Rights Act of 1964. To win a case for a hostile work environment based on race, an employee must prove that: (1) the employee suffered intentional discrimination because of his/her race; (2) the discrimination was severe or pervasive; (3) the discrimination detrimentally affected the plaintiff; (4) the discrimination would detrimentally affect a reasonable person in like circumstances; and (5) the employer is responsible.

The employees in *Castleberry* appealed the trial court's decision, arguing that the court applied the wrong legal standard when it required them to plead discrimination that was "pervasive <u>and</u> regular." The Third Circuit agreed. While conceding that its case law was conflicting, the Third Circuit cleaned up the confusion and held, based on Supreme Court precedent, that the correct standard is "severe <u>or</u> pervasive." The Third Circuit explained that "'some harassment may be severe enough to contaminate an environment even if not pervasive; other, less objectionable conduct will contaminate the workplace only if it is pervasive.'"

In *Castleberry*, the parties disputed whether the supervisor's single use of the "n-word" is adequately "severe," and if one isolated incident is sufficient to state a claim under that standard. The Third Circuit answered in the affirmative, but explained that for it to serve as the basis of a harassment claim, the employee must allege the incident was so "extreme to amount to a change in the terms and conditions of employment." The Third Circuit's decision is in harmony with the Fourth, Seventh, Eleventh, and D.C. Circuits.

While the Third Circuit's decision creates a precarious situation for employers — it is important to keep in mind that in *Castleberry*, the supervisor's expletive was used in the same breath as his threat to terminate the employees (which ultimately occurred). Moreover, this case was based on a motion to dismiss (based on the allegations of the complaint), rather than a motion for summary judgment (filed after the close of discovery after all the facts are uncovered). Indeed, a claim of employment discrimination survives a motion to dismiss so long as the required *prima facie* elements have been established, whereas a motion for summary judgment involves a burden-shifting test in which an employer may offer a legitimate, non-discriminatory explanation for its action.

Each case is very fact specific. Employers should continue to provide anti-harassment training to employees and managers. Supervisors should be reminded to choose their words carefully and consider the significant impact of even a single racially charged comment in the workplace.

Contact the author at brandon.sher@leclairryan.com.

Superior Court Finds Workers Compensation Carrier Had No Duty to Defend Wrongful Death Action

by Catherine Bednar

In this action before the Suffolk Superior Business Litigation Session, the Plaintiff, Philadelphia Indemnity Insurance Company ("PIIC") provided a Commercial General Liability Policy to North Suffolk Mental Health Associated, Inc. ("North Suffolk"), while the Defendant, National Union Fire Insurance Company ("NUFIC") was North Suffolk's workers' compensation carrier. PICC sought to recover its defense costs in successfully dismissing a wrongful death civil action. North Suffolk provides mental health and rehabilitation services. The Estate of Stephanie Moulton brought the underlying civil action against numerous directors of North Suffolk on the grounds that the corporation's inadequate policies had caused Ms. Moulton's death at the hands of a North Suffolk patient.

NUFIC's policy was a standard workers' comp policy. Part One of the policy provided for the payment of any benefits required of the employer under the workers compensation law. Part Two provided coverage in tort actions for employees who had affirmatively opted out of the workers comp system at the time of hire. NUFIC denied coverage under the policy. PIIC then defended the civil action under a reservation of rights.

After PIIC's motion to dismiss was denied by the trial court, the case went before the Massachusetts Supreme Judicial Court on interlocutory appeal. The SJC held that the directors were immune from suit because they were deemed Moulton's employer for the purposes of the exclusivity provision of the workers compensation action, M.G.L. c. 152. PIIC then brought this action against NUFIC to recover its defense costs. In this subrogation action, PIIC argued North Suffolk's directors were additional insured under the workers comp policy, and further argued that there was at least a "possibility" the underlying claims were covered under either Part One or Part Two, thereby triggering NUFIC's duty to defend.

The Superior Court did not reach the issue of whether the directors were additional insureds under the policy, which identified only North Suffolk as the named insured. Instead, the Court held that NUFIC had no duty to defend the underlying action, as the Estate's claims were expressly outside the scope of coverage. With respect to Part One, the Court held the policy provided coverage only for claims for workers compensation benefits, and which benefits can only be claimed in the Department of Industrial Accidents. The Court cited *HDH Corp. V. Atlantic Charter Ins. Co.*, 425 Mass. 433 (1997), a prior decision which held a claim for monetary damages in a civil action - and not for workers compensation benefits – falls squarely outside of Part One's coverage and duty to defend. Regarding Part Two of the policy, the Court held an employer is not required to assert non-waiver as an affirmative defense; instead, a plaintiff must allege in the complaint that he or she opted out of the right to payment under the act. As there were no such allegations in the underlying action, NUFIC had no obligation to defend the claims under Part Two.

Relying heavily on the public policy set forth in prior cases, the Superior Court declined to expand a workers' comp carrier's obligation to defend claims falling outside the statutory framework of M.G.L. c. 152. The Superior Court noted c. 152 purpose is to provide an effective vehicle for providing benefits to injured workers, and stressed the increased costs to carriers and employers that would result from a broader interpretation of workers' compensation policies.

Philadelphia Indemnity Insurance Company V. National Union Fire Insurance Company Of Pittsburgh, Pa (Civil Action No. 2016-00045 BLS1)

Contact the author catherine.bednar@leclairryan.com.

U.S. Supreme Court Limits Venue Options for Patent Infringement Actions

by Gunnar G. Leinberg, Esq. and Bryan C. Smith, Esq.

The U.S. Supreme Court recently issued a unanimous decision in *TC Heartland LLC v. Kraft Food Group Brands LLC* related to proper venue for patent infringement actions against a domestic corporation. Prior to this decision, a patent plaintiff was essentially able to shop for a plaintiff-friendly venue for bringing a patent infringement action. These jurisdictions, which were often far removed from the defendant's state of incorporation, rarely allowed for a transfer of venue after the action was filed. The Supreme Court's decision now significantly narrows the available venues for patent infringement actions against domestic corporations, thereby limiting this type of forum shopping by patent plaintiffs.

The Patent Venue Statute

The Supreme Court's decision dealt with the proper interpretation of 28 U.S.C. § 1400(b), which is the patent-specific venue statute. This statue allows a patent infringement action to be brought in a judicial district: (1) where the defendant resides, or (2) where the defendant has committed acts of infringement and has a regular and established place of business. The Supreme Court's decision evaluated the question of where proper venue lies for a patent infringement lawsuit against a domestic corporation based on the interpretation of the term "resides" in the statute.

The Federal Circuit's Interpretation

Prior to *TC Heartland*, the Federal Circuit interpreted the term "resides" to incorporate the broader definition of corporate residence found in the general venue provisions for non-patent cases. The Federal Circuit's interpretation allowed a plaintiff to file a patent infringement action in

any judicial district in which the defendant corporation was subject to personal jurisdiction. Thus, a defendant's residence, according to the Federal Circuit's interpretation, could include a number of venues outside of the defendant's place of incorporation or actual place of business in which the defendant could be sued for patent infringement.

Procedural Background

TC Heartland LLC (TC Heartland) is an entity organized under Indiana law and headquartered in Indiana, while Kraft Food Group Brands LLC (Kraft) is an entity organized under Delaware law with a principal place of business in Illinois. Kraft sued TC Heartland for patent infringement in the District Court for the District of Delaware. Although TC Heartland shipped allegedly infringing products into Delaware, TC Heartland is not registered to conduct business in Delaware and has no meaningful local presence there.

TC Heartland sought to have the case dismissed or transferred to the District Court for the Southern District of Indiana arguing that it did not "reside" in Delaware under the terms of the patent venue statute. The Delaware District Court denied TC Heartland's motion, relying on the Federal Circuit's interpretation of the term "resides" in the patent venue statute, and determining that TC Heartland was subject to personal jurisdiction in Delaware based on TC Heartland's shipping of allegedly infringing products into Delaware. TC Heartland appealed the denial of its motion.

The Supreme Court's Decision

The Supreme Court held that the Federal Circuit's interpretation was improper, and that for purposes of the patent venue statute, a domestic corporation "resides" only in its state of incorporation. The Supreme Court relied on its prior precedent holding that the patent venue statute constituted the exclusive provision controlling venue in patent infringement proceedings and could not be supplemented or modified by general venue provisions. The Supreme Court further held that subsequent amendments to the general venue statutes did not alter the basis for the Supreme Court's precedent.

The Supreme Court's decision limits the proper venue against a domestic corporation to the corporation's state of incorporation, or a venue where the defendant has committed acts of infringement and has a regular and established place of business. This decision significantly limits the ability for plaintiffs to forum shop in order to take advantage of what may be perceived to be plaintiff-friendly jurisdictions.

Contact the authors at gunnar.leinberg@leclairryan.com and bryan.smith@leclairryan.com.

Back to Basics: Massachusetts Superior Court Tears Up Adhesion Contract and Applies Doctrine of *Forum Non Conveniens* to Dismiss California-Centric Dispute *by Michael T. Grant*

In *Oxford Global Resources, LLC v. Jeremy Hernandez*, 2017 WL 2623137 (Mass. Super.) a Superior Court judge in the Business Litigation Session allowed the defendant's motion to dismiss on the grounds of *forum non conveniens.* The judge disregarded the "choice-of-law" and "forum selection" clauses in the operative agreement between the parties, ultimately finding that California is the appropriate forum for any litigation between the parties.

Oxford Global Resources, a recruiting and staffing company based in Massachusetts, hired Hernandez, a California resident, to work in one of Oxford's California offices. As a condition of employment, Hernandez was required to sign an offer letter which stated that Massachusetts law governed the parties' agreement and that any lawsuit arising from the relationship must be brought in Massachusetts.

In 2016, Oxford sued Hernandez in Massachusetts Superior Court, alleging that Hernandez breached the parties' agreement by soliciting Oxford's customers on behalf of a competitor in California. Hernandez moved to dismiss on the grounds of forum non conveniens.

The judge allowed Hernandez's motion, finding that the "choice-of-law" and "forum selection" clauses in the agreement were void. As to the former, the judge found that the agreement was an adhesion contract for which Hernandez had no opportunity or bargaining power to negotiate terms. The judge also found that the "choice-of-law" clause was void as against California public policy because Massachusetts law was chosen by Oxford to circumvent California's strong public policy against non-competition (even though the judge noted that the non-competition clause at issue was violative of Massachusetts public policy as well). The judge found the forum selection clause unenforceable for the same reasons.

After disregarding the aforementioned contractual provisions, the judge applied the doctrine of *forum non conveniens* to conclude that it would be "in the interest of substantial justice" for the dispute to be adjudicated in California. The judge relied on the fact that virtually all of the witnesses and other sources of evidence were located in California (or otherwise electronically available). The judge also found that California has a much greater interest than Massachusetts with respect to resolving the parties' dispute. Consequently, the judge allowed Hernandez's motion to dismiss on grounds of *forum non conveniens.*

Oxford Global Resources is a useful reminder that the "adhesion contract" argument remains a viable weapon to challenge both substantive and procedural clauses in agreements. Contracting parties should consider this in the context of drafting and negotiating agreements.

Contact the author at michael.grant@leclairryan.com.

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