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Class Action

The Unheard Tree: The Struggle Over Unmanifested Defects in Consumer Class Actions

One of the most famous questions in philosophy is "if a tree fell in a forest and nobody was there to hear it, would it still make a sound?" A similar question dominates the world of consumer class actions. If a product contains a defect but the buyer never experiences the defect and the product performs satisfactorily for its useful life, does the buyer have a cause of action? Manufacturers and sellers insist that the answer is "no." Causation of injury is an essential part of any cause of action and no claim can succeed unless the plaintiff proves that the alleged defect manifested itself to create personal or economic harm. This view is strongly supported by the case authority and numerous cases have dismissed proposed class actions where the claimant never experienced the defect.

In many instances, however, the named plaintiff alleges that he or she has experienced the defect and can avoid dismissal or summary judgment. In almost all such cases, most of the purchasers have not and will not experience the defect. Defendants resist class certification, contending that the necessity of establishing loss causation for each class member means that the class cannot meet the requirement of Federal Rule of Civil Procedure 23(b)(3) that issues common to the class predominate over individual issues. Unfortunately, some courts have rejected this argument and have certified class actions despite the causation issue. These courts reason that the very fact of purchasing a product containing a defect in itself may give rise to "point-of-sale" damages that do not require the defect to manifest itself. They reach this breathtaking conclusion without careful consideration of whether the substantive causes of action permit the recovery of point-of-sale damages.

An example of this trend is found in *In re Whirlpool Corp. Front-Loading Washer Prods. Liab. Litig*, 678 F.3d 409 (6th Cir. 2012), where the court approved the certification of a class action of purchasers of washing machines that were allegedly susceptible to offensive odors caused by mold. In response to the defendant's contention that the majority of purchasers would never experience a mold problem, the Sixth Circuit Court of Appeals replied that the "class members may be able to show that each class member was injured at the point of sale upon paying a premium price for the [washing machines], even if the washing machines purchased by some members have not developed the mold problem." The Sixth Circuit did not show, however, that any cause of action under Ohio law, which governed the case, allowed recovery of such point-of-sale damages. Nor did the court address the copious authority requiring actual manifestation of the defect in order to state a cause of action. Unfortunately, it appears that Whirlpool is gaining some jurisprudential traction. The Seventh Circuit Court of Appeals recently approved the certification of a similar class action in *Butler v. Sears, Roebuck and Co*., 702 F.3d 359 (7th Cir. 2012).

A sounder approach to the issue was taken in *In re Toyota Motor Corp Hybrid Brake Marketing, Sales Practices and Prod. Liab. Litig*., 2013 WL 150205 (C.D. Cal. 2013). The court rejected certification of a class action alleging that certain brake systems were defective, finding that the predominance requirement was not satisfied. The district court noted that actual loss was a requirement of each of the causes of action alleged. A class member with a vehicle that had not experienced substandard performance had no valid claim. Merely asserting that the defect diminished the value of the vehicle did not provide a basis for relief.

The rule requiring that the defect manifest itself makes good jurisprudential and policy sense. Almost all consumer products have a limited useful life. If the consumer uses the product without incident during that useful life, he or she has received the benefit of his or her bargain, even if the product contains some latent "defect." If persons who have sustained actual loss as a result of the defect are compensated and then persons who have had no actual loss are also contemplated, the seller in effect pays for far more damage than was actually caused, an economically inefficient result that can only result in higher costs to consumers in the long run.

By ignoring the manifestation requirement and speculating on point-of-sale damages theories that are not supported by the substantive law, cases like Whirlpool create a disconnect between substantive and procedural law. They may even go so far as to effectively alter the substantive law in class actions cases in violation of the Rules Enabling Act. The cases deserve close and critical scrutiny.

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Class Action

Another Court Holds *Daubert* Analysis Required When Critical to Class Certification

This Alert focuses on a recent decision by the U.S. District Court for the Western District of Pennsylvania in a multidistrict price-fixing antitrust case, holding that a *Daubert* analysis is appropriate and necessary at the class certificate state when the expert testimony is critical to the determination of class certification. As the Alert explains, the issue regarding whether *Daubert* applies at the class certification stage is a critical one: the Circuits are split and the Supreme Court has recently granted certiorari on the issue.

With a split among the Circuits, no authoritative decision from the Third Circuit, and certiorari already granted by the U.S. Supreme Court on the issue, another district court has concluded that a thorough *Daubert* analysis is appropriate and necessary at the class certification stage when the expert testimony at issue is critical to the determination of class certification. *In re Chocolate Confectionary Antitrust Litig*., 08-MDL-1935 (M.D. Pa. Dec. 7, 2012).

In re Chocolate Confectionary Antitrust Litigation is a multidistrict price-fixing antitrust case brought pursuant to Section 1 of the Sherman Act, 15 U.S.C. § 1, as well as various state antitrust and consumer protection statutes. In that case, the Direct Purchasers alleged that Defendants, multi-national corporate entities who produce approximately 75 percent of America's chocolate confectionary products, conspired to implement three price increases on chocolate from 2002 through 2007. The Direct Purchasers sought to certify a class comprised of "All persons and entities who directly purchased single serving standard and King size chocolate candy for resale directly from Defendants between December 9, 2002 and December 20, 2007." Defendants argued that the diverse nature of the customer base made this matter unsuitable for class action disposition. According to Defendants, the complex mixture of promotional programs and customer-specific pricing negotiations made it impossible to determine the actual price paid for chocolate confectionary products with evidence common to the class.

Plaintiffs sought to prove predominance — that issues common to the proposed class members predominated over issues affecting individual class members, an element required for class certification under Federal Rule of Civil Procedure 23(b)(3) — through the use of expert testimony, which was based on econometric modeling and focused on the nature of the chocolate confectionary industry as purportedly conducive to price-fixing. Defendants moved in limine to exclude the expert opinion testimony, which testimony was critical to whether the plaintiffs could show that issues common to the proposed class members predominated over issues affecting individual class members.

The threshold question before the District Court was whether *Daubert v. Merrell Dow Pharmaceuticals, Inc*., 509 U.S. 579 (1993), and Federal Rule of Evidence 702 presented any barriers to the court's consideration of the plaintiffs' expert opinions, which were central to the class certification issue. In dicta, the U.S. Supreme Court, in *Wal-Mart Stores, Inc. v. Dukes*, 131 S.Ct. 2541 (2011), expressed its "doubt" of the soundness of the trial court's conclusion that *Daubert* did not apply at this stage. ("The District Court concluded that *Daubert* did not apply to expert testimony at the certification stage of class-action proceedings. We doubt that is so, but even if properly considered, [the expert witness's] testimony does nothing to advance respondents' case.")

The Circuits are split on the issue of whether *Daubert* is applicable at the class certification stage. The Seventh Circuit has held that when an expert's report or testimony is "critical to class certification," a district court "must perform a full *Daubert* analysis before certifying the class if the situation warrants." *American Honda Motor Co. v. Allen*, 600 F.3d 813, 815-16 (7th Cir. 2010). Similarly, the Fifth Circuit, in *Unger v. Amedisys Inc*., 401 F.3d 316, 323 n.6 (5th Cir. 2005), held that "[i]n many cases, it makes sense to consider the admissibility" of expert testimony at the Rule 23 certification stage, because "[i]n order to consider Plaintiffs' motion for class certification with the appropriate amount of scrutiny, the Court must first determine whether Plaintiffs' expert testimony supporting class certification is reliable."

In contrast, the Eighth Circuit, in *In re Zurn Pex Plumbing Products*, 644 F.3d 604, 612 (8th Cir. 2011), reached the opposite conclusion, noting that a full *Daubert* analysis at the class certification stage would be "impractical" because the parties had engaged in bifurcated discovery, resulting in a limited evidentiary record.

Whether *Daubert* applies at the class certification stage is an open question in the Third Circuit. While the Court of Appeals in *Behrend v. Comcast Corp*., 655 F.3d 182 (3d Cir. 2011), acknowledged that the issue was not before it, it nevertheless interpreted the Supreme Court's *Wal-Mart* decision "to require a district court to evaluate whether an expert is presenting a model which could evolve to become admissible evidence, and not requiring a district court to determine if a model is perfect at the certification stage." See id. at 204 n.13. The Supreme Court recently granted certiorari in *Behrend* on the issue of whether a district court may certify a class action without resolving whether the plaintiff class has introduced admissible evidence, including expert testimony, to show that the case is susceptible to awarding damages on a class-wide basis. 133 S. Ct. 24 (June 25, 2012).

Against this backdrop, after a thorough review of *Wal-Mart* and the Circuit Court decisions addressing the issue, the District Court in *In re Chocolate Confectionary Antitrust Litigation* held that a thorough *Daubert* analysis was appropriate and necessary at the class certification stage in light of the court's responsibility to apply a "rigorous analysis" to determine if the putative class had satisfied the requirements of Rule 23. The District Court was particularly persuaded by Judge Jordan's concurring and dissenting opinion in Behrend:

> [S]imple logic indicates that a court may consider the admissibility of expert testimony at least when considering predominance. A court should be hard pressed to conclude that the elements of a claim are capable of proof through evidence common to the class if the only evidence proffered would not be admissible as proof of anything.

655 F.3d at 215, n.18. The District Court then reasoned that the expert testimony at issue in the present case was integral to the court's determination of whether the Direct Purchasers could both prove and quantify their antitrust injury with evidence common to the class because the Direct Purchasers' proof of predominance rested entirely on the shoulders of their expert witnesses.

After a full *Daubert* hearing and extensive briefing, the District Court concluded that the expert opinions presented by plaintiffs' experts met the requirements of Rule 702 and the standard announced in *Daubert*, denied defendants' motions in limine to exclude the expert testimony concluding that any dispute as to the bases for these opinions or the merits of the experts' conclusions went to the weight, not to the admissibility, of the expert testimony, and certified the class.

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Class Action

Rule 23(b)(3) and the Superiority of Class Actions for Statutory Damage Claims Involving Technical Violations Resulting in No Actual Damages

Real World Impact of Class Actions for Technical Violations of Consumer Protection Laws

Mama Mia, a Florida restaurant, accepts credit cards as payment for meals. A customer provides his credit card to pay for his meal and receives a receipt from the restaurant. The receipt displays the customer's credit card number and expiration date. A month later the customer files a class action against the restaurant for violation of the Fair and Accurate Credit Transactions Act (FACTA) seeking statutory, but not actual damages, of not less than $100 and not more than $1,000. A month later, Mama Mia corrects its credit card receipts and truncates the credit card number on the receipt in compliance with FACTA. There is no claim that plaintiff or any other member of the proposed class suffered any actual damages because the receipts Mama Mia provided customers failed to comply with FACTA. Based on the proposed class, however, Mama Mia, a small business with about $40,000 in net assets, faces statutory damages of between $4,600,000 and $46,000,000.[1]

Dr. David Jansen is a new chiropractor trying to start his business. To attract patients he purchases a list of local fax numbers from a marketing company. He emails electronic faxes to the numbers on the list informing the recipients of his office and offering a free chiropractic massage for new patients. The doctor stops sending the unsolicited faxes after three months. Two years later, a recipient files a class action against the doctor for sending unsolicited faxes in violation of the Telephone Consumer Protection Act (TCPA). The recipient demands over $3,500,000 in statutory damages for the class for approximately 7,000 unsolicited faxes that were sent by the doctor. There is no claim that plaintiff or any other recipient suffered any harm from receiving the unsolicited faxes. No recipient other than the plaintiff filed a complaint against the doctor.[2]

Should Courts Consider Disproportionate Impact of Aggregate Statutory Damages to Actual Harm in Deciding Certification Under Rule 23(b)(3).

As these examples demonstrate, the aggregation of statutory damages through the class action mechanism can create potential damage awards that are ruinous to small businesses and, in some cases, large corporations, and grossly disproportionate to any actual harm caused by the technical violations of the consumer protection statutes giving rise to the statutory damage claims.[3]

Rule 23(b)(3) provides a mechanism for courts to address the propriety of aggregating statutory damages to resolve technical violations of consumer protection statutes that result in no actual harm and no damage to the plaintiff and proposed class. Before certifying a class under Rule 23(b)(3), the court must determine if the class action is superior to other available methods for fairly and efficiently adjudicating the controversy.[4] The question is: Should courts consider the proportionality of the potential statutory damages to the actual harm to determine if the proposed class action is superior to other available methods to adjudicate claims for technical violations of consumer protection statutes?

Divergent Views on Class Certification that Aggregates Statutory Damages for Technical Violations of Consumer Protection Statutes

The federal courts are divided on whether the proportionality of potential statutory damages to actual harm is an appropriate consideration in determining if the class action is the superior method to adjudicate such statutory claims. In the first and seminal case to address this issue, *Ratner v. Chemical Bank of New York Trust Co.*,[5] Judge Frankel ruled that the proportionality of potential statutory damages to actual damage or harm is a factor to consider to determine if the class action mechanism is superior under Rule 23(b)(3). Judge Frankel's approach has been widely followed in the 40 years since *Ratner*.[6] In other federal cases, however, including Seventh and Ninth Circuit decisions, courts have ruled that the proportionality of claimed statutory damages to actual damage or harm is not an appropriate factor to determine if the class action is superior under Rule 23(b)(3).[7] The difference in these approaches results from the court's view of the discretion afforded courts under Rule 23(b)(3) to determine if the class action is the superior mechanism to adjudicate a technical statutory violation given the legislative intent of the consumer protection statute at issue in the case.

Ratner and Progeny: Proportionality of Aggregate Statutory Damages to Actual Harm Is a Factor in Determining Superiority

In *Ratner*, the plaintiff claimed that his periodic Master Card credit card statement failed to disclose the nominal annual percentage rate on the outstanding principal balance on his credit card account in violation of the Truth in Lending Act (TILA). The bank corrected its Master Charge credit card customer account statements to include the previously excluded annual percentage rate in compliance with the TILA. Plaintiff suffered no damage or, at most, an inconsequential damage amount as a result of the alleged denial of plaintiff's ability to make an informed choice regarding credit cards in a market where the annual percentage rates varied little if at all. The parties agreed that plaintiff was individually entitled to recover the statutory minimum amount of damages and his attorneys' fees and costs.[8]

Plaintiff, nevertheless, sought to certify a class of approximately 130,000 Master Charge card customer account holders who were entitled, based on the minimum $100 statutory violation rate, to $13 million plus costs and attorneys' fees.[9]

Judge Frankel declined to certify the plaintiff's claim as a class action. He concluded that class certification was not the superior mechanism to resolve the TILA claim. He considered the proposed class recovery of statutory damages a "possibly annihilating punishment" unrelated to any actual harm to the purported class or benefit to the defendant for at most a "technical and debatable" violation of the TILA. The facts supporting these conclusions arguably went to the merits of the claimed violation, but they were undisputed facts before the court on the motion for class certification.

Judge Frankel concluded that under these circumstances there was no affirmative need or justification for the class action mechanism to augment the individual enforcement mechanism Congress provided for a $100 minimum statutory recovery, attorneys' fees, and costs in the TILA.[10]

This decision is consistent with Rule 23(b)(3). Rule 23(b)(3) provides that:

> A class action may be maintained if Rule 23(a) is satisfied and if: . . . (3) the court finds that the questions of law or fact common to class members predominate over any questions affecting only individual members, and that a class action is superior to other available methods for fairly and efficiently adjudicating the controversy. The matters pertinent to these findings include: (A) the class members' interests in individually controlling the prosecution or defense of separate actions; (B) the extent and nature of any litigation concerning the controversy already begun by or against class members; (C) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; and (D) the likely difficulties in managing a class action," (emphasis supplied).

The courts and parties are required to assess the relative advantages of alternative procedures to the class action mechanism to resolve the controversy. See notes to1966 amendments to Rule 23(b)(3). This assessment must include the factors listed in Rule 23(b)(3), but these factors are not exhaustive, rather the district courts have wide discretion to determine if the class action presents greater practical advantages to resolve the dispute than do other available dispute resolution mechanisms.[11]

Judge Frankel's decision in *Ratner* recognizes that the concentration of the litigation of the TILA claims in a class action was an undesirable mechanism to resolve the dispute consistent with Rule 23(b)(3). The aggregation of statutory damages for the class for the TILA violation was potentially "annihilating" for the bank, plaintiff suffered no actual damage or harm as a result of the violation, and there was no claim that the bank had profited from the violation. The claim was at most a technical violation that was admittedly corrected by the bank. No one else sued the bank for the claimed TILA violation and there was no claim for actual damages for the purposed class. The TILA provided an individual cause of action for actual or statutory damages, attorneys' fees, and court costs. At the time of *Ratner*, Congress was silent on the aggregation of statutory damages in a TILA class action.[12] The TILA neither provided for nor precluded a class action. Under these circumstances, Judge Frankel exercised his discretion to determine that a class action was not superior to an individual action to fairly and efficiently resolve this claimed TILA violation.

The Alternative View: Courts May Not Consider Proportionality of Aggregate Damages to Actual Harm in Deciding Certification

Conversely, the Seventh Circuit vacated a district court decision denying class certification in part because the district court had considered the potential liability of a defendant faced with billions of dollars in statutory damages for technical violations of the Fair Credit Reporting Act (FCRA). For the Seventh Circuit, Rule 23 was a procedural devise that must give way to congressional intent under the FCRA. For this reason, the court concluded that it was inappropriate for the district court to use Rule 23 to deny class certification because, in the court's view, the district court did not approve of aggregate damages for what the district court deemed trivial violations of the FCRA.

Plaintiff received a credit solicitation from GMAC Mortgage Corporation for a loan secured by a mortgage on her house. GMAC obtained plaintiff's name and address from a credit bureau. Plaintiff sued GMAC contending the solicitation was not a firm offer of credit and, thus, it violated the FCRA. She had only received the unsolicited mailing, she did not take the offer of credit or pay GMAC anything, and she did not claim actual damages. Instead, she demanded statutory damages ranging from $100 to $1,000 for a potential class of 1.2 million. Plaintiff and GMAC settled, but the district court refused to consider the settlement, finding that the class should not be certified.[13]

The district court found the aggregation of statutory damages potentially for billions of dollars for the class an inappropriate mechanism to resolve the alleged FCRA violations resulting in unwanted credit solicitations to the class. For the Seventh Circuit, the denial of class certification based in part on the potential effect of the aggregation of statutory damages undermined the FCRA. Congress defined the acts or omissions that violated the FCRA, provided for statutory damages for such violations when actual damages did not exist or were not proven, and failed to cap the aggregation of damages for violations in a class action. Courts were obligated to enforce the FCRA, even for what the district court deemed technical FCRA violations, therefore, the Seventh Circuit held the district court inappropriately considered the potential impact of aggregate statutory damages in denying class certification.

The consideration of disproportionate statutory damage awards, in the Seventh Circuit's view, was appropriate only after class certification, when the award may be reduced if it was unconstitutionally excessive based appropriately at that time on an evaluation of the merits of the defendant's conduct and exposure under the FCRA.[14] Apparently, for the Seventh Circuit, the consideration of the proportionality of the aggregate statutory damages to the actual damage caused by the alleged technical statutory violation was an improper merits determination.[15]

The Ninth Circuit followed the Seventh Circuit in reversing the denial of class certification for violations of the FACTA by American Multi-Cinema, Inc. (AMC).[16] AMC allegedly printed more than the last five digits of consumer credit or debit card numbers on electronically printed movie receipts. Plaintiff was not injured and claimed no actual damages for the proposed class. Plaintiff sought statutory damages between $29 million and $290 million for the proposed class. After the lawsuit was filed, AMC corrected the printing error in its receipts and complied with the FACTA. The district court refused to certify the class because the potential liability was enormous and disproportionate to any actual harm caused by a technical FACTA violation that was subsequently corrected. The Ninth Circuit held that the district court abused its discretion in considering these grounds to deny class certification. Quoting the Seventh Circuit, the Ninth Circuit stated that the FACTA "must be enforced rather than subverted," until Congress amended the FACTA in response to such class actions.[17]

For the Ninth Circuit, legislative intent displaced the district court's admittedly "wide" discretion in deciding whether to certify a class under Rule 23.[18] Because there is a presumption that class actions are available in all federal court civil actions, the Ninth Circuit presumed further that Congress intended class relief to be available under the statute even though Congress was silent with respect to the aggregation of statutory damages in a class action. The Ninth Circuit reasoned that the class action mechanism was consistent with the legislative intent to compensate individuals for violations without requiring them to prove actual harm where statutory damages were available and that such class actions also served the purpose of deterring violations.[19] The Ninth Circuit further reasoned that if Congress intended otherwise, Congress would have imposed or could later impose a cap on the total amount of aggregate damages.[20]

Building a Case for Application of Ratner to Oppose Certification Under Superiority Analysis

It is difficult to reconcile these two approaches to the certification of classes under Rule 23(b)(3) in cases involving the aggregation of statutory damages for technical violations of consumer protection statutes. At least one federal court in the Ninth Circuit has tried, declining to follow, and distinguishing the Ninth Circuit decision in *Bateman* because it involved a billion-dollar movie company compared to the small municipality before it from whom plaintiff wanted to recover $15 million in statutory damages for violating the FACTA by printing credit card numbers on parking receipts.[21]

This distinction, however, ignores the fact that an award of millions of dollars in statutory damages can be just as potentially devastating to a large company as to a small one or a public entity. This district court decision in the Ninth Circuit after Bateman does show, nevertheless, that district courts may be willing to consider the Ratner approach even in the Ninth or Seventh Circuits when faced with motions to certify classes for potentially annihilating statutory damages for technical violations of consumer protection statutes.[22] The inclination can be supported by the defense to the motion for class certification in such cases.

In *Ratner*, the facts related to the TILA violation were undisputed; there was no issue that the claimed TILA violation had occurred, that it had been corrected, and that neither the plaintiff was harmed nor the defendant benefited by the claimed TILA violation.[23] In *Murray*, the parties settled the claimed FCRA violation, but there was no indication that the FCRA violation was admitted, corrected, or that the defendant did not benefit from it even though the plaintiff sought only statutory damages not actual damages for the allegedly improper credit solicitations under the FCRA.[24] This distinction favors consideration by courts of the proportionality of statutory damages to actual harm or damage for claimed violations of consumer protection statutes in determining if class certification is the superior method to resolve the controversy under Rule 23(b)(3).

To begin with, defendants should correct statutory violations if they are discovered after a class action is filed, better yet, implement or enhance an existing compliance program to detect and correct any technical statutory violations before they occur. If there was a statutory violation, however, admit it, demonstrate that it has been corrected at or by the time of class certification, and that a compliance program has been established or enhanced to ensure future compliance. Often for technical statutory requirements, the defendant will also be able to demonstrate that there was no benefit from the violation or harm to the plaintiff or class. Under these circumstances, courts arguably should consider the proportionality of the claimed statutory damages to the actual damage or harm caused to determine under Rule 23(b)(3) if the class action is the superior method to fairly resolve the controversy. In such cases, individual claims for statutory damages, attorneys' fees and costs under the statute provide an adequate and fair remedy.[25]

Rule 23(b)(3) requires district courts to consider if the class action mechanism is superior to other available means to resolve a dispute. That Rule further requires district courts to consider the "fairness" as well as the "efficiency" of the class action mechanism to determine if it is superior to available dispute resolution alternatives such as individual claims for actual or statutory damage, attorneys' fees, and costs.[26] The determination of the fairness of the aggregation of statutory damages in a class action does not inappropriately infringe on the merits of the underlying conduct when the facts related to that conduct are undisputed on the motion for class certification.

If, as the Seventh Circuit recognized, courts can consider whether the award is unconstitutionally excessive after certification, under such circumstances, nothing will have changed with respect to the defendant's conduct or exposure after certification.[27] Courts, therefore, should consider if the proposed statutory damage award to the class raises due process concerns in determining the fairness of the class action mechanism to analyze the superiority of the class action under Rule 23(b)(3). Indeed, the court's wide discretion on class certification includes an inquiry into the merits when necessary to determine if the requirements of Rule 23 have been satisfied.[28] As a result, as Judge Frankel recognized in *Ratner*, district courts should consider the disproportionate impact of aggregating statutory damages in a class action for demonstrated technical violations of a statute in determining if a class action is superior to alternative dispute resolution mechanisms under Rule 23(b)(3).

The courts were further divided in their views on whether consideration of the proportionality of statutory damages to the actual harm in determining if the class action was a superior dispute resolution mechanism was consistent with legislative intent. To the Seventh and Ninth Circuits, this factor undermined legislative intent because in their view the disproportionality of aggregate statutory damages to actual damages was inherent in the statute–not the certification of the class under Rule 23. They noted that Congress had limited aggregate awards in some statutes, but not in others, indicating to them an intent not to limit aggregate class awards in those statutes lacking any such limitation. They also viewed consideration of this factor in denying class certification on superiority grounds inconsistent with the purposes of the legislation.[29] None of these grounds should be insurmountable when opposing class certification for technical violations of consumer protection statutes.

It bears emphasis that in the legislation addressed by these courts, Congress neither expressly approved nor disapproved class relief. Congress, therefore, did not expressly prohibit the consideration of the disproportionate award of statutory damages to the actual harm caused by the statutory violation in the superiority analysis under Rule 23(b)(3).[30] If Congress is presumed to know that class actions are available in federal civil actions, as the Ninth Circuit held in Bateman, then Congress must also be presumed to know the requirements for class certification under Rule 23.[31]

As such, if by its silence Congress intended class relief to be available, it did so only if the express requirements for class certification were met as determined by the federal district courts. This includes the requirement that the claimant demonstrate that the class action mechanism was superior to the alternative methods available for the fair and efficient resolution of the dispute. In most if not all cases, this means a determination if a class action is superior to the individual cause of action that Congress expressly provided for statutory violations for actual or statutory damages, attorneys' fees, and costs. Thus, consideration of the proportionality of aggregated statutory damages to actual damage or harm should not be considered an inherent conflict with the statute that undermines legislative intent when Congress is silent with respect to the class action mechanism.

Courts have recognized that the purpose of individual remedies under consumer protection statutes is to compensate for harms caused by violations even when damages are difficult to prove and to deter statutory violations.[32] These purposes are not undermined when the proportionality of aggregate damages to actual harm is considered in determining the superiority of class action relief under circumstances involving a technical violation of the statute that has been corrected. The plaintiff can be adequately compensated by statutory damages, and attorneys' fees and costs under the statute. The difficulty in proving actual damages is addressed by the express provision for statutory damages and any disincentive to bring the action is addressed by the recovery of attorneys' fees and costs.[33]

There is no apparent reason these individual statutory remedies should be deemed inadequate absent the availability of the class action relief when Congress expressly provided this remedy. When the violation is technical, and it has been corrected, then arguably too the deterrent purpose of the statute has been satisfied.[34] The denial of class certification for class-wide technical violations does not risk "underdeterrence," as the Ninth Circuit reasoned, if the technical violation is eliminated and compliance measures are enacted or enhanced to ensure the technical violation is corrected for all consumers.[35] For these reasons, courts should consider compliance with the purposes of the consumer protection statute when the technical violation is corrected and the individual plaintiff has a remedy for damages, fees, and costs in determining if class wide relief is superior under Rule 23(b)(3).

Conclusion

As a practical matter, the viability of the proportionality of statutory damages to actual harm for technical violations of consumer protection statutes as a factor in determining the superiority of the class action mechanism under Rule 23(b)(3) remains an open issue with courts divided on the propriety of considering this factor. The defense of a class action on this ground, however, can be enhanced. If the conduct is not disputed and it is not disputed that the conduct is inconsistent with the requirements of the consumer protection statute, then, the conduct should be changed to eliminate the statutory violation and place the conduct in compliance with the statutory requirements. This should be demonstrated at least at the time of class certification including the lack of any benefit as a result of the conduct. This should be the case for most violations of a purely technical statutory requirement when the plaintiff claims no actual damages or harm for the plaintiff or the class. Under these circumstances on a class certification motion, the argument should be made that the class action mechanism is not the superior method to resolve the controversy over a technical violation of the consumer protection statute. Indeed, the American Law Institute has recognized that aggregation is not an end unto itself, rather, aggregation is a means by which courts may promote justice under the law more fully.[36]

The consideration of the proportionality of aggregate statutory damages to actual damage or harm for technical violations of consumer protection statutes in determining if a class action is superior to alternative dispute resolution mechanisms under Rule 23(b)(3) is consistent with this principle.

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1. *Leysoto v. Mama Mia I, Inc.*, 255 F.R.D. 693 (S.D. Fla. 2009).
2. *Chiropractic and Sports Injury Center of Creve Coeur, P.C. v. All American Painting, Inc.*, 12-409 (Petition for Writ of Certiorari to S. Ct., October 1, 2012).
3. There are several federal consumer protection statutes establishing statutory damages, including the FACTA, 15 U.S.C. § 1681, the TCPA, 47 U.S.C. § 227, the Truth in Lending Act (TILA), 15 U.S.C. § 1601, the Drivers' Privacy Protection Act, 18 U.S.C. § 2721; and the Fair Debt Collection Practices Act (FDCPA), 15 U.S.C. § 1692(a)(2).
4. Class action plaintiffs must of course demonstrate the other prerequisites to class certification under Rule 23(a) and 23(b)(3), however, for purposes of this article that demonstration is assumed. Also, this article does not address proposed class actions, if any, for statutory damages for violations of consumer protection statutes under Rule 23(b)(1) or 23(b)(2).
5. 54 F.R.D. 412 (S.D.N.Y. 1972).
6. *See, e.g., Watkins v. Simmons and Clark, Inc.*, 618 F.2d 398 (6th Cir. 1980); *Wilson v. American Cablevison of Kansas City, Inc.*, 133 F.R.D. 573 (W.D. Mo. 1990); *Shroder v. Suburban Coastal Corp.*, 729 F.2d 1371 (11th Cir. 1984). *Accord Parker v. Time Warner Entertainment, Co.*, 331 F. 3d 13 (2d Cir. 2003); *Klay v. Humana, Inc.*, 382 F. 3d 1241 (11th Cir. 2004), *abrogated in part on other grounds by Bridge v. Phoenix Bond & Indemnity Co.*, 553 U.S. 639 (2008). *London v. Wal-Mart Stores, Inc.*, 340 F. 3d 1246 (11th Cir. 2003).
7. *Murray v. GMAC Mortgage Corp.*, 434 F. 3d 948 (7th Cir. 2006); *Bateman v. American Multi-Cinema, Inc.*, 623 F. 3d 708 (9th Cir. 2010).
8. *Ratner*, 54 F.R.D. at 413, n. 2, 414.
9. Id.
10. *Ratner*, 54 F.R.D. at 416.
11. Id. *see also, e.g., Klay*, 382 F.3d at 1251; *Castano v. American Tobacco Co.*, 84 F.3d 734, 740 (5th Cir. 1996).
12. Congress subsequently amended the TILA to place a cap on recovery of statutory damages in a class action for violations of the TILA. 15 U.S.C. § 1640(a) (1976).
13. *Murray v. GMAC Corporation*, 434 F. 3d 948, 953-54 (7th Cir. 2006).
14. *Id.*
15. *See, e.g., Eisen v. Carlisle & Jacquelin*, 417 U.S. 156, 177-78 (1974) (a court may not pass on the merits of the case in exercising its discretion under Rule 23).
16. *Bateman v. American Multi-Cinema, Inc.*, 623 F.3d 708 (9th Cir. 2010).
17. *Id.*at 715.
18. Id. at 716.
19. Id. at 716-719.
20. *Id.*
21. *Rowden v. Pacific Parking Systems, Inc.*, 282 F.R.D. 581 (C.D. Cal. 2012).
22. It bears some emphasis that with respect to class actions under the FACTA, the Ninth Circuit's approach in *Bateman* is currently the majority view. *See, e.g., Armes v. Sogo, Inc., No. 08-C*-0244 (E.D. Wis. 2011). *But cf. Ehren v. Moon, Inc.*, 2010 BL 286818 (S.D. Fla. 2010).
23. *Ratner*, 54 F.R.D. at 413, 416, n. 6.
24. *Murray*, 434 F.3d at 949.
25. *Ratner*, 54 F.R.D. 416, n.6. *See also Leysoto*, 255 F.R.D. at 694.
26. F.R.C.P. 23(b)(3).
27. Due process concerns are not academic when defendants face aggregate statutory damages in proposed class actions for what amounts to technical violations of statutes. Such aggregate damages may be so disproportionate to the actual harm that they are no longer compensatory but rather punitive for what is essentially accidental or mistaken conduct in disregard of the statutory requirements. *Murray*, 434 F.3d at 953-54 ("An award that would be unconstitutionally excessive may be reduced.").
28. *Leysoto*, 255 F.R.D. at 696; *Heffner v. Blue Cross & Blue Shield of Ala. Inc.*, 443 F. 3d 1330, 1337 (11th Cir. 2006); *Love v. Turlington*, 733 F. 2d 1562, 1564 (11th Cir. 1984).
29. *Murray*, 434 F.3d at 953-54; *Bateman*, 623 F.3d at 716-719.
30. The Seventh Circuit failed to even reference the superiority analysis in Rule 23(b)(3) in *Murray.*
31. *Bateman*, 623 F. 3d at 717.
32. *See, e.g., Bateman*, 623 F. 3d at 718-19; *Harris v. Mexican Specialty Foods, Inc.,* 564 F. 3d 1301, 1312 (11th Cir. 2009).
33. *See, e.g., Ratner*, 54 F.R.D. at 416.
34. Id.

35. *Bateman*, 623 F 3d at 719. The Ninth Circuit further held in *Bateman* that the district court's reliance on the movie theatre company's good faith compliance with the FACTA was inconsistent with the intent of FACTA because Congress failed to include a "safe harbor" for good faith compliance, failed to limit aggregate damages, and because the court presumed the company's speedy compliance was promoted at least in part by the specter of a substantial damage award. *Id.* at 723. Arguably, the Ninth Circuit reads more into what Congress did not expressly provide for in the FACTA than what Congress actually said in the Act. Again, Congress provided expressly for an individual remedy, not a class remedy, including statutory as well as actual damages, attorneys' fees, and costs. Congress was well aware of the availability of class action relief under Rule 23, consistent with the specific rule requirements, including the superiority analysis of Rule 23(b)(3). It is difficult to read more into the FACTA than this. Further, if the movie company was motivated to comply with the FACTA by the specter of the class action damages sought by plaintiff the deterrent effect intended by Congress was achieved by the company's compliance with the FACTA. Denying class certification after such compliance was brought about because the aggregate
36. Principles of the Law of Aggregate Litigation, § 1.03, comment a (2010)

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Class Action

Don't "Put the Cart Before the Horse": Supreme Court Rejects Amgen's Argument that Securities Fraud Plaintiffs Must Prove Materiality of Alleged Misrepresentations at the Class Certification Stage

On February 27, 2013, the Supreme Court issued a split decision in *Amgen Inc. v. Conn. Retirement Plans and Trust Funds* upholding the Ninth Circuit's decision that plaintiffs in securities fraud actions based on the fraud-on-the-market theory of reliance do not have to *prove* the materiality of alleged misrepresentations or omissions regarding the securities at issue to certify a class under Federal Rule of Civil Procedure 23(b)(3). Acknowledging that materiality is essential to the fraud-on-the-market presumption itself, the Court nonetheless concluded that materiality need not be proven at the class certification stage because it is a question common to all class members: "failure of common proof on the issue of materiality ends the case for the class."

On February 27, 2013, the Supreme Court issued a split decision in *Amgen Inc. v. Conn. Retirement Plans and Trust Funds*, No. 11-1085, 2013 U.S. LEXIS 1862 (February 27, 2013) upholding the Ninth Circuit's decision that plaintiffs in securities fraud actions based on the fraud-on-the-market theory of reliance do not have to *prove* the materiality of alleged misrepresentations or omissions regarding the securities at issue to certify a class under Federal Rule of Civil Procedure 23(b)(3)[1]. Acknowledging that materiality is essential to the fraud-on-the-market presumption itself, the Court nonetheless concluded that materiality need not be proven at the class certification stage because it is a question common to all class members: "failure of common proof on the issue of materiality ends the case for the class." *Id.* at *34.

Background

Connecticut Retirement Plans and Trust Funds ("Connecticut Plans") sued Amgen Inc. ("Amgen") alleging that Amgen made misrepresentations and misleading omissions regarding the safety, efficacy, and marketing of two of its flagship drugs. The Connecticut Plans sought to represent all investors who purchased Amgen stock between the date of the first alleged misrepresentation (April 22, 2004) and the date of the last alleged corrective disclosure (May 10, 2007). *Id.* at *16. The District Court granted Connecticut Plans' motion and certified the proposed class under Rule 23(b)(3). Amgen moved for interlocutory appeal from the District Court's class-certification order. Amgen argued that reliance cannot be proved on a class-wide basis unless materiality is also proved because, by definition, a class member could not rely on an immaterial representation. The Court of Appeals did not accept this argument and affirmed the class certification.

The Supreme Court granted Amgen's petition for certiorari, 132 S. Ct. 2742 (2012), citing a split among the Courts of Appeals. While the Seventh Circuit had held that plaintiffs must "plausibly allege-but need not prove" materiality at the certification stage, *Schleicher v. Wendt*, 618 F.3d 679 (7th Cir. 2010), the Second and Fifth Circuits had required proof of materiality, or allowed defendants to rebut materiality on a certification motion. *See In re Salomon Analyst Metromedia Litig.*, 544 F.3d 474 (2d Cir. 2008); *Oscar Private Equity Invs. v. Allegiance Telecom, Inc.*, 401 F.3d 316 (5th Cir. 2005).

"Fraud-On-The-Market" Theory

The fraud-on-the-market theory was created by the Supreme Court in its decision in *Basic Inc. v. Levinson*, 485 U.S. 224 (1998). There, the Court held that "if a market is shown to be efficient, courts may presume that investors who traded in that market relied on public, material misrepresentations regarding those securities." *Id.* at 245. This theory is important to securities fraud class actions because, as the Court notes in *Amgen*, requiring a showing of individual reliance for each class member would likely "overwhelm questions common to the class" and preclude certification of a class action. *Amgen* at *14. Materiality is both an element of a securities fraud claim under Rule 10b-5, and "an essential predicate of the fraud-on-the-market" theory. *Id.*at *20.

The Supreme Court last addressed the showing required by plaintiffs invoking fraud on the market at the class certification stage in *Erica P. John Fund, Inc. v. Halliburton Co.*, No. 09-1403, 2011 U.S. LEXIS 4181 (June 6, 2011). In *Halliburton*, the Court held unanimously that securities fraud plaintiffs do not need to prove loss causation to obtain class certification, noting however, that to invoke the fraud-on-the-market theory, plaintiffs did have to prove the elements of market efficiency and the public nature of an alleged misrepresentation.[2] The Court side-stepped the issue of whether plaintiffs must prove other elements of fraud-on-the-market theory—including reliance—or whether defendants may rebut these elements at the class certification stage, admonishing that, "we need not, and do not, address any other questions about *Basic*, its presumption, or how and when it must be rebutted." 2011 U.S. LEXIS at *19.

By contrast, in *Amgen,* the Court addressed these questions left open in *Halliburton*. Handing the defense a significant setback, the Court defined the issue on certification as whether "proof of materiality is needed to ensure that the questions of law or fact common to the class will 'predominate over any questions affecting only individual members.'" *Amgen* at *2. On the merits, the Court held the answer is "clearly 'no'" for two reasons. First, the question of materiality is an objective one, to be proven through evidence common to the class. Second, a failure of proof on materiality will not result in a predominance of individual questions; instead, such a failure will end the case for all class members. *Id.* at *[3].

Responding to the dissents' suggestion that materiality must be assessed at the certification stage as an element of the fraud-on-the-market theory, the majority focused on the narrow question presented on certification —whether common questions predominate over questions affecting only individual class members, allowing certification of a class for monetary damages under Rule 23(b)(3). The majority of the Court reasoned that plaintiffs' ultimate inability to prove materiality on summary judgment or at trial, while fatal to the entire case, is not a "fatal dissimilarity" among class members that would render the use of the class-action device inefficient or unfair so as to defeat certification. *Id.* at *26-27. Thus, the Court held that materiality is not an issue relevant to the predominance analysis required to decide certification under Rule 23(b)(3).

The Court contrasted materiality from the other elements of the fraud-on-the-market theory required by *Halliburton* to be addressed at certification—market efficiency and publicity—noting that, although failure to prove these elements might defeat a finding of commonality and certification, such a failure would not by itself end the case on the merits. *Amgen* at *33. For example, if the defendant's alleged misrepresentations or omissions were not aired publicly, or if the market for its securities were not efficient, individual plaintiffs could not invoke the fraud-on-the-market presumption of reliance, but might still be able to establish individual reliance, along with all of the remaining requisite elements of a Rule 10b-5 claim. Conversely, a failure on materiality would end the case for all plaintiffs in the potential class.

The Court gave short shrift to *Amgen's* public policy argument that certification often leads to *in terrorem* settlements, warranting closer scrutiny before granting certification. The Court noted that Congress has addressed perceived litigation abuses with the enactment of the Private Securities Litigation Reform Act of 1995, 15 U.S.C. § 78u–4 (2006), imposing certain burdens on plaintiffs, and the Securities Litigation Uniform Standards Act of 1998, 15 U.S.C. §78bb(f)(1) (2006). Yet Congress has never opted to legislatively reject *Basic* or its presumption of classwide reliance. *See Amgen* at *38. Therefore, the Court did not think it "appropriate" for the judiciary to reinterpret the tenets of securities law where Congress has declined to do so. *Id.* at *39.

The Justices' comments at oral argument had revealed a philosophical split and gave rise to speculation that the Court might take the occasion to do what Congress has not: revisit *Basic* and the fraud-on-the-market theory's appropriateness as a whole. Indeed, Justice Alito's concurring opinion notes that although the petitioners did not ask the Court to revisit *Basic'*s fraud-on-the-market presumption, reconsideration of *Basic* itself may be appropriate as "more recent evidence suggests that the presumption may rest on a faulty economic premise." *Amgen* at *49. Likewise, Justice Scalia's dissent leaves no doubt of his view of the fraud-on-the-market theory, suggesting that "some" consider the four-justice opinion in *Basic* "regrettable" and warning that the Court's opinion expands the consequences of *Basic* "from the arguably regrettable to the unquestionably disastrous." *Amgen* at *54-55.

In the end, the Justices agreed that materiality is an element of the fraud-on-the-market theory, but differed in their views of when materiality must be proven or may be rebutted. The majority held that adjudicating materiality at the certification stage would "have us put the cart before the horse." *Id.* at *9. The dissents challenged that characterization with Justice Thomas asserting that the majority, rather than Amgen, would put the cart before the horse. In his view, joined by Justice Kennedy, the plaintiff who cannot prove materiality should never get to the merits, because without materiality, fraud-on-the-market does not apply, individual questions of reliance predominate, and certification is not possible. *Id.* at *71. Similarly, Justice Scalia's dissent would have required a plaintiff to establish at the class certification stage all of the elements of the fraud-on-the-market theory, including materiality, if the presumption is relied upon to justify certification. *Id.* at *51-53.

Analysis

The majority position in *Amgen* includes justices all along the ideological spectrum, and seems at first glance to be an exception to the recent general trend of cases limiting the availability of class actions and favoring defendants. From a class-action plaintiffs' perspective, the *Amgen* decision also appears to be a win on two key fronts: the fraud-on-the-market presumption is preserved for the time being, and the battle over materiality is removed from the certification landscape. Whether *Amgen* actually marks an end point generally to decisions disfavoring class actions, however, may not be known until the outcome of *American Express v. Italian Colors Restaurant*, No. 12-133, 2012 US LEXIS 8697 (Nov. 9, 2012).3 Further, on March 25, the Court is scheduled to hear arguments in *Oxford Health Plans LLC v. Sutter*, cert. granted, No. 12-135, 2012 U.S. LEXIS 9417 (December 7, 2012)[4] over whether an arbitrator correctly ruled that the parties had consented to authorize class arbitration of pay disputes under the broad language of their individual plans requiring arbitration. This case may finally test whether the Court will apply limits to an arbitrator's power under the Federal Arbitration Act.

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1. Rule 23(b)(3) requires that “questions of law or fact common to class members predominate over any questions affecting only individual members.”
2. See our prior alert here: http://www.nixonpeabody.com/files/Class_Action_Alert_06_08_2011.pdf.
3. See our prior alert here: http://www.nixonpeabody.com/landmark_class_action_waiver_case
4. Docket available at: http://www.supremecourt.gov/Search.aspx?FileName=/docketfiles/12-135.htm

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Data Privacy

Ukraine's New Data Protection Law Amendments and Other Important Recent Developments

Some two-and-a-half years have passed since Ukraine enacted its Data Protection Law[1]. Although the ideas behind the Data Protection Law were really positive and progressive, during its short life, the law has received a lot of criticism. Much of this criticism relates to a number of unclear and unenforceable provisions, as well as some burdensome procedures that businesses were required to follow.

Given the imperfections of the Data Protection Law, not only companies but also governmental bodies, in particular the State Service of Ukraine for Protection of Personal Data (the ''Data Protection Authority''), have suffered. The Data Protection Authority was required to process millions of applications for the registration of databases, a demand with which it has not been able to cope. Having learned from the experience of the Europe Union, as well as that of neighboring countries, the Parliament of Ukraine decided to follow the rest of the progressive world, and in late December 2012 substantially amended the Data Protection Law[2](the ''New Law'')

The New Law became effective from January 1, 2013.

This article considers the most important amendments of the Old Law brought about by the New Law, and reviews some other changes in Ukrainian legislation from the past year that impact data protection procedures.

The New Law — What's New?

Coverage

Unlike before, when the Old Law quite narrowly protected only personal data contained in certain databases, the New Law covers all personal data, irrespective of their location. This is an important step toward international practice, and means that a data subject does not have to clarify whether his or her personal data is contained in a database before he or she can claim protection.

Consent of Data Subjects

One of the most controversial aspects of the Old Law involved the form in which a data subject had to give consent to the processing of his or her personal data. The wording offered by the Old Law was very vague, and in fact envisaged only a ''documented form'' of consent. This meant that collecting electronic or web consents was quite an issue, and, in practice, to be safe, companies tended to collect paper consents, which was quite burdensome.

The New Law clarifies this requirement, and now a data subject can give his or her consent in any form that can be confirmed. From a practical standpoint, this amended definition makes life much easier for data controllers, as they can now lawfully collect consents from data subjects in a more ''modern'' way, i.e., via emails, web resources, video records, etc., provided they can technically confirm that such consent was really granted.

Employment Relations

Until recently, another difficult issue related to the registration of databases containing personal data. The Old Law required all such databases to be registered with the Data Protection Authority, irrespective of the nature of the relations between data subjects and data controllers. Thus, even employers' databases, which naturally contained employees' personal data, were subject to mandatory registration. That requirement led to a situation in which the Data Protection Authority had to review and process an enormous number of applications for the registration of employers' databases from all over Ukraine. Consequently, the regulator became so overloaded that currently it is more than a year behind in processing applications[3].

The New Law corrects this ridiculous situation, exempting data controllers from having to register those databases connected to employment relations. As a matter of practice, those data controllers whose employment-related databases have not yet been registered by the Data Protection Authority are recommended to withdraw their applications. This will ease the burden on the Data Protection Authority and also enable those databases which are still subject to mandatory registration to be registered in a shorter time.

Registration of Databases

The New Law extends the term for registration of databases to 30 business days (it had been 10 days under the Old Law) and removes the obligation of the Data Protection Authority to notify applicants about the receipt of their applications. In addition, the New Law supplements the list of information to be disclosed by data controllers when applying for registration by adding three more points: 1) information about the content (i.e., the type of information processed, not the personal data itself) of the personal data processed; 2) information about third parties to which personal data are transferred; and 3) information about cross-border transfers of personal data.

It is worth noting that the first additional point has already been included in the standard application form developed by the Data Protection Authority, and the requested information is, in fact, being disclosed by applicants. However, the two other points are new, and they are to be added to notifications from January 1, 2013.

Cross-Border Transfers

While the Old Law contained very vague and sometimes ambiguous provisions regarding international data transfers (for instance, concerning the necessity to seek approval of the transfer by the regulator), the New Law clarifies this issue to a certain extent. Significantly, the New Law eliminates the requirement for Data Protection Authority approval of data transfers abroad.

Although the New Law still requires that personal data be transferred only to countries which provide an adequate level of data protection, it now clarifies what those countries are. Specifically, the New Law refers to member states of the European Economic Area (EEA), as well as all other countries that have joined the Council of Europe Convention for the Protection of Individuals with regard to Automatic Processing of Personal Data (the ''Convention''). The above list is not exhaustive, and the New Law provides that other countries which provide an adequate level of data protection (i.e., non-EEA members and non-members of the Convention) will be defined separately by the Cabinet of Ministers of Ukraine. This is really important in terms of business activity in Ukraine, as important business relations have been developed with, inter alia, the United States and Canada, which are not members of the EEA or the Convention. There is a chance they will be included in the additional list.

Another amendment regarding cross-border data transfers relates to the grounds for transfers. Grounds for transfers were not directly defined as regards international data transfers, and it was only implied that the data subject should provide his or her consent to such an action. The New Law offers five alternative actions which may serve as legal grounds for cross-border data transfers, and gives business entities more room to process personal data internationally. These five actions are: 1) providing unambiguous consent by the data subject; 2) concluding or fulfilling an agreement between the data controller and a third party for the benefit of the data subject; 3) protecting vital interests of the data subject; 4) protecting the public interest or pursuing legal remedies; and 5) providing relevant guarantees by the data controller regarding non-interference into the private and family life of the data subject.

Controlling Functions of the Data Protection Authority

The New Law brings clarity regarding controlling functions of the Data Protection Authority by officially granting it the right to conduct both on-site and off-site inspections. Inspections, in turn, will be initiated by the Data Protection Authority based on the Order of the Ministry of Justice of Ukraine adopted in mid-2012[4]. Given the above official right of the Data Protection Authority, it is recommended that companies check their existing internal data protection rules and make sure they fully comply with the data protection law. In particular, it is advisable to check whether consents to the processing of personal data have been duly collected from all data subjects, whether the company developed and approved its own data protection policy (be it reflected in a separate document or in the company's charter), whether databases which are subject to mandatory registration have been really registered/notified, etc. It is worth recalling that, from July 1, 2012, liability for infringements in the data protection sphere have been substantially strengthened, and now it is not limited to monetary penalties, but may result in up to five years' imprisonment (see report by the author and Olexander Martinenko, of CMS Cameron McKenna LLP, Kyiv, at WDPR, February 2012, page 43).

Other Amendments

The New Law provides a legal ground for relations between data controllers and data processors. Now it is finally established that their relations are regulated by contractual agreement. Under the New Law, data processors, in processing personal data, may not go outside the purpose of processing and the volume of personal data as agreed in the relevant contract. Although no mandatory requirements for agreements between data controllers and data processors have been established, this provision means that
the agreement between a data controller and a data processor should at least contain the purpose and the volume of the processing.

At the same time, the parties are free to agree on other terms and conditions of their cooperation.

Another amendment relates to a range of data subjects' rights. In fact, the New Law establishes in law certain rights which had always been implied but had been absent as law. As a result, data subjects now can legally recall previously provided consents to data processing, make reservations while providing consents, make complaints about data processing to the Data Protection Authority, etc. The New Law also introduces some new general elements of data processing, such as protection of vital interests of data subjects, conclusion or fulfillment of the agreement to which a data subject is a party, and the necessity to protect the legitimate interests of data controllers and/or third parties, with certain exceptions. Thus, unlike earlier, when data controllers almost always had to seek data subjects' consent before processing certain personal data, now they will have an opportunity to avoid it in relevant cases.

Over the past year it became popular to discuss and adopt codes of conduct regarding data protection in different business sectors. Such discussions took place, forinstance, in the IT and direct marketing sectors. The New Law leaves this right intact, but now requires professional bodies to obtain approval of the Data Protection Authority for such codes.

Data Protection in the Banking Sector

It is worth noting that, in mid-2012, the National Bank of Ukraine (the ''NBU'') made important amendments to the existing Rules of Storage, Protection, Use and Disclosure of Banking Secrets[5] (the "New Rules''). The New Rules, inter alia, touched upon data protection issues.

The amendments set strict rules for the processing of personal data relating to bank secrecy (such data are defined as data or a range of data about an identified or identifiable individual made available to a bank 1) while providing banking services to such an individual and 2) during relations with him/her or with a third party). According to the New Rules, banks (and other institutions which deal with personal data relating to bank secrecy, together ''banks'') are required:

- to register all relevant databases that contain personal data relating to bank secrecy; and
- adopt internal regulations regarding personal data processing, such regulations necessarily to contain, inter alia, the purpose of the processing and the structure of personal data; the order for inclusion, modification, renewal, use, dissemination, or depersonalization of personal data in the relevant database; the order for personal data protection, etc.

The New Rules also established specific requirements for the form of consent provided by the data subject. Specifically, consent may be made in a free form, but must be personally signed by the data subject with his/her signature to be certified by a notary or by the head of the bank and (in the latter case) stamped by the bank seal.

Alternatively, consent may be 1) included in the body of the agreement for banking services between the bank and the client, or 2) confirmed by electronic digital signature, or 3) provided via web resources.

Recommendations from the Data Protection Authority

During 2012 the Data Protection Authority was quite active in providing its views on different issues related to data protection.

On its website[6] it uploaded a range of recommendations, which may be quite useful in business activities. However, it must be stressed that those recommendations are not recognized as rule of law, but rather are considered to be guidance in certain cases.

Among other things, the Data Protection Authority clarified what to do with data in case of the liquidation of a legal entity, and provided its recommendations as regards drafting a data protection policy.

One of the Data Protection Authority's most important analyses related to video surveillance. Both the Old Law and the New Law are silent on this issue, but, in practice, many entities have faced problems with properly organizing their business activities when using video systems. Supermarkets, shops, and business centers were among the first types of businesses to use video surveillance.

The regulator developed a number of recommendations regarding video surveillance[7], which may be summarized as follows.

Those who intend to introduce video surveillance must notify data subjects by placing a notice of this fact. Such notice must be located in a public place and must be clearly visible, so that a data subject can easily see it before processing of his/her personal data begins.

Moreover, it is recommended that such notice include the following information:

- a warning about the use of video surveillance;
- the name and address of the data controller that conducts the video surveillance;
- the purpose of the video surveillance;
- contact details to enable the data subject to claim modification or destruction of his/her personal data from the system; and
- contact details of the Data Protection Authority which can be used by the data subject for purposes of complaining in case his/her rights have been infringed.

The data controller must also equip video surveillance systems with necessary technical tools in order to prevent illegal access to them. In addition, video surveillance systems must maintain the correct time and date.

Conclusions

Obviously, the New Law provides answers to some old questions, but at the same time gives rise to new ones. It is still necessary to sort out in a legal manner a range of
issues, such as a general algorithm for cross-border transfers, an exhaustive list of countries that provide an adequate level of data protection, etc.

However, it is also clear that many issues may be resolved only based on Ukraine's own steps toward the practical application of data protection law.

Hopefully, Ukraine will build up its data protection system quickly in a way that will suit both the state and businesses.

NOTES

1. Law of Ukraine On Protection of Personal Data No. 2297-IV, dated June 1, 2010.
2. By the Law of Ukraine On Amending the Law of Ukraine on Protection of Personal Data No. 5491-IV, dated December 20, 2012 (the "New Law"). The Data Protection Law is hereinafter referred to as the "Old Law".
3. According to information contained on the Data Protection Authority's official website, http://zpd.gov.ua/dszpd/uk/index.
4. Order of the Ministry of Justice of Ukraine On Adoption of the Order of Conduction by the State Service of Ukraine for Protection of Personal Data of State Control for Compliance with the Data Protection Legislation No. 947/5, dated June 22, 2012.
5. Approved by National Bank of Ukraine Order No. 292, dated July 11, 2012.
6. Available, in Ukrainian, at http://zpd.gov.ua/dszpd/uk/publish/category/36425.
7. Available, in Ukrainian, at http://zpd.gov.ua/dszpd/uk/publish/article/39649.

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Data Privacy

Mexico Issues Minimum Content Requirements for Privacy Notices

Recent Developments

The new regulation, issued by the Ministry of Economy expands the level of detail that must berevealed in privacy notices; it also clarifies the structure that notices must have and the timing where such notices must be delivered to individuals. The framework applicable to companies that collect data through third parties is further elucidated; the Regulations also include a new obligation for companies that collect data in online environments through the use of "cookies" and other technologies that permits monitoring of user habits, which must now provide notice regarding the use of such technologies, including the mechanisms available for the users to deactivate such tools.

Implications Of The New Regulation

While the purpose of the new regulation is to provide guidance to companies on how to appropriately draft and deliver privacy notices, the new rules will demand companies to conduct a more in-depth analysis regarding their existing data processing practices.

Since the regulations mandate to disclose specific information and prohibit the use of phrases such as "for example" or "among other" when a company describes which personal data is obtained or the purposes for which data is processed, the use of generic or pro-forma privacy notices is strongly discouraged. Additionally, the new provisions require privacy notices to distinguish between necessary purposes for processing personal data from those that are not, and between personal data obtained directly from data subject and those obtained through third parties. Modified privacy notices and new processes and procedures related there to must be in place before April 17, 2013.

Relevant Aspects Of New Regulation

On January 17th, 2013, the new "Guidelinesfor the Privacy Notice" were published on the Federal Official Gazette. (the"Regulations"). Regulationsspecify and expand the level of detail that shall be revealed in the privacynotices and the structure such must have, which should be aligned with theprocess in which such are delivered to data owners. A non-binding chapter named"Good Practices in Personal Data Protection" is also included.

Increase in the level of detail to be disclosed regarding the mandatory information elements

- Privacy Notices must be drafted in Spanish.
- Use of ambiguous or inaccurate phrases are prohibited (e.g. "…among other personal data" or "…purposes such as, for example… ").
- Transfers of personal data which require data subject's consent must be distinguished from transfers that do not require such consent.

Processes and procedures

- The Regulations allow companies to use differentforms of privacy notices (either "integral", "simplified" or " short" versions of the notice); each version should be employed in conformity with the process and channel used for the collection of personal data (e.g. personal interviews, telephone calls, application forms, etc.). Therefore, a privacy notice made available by telephone may be simpler and shorter than another delivered personally.
- Regarding the Access, Rectification, Correction and Opposition (ARCO) rights requests, privacy notices must inform, at least: terms to provide an answer to data subject; means for providing answers; form of the deliverable (copies, certified copies, digital versions, etc.) and, the information that the data subject must provide for identification purposes.
- In cases where personal data is obtained through the logon or the user's activity in a webpage, including the type of browser and preferences (through cookies or web beacons), companies have the duty to show a warning message in a visible place, so the user knows that their personal data is being obtained. Also, the steps needed to disable these technologies must be informed.

Next Steps

Regulations are mandatory to any company that obtains or uses personal data from their clients, employees or suppliers. Weadvise all entities to carefully review already implemented privacy notices andimprove the quality of the information quality they reveal, ensuring they allnotices are consistent with their data processing practices and operations.

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Data Privacy

FTC Announces Settlement with Social Networking App and Issues Staff Report Regarding Mobile Device Privacy Disclosures

On February 1, 2013, the Federal Trade Commission ("FTC") announced an agreement with social network mobile application ("app") operator Path, Inc. ("Path") to settle the FTC's claims that Path collected personal information from Path users' mobile device address books without their knowledge and consent, in violation of the FTC Act,[1] and violated the Children's Online Privacy Protection Act and Rule ("COPPA")[2] by collecting children's information without providing the requisite notice and obtaining parental consent (the "Settlement").[3] On the same day, the FTC issued a Staff Report on best practices for mobile privacy disclosures by key mobile industry actors (the "Staff Report").[4] The Settlement and the Staff Report are important because they reflect that the FTC continues to focus on mobile privacy concerns and that separate and prominent just-in-time disclosures and express consent prior to the collection of personal information from mobile devices may be required for information that consumers consider to be sensitive information or unexpected in the context of collection by a particular app.

The Path Settlement

Path operates a social networking service that allows users to keep journals (including photos, written thoughts, location information and names of songs to which the user is listening) about their lives and share their journals with their Path friend network (the "Path App"). The FTC alleged in its complaint that Path App users could search for friends to add to their networks by selecting one of several friend-finder features of the Path App, including by accessing contacts in the user's mobile device address book. The Path App, however, automatically collected and stored personal information (including first and last name, address, phone number, email address, Facebook and Twitter usernames, and birth date) from its users' mobile device address books, even if the user did not select the "find friends from your contacts" option. According to the FTC, Path's privacy policy claimed that Path automatically collected only certain enumerated types of information about its users (such as IP address, operating system, browser type, the address of a referring site and site activity). The FTC claimed that Path's automatic collection of mobile device contact information and its failure to accurately disclose the same to its users denied Path App users any meaningful choice concerning the collection of their personal information and constituted deceptive representations and practices in violation of Section 5 of the FTC Act.[5]

Path also agreed to settle charges that it failed to accurately and fully disclose its information collection practices for children and collected children's personal information (including email address, first and last name and, if provided, gender and phone number) without first obtaining verifiable parental consent, in violation of COPPA.[6] According to the FTC's complaint, Path automatically collected (without first providing notice and obtaining parental consent) the mobile device contact information described above and allowed children under thirteen to register and use the Path App without restriction, enabling the sharing of their photos, location and other personal information.[7] Under the terms of the Settlement, Path agreed to pay a civil penalty of $800,000 and is permanently enjoined from violating COPPA or using in any manner the personal information it has collected from children, all of which must be destroyed.[8] Path is permanently enjoined from misrepresenting its personal information practices and, in connection with mobile device contact information, must clearly and prominently disclose (separate from any privacy policy or terms of use) the categories of information to be collected or accessed from a user's mobile device, and obtain the user's affirmative express consent to the access or collection of the information before the collection takes place.[9] Path must also establish and maintain a comprehensive privacy program, undergo biannual independent privacy assessments, create and retain certain privacy records for twenty (20) years, and submit compliance reports to the FTC within one hundred eighty (180) days after the entry of the Settlement order, and within fourteen (14) days of any change that occurs during the next twenty (20) years in Path's or its affiliates' corporate structure that could affect compliance obligations under the Settlement.[10]

FTC Mobile Privacy Disclosure Guidance

The Staff Report contains best practices recommendations specifically directed to "key commercial players" in the mobile marketplace, namely, mobile platforms and providers (mobile operating systems and providers, as well as the app stores they offer), app developers, advertising networks and analytics companies, and app developer trade associations.[11] The Staff Report recommendations vary for each type of entity[12] but generally reflect the FTC's position that key mobile industry players need to: (a) provide clear, just-in-time disclosures and obtain express affirmative consent before apps collect or use personal information of mobile device users, including information that is by its nature sensitive and information that may be sensitive to consumers in certain contexts, such as photos, calendar entries and contacts; (b) work together to accurately notify consumers concerning information collection and sharing practices; (c) consider offering a do-not-track mechanism to allow consumers to opt out of third party tracking across apps; and (d) develop standardized privacy policies and simple "dashboard" approaches to allow mobile device users to review and change their information collection preferences for all apps and categories of information. These recommendations echo the disclosure and consent requirements imposed on Path and emphasize the importance of transparency and meaningful choice in the FTC's current initiatives.

Although the Path Settlement does not bind app developers or entities other than those specifically covered by the settlement, and the Staff Report is not binding law, these FTC actions are important because they may be setting the tone for future FTC enforcement. It is likely that in resolving enforcement actions, the FTC will now seek to impose the requirements discussed above in the mobile space. App developers, platform providers and other mobile device players should closely monitor the FTC's enforcement actions and published guidance concerning mobile disclosures and take the FTC's recommendations and agreements into consideration in developing and rolling out apps and working with other mobile device industry participants.

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1. *See* 15 U.S.C. §§ 45(a)(1) (prohibiting unfair or deceptive acts or practices in or affecting commerce).
2. *See* 15 U.S.C. §§ 6501-6506; 16 C.F.R. pt. 312 *et seq.* (1999).
3. United States v. Path, Inc., No. C13-0448 (N.D. Cal. Jan. 31, 2013) (consent decree and order for civil penalties, permanent injunction and other relief), *available at* http://www.ftc.gov/os/caselist/1223158/130201pathincdo.pdf; Press Release, FTC, Path Social Networking App Settles FTC Charges it Deceived Consumers and Improperly Collected Personal Information from Users' Mobile Address Books (Feb. 1, 2013), *available at* http://ftc.gov/opa/2013/02/path.shtm
4. FTC, FTC Staff Report, Mobile Privacy Disclosures, Building Trust Through Transparency (Feb. 2013), *available at* http://www.ftc.gov/os/2013/02/130201mobileprivacyreport.pdf; Press Release, FTC, FTC Staff Report Recommends Ways to Improve Mobile Privacy Disclosures (Feb. 1, 2013), *available at* http://www.ftc.gov/opa/2013/02/mobileprivacy.shtm.
5. United States v. Path, Inc., No. C13-0448, 3-4 (N.D. Cal. Jan. 31, 2013) (complaint), *available at* http://www.ftc.gov/os/caselist/1223158/130201pathinccmpt.pdf (hereinafter "Complaint").
6. Complaint, at 7.
7. *Id.* at 8.
8. Settlement, at 9-11.
9. Settlement, at 12.
10. Settlement, at 12-18.
11. Staff Report, at 1.
12. The Staff Report emphasizes the important role that platforms play in controlling operation of apps in mobile devices and recommends that mobile platforms: (a) provide just-in-time disclosures to consumers and obtain their affirmative express consent prior to collecting or using sensitive information, and consider doing so for other information that consumers may find to be sensitive in context, such as contacts and photos; (b) consider developing a "dashboard" approach to allow users to review and make changes to which apps have accessed their information; (c) consider developing icons to reflect data transmission; (d) promote app developer best practices by, for example, contractually requiring that app developers make just-in-time privacy disclosures; (e) consider providing consumers with clear disclosures concerning the extent to which platform providers review apps prior to their becoming available in an app store; (f) consider offering a mobile device do-not-track mechanism to allow consumers to choose to opt out of tracking across apps. Staff Report, at 14-21. The Staff Report recommends that app developers: (a) have a privacy policy in place; (b) to the extent not taken care of by platforms, provide just-in-time disclosures and obtain affirmative express consent before collecting and sharing sensitive information outside the platform's API; (c) improve coordination with ad networks and other third parties that provide services for apps to better understand how the third party software works with respect to data collection and use and provide more accurate disclosures to consumers; and (d) consider participating in self-regulatory programs, trade associations and industry organizations. Staff Report, at 22-24. Trade associations representing app developers, academics and other experts and researchers are asked to: (a) develop icons for app developers to reflect data practices and activity; (b) promote standardized app developer privacy policies or develop "badges" to enable quick comparison of practices across apps; and (c) educate app developers on privacy issues and seek to develop standardization within app privacy policies. Staff Report, at 24-27.

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Defenses

Denial Of Qualified Immunity - Tragic Facts Make Bad Law

It is well established that qualified immunity shields law enforcement officers from liability for civil damages unless the officer violated a statutory or constitutional right that was "clearly established" at the time of the challenged "misconduct." *Reichle v. Howards*, 132 S. Ct. 2088, 2093 (2012). "Clearly established" means the parameters of the right were "sufficiently clear that every reasonable [officer] would have understood that what he is doing violates that right."' Staying up to date on current trends and decisions in constitutional "police" law is so important - because the "devil's in the details."

In *Maxwell v. County of San Diego*, 2013 U.S. App. LEXIS 3106 (9th Cir. Cal. Feb. 14, 2013), the Ninth Circuit, in a split decision, affirmed the denial of summary judgment to San Diego County deputies based on qualified immunity grounds. *Maxwell* is a case involving the alleged interference with medical care of a crime victim and the detention of witnesses.

This case involves a tragic and ill-fated sequence of events, which, distilled to the bare facts, are as follows: Kristin Maxwell-Bruce was shot inside her house on December 14, 2006. At that time, Kristin was able to call 911, to move about the house, to sit upright, and to communicate effectively. When the first and second ambulances arrived, the paramedics determined that Kristin's vital signs were within normal limits. It was not until the paramedics first placed Kristin on a gurney that she began exhibiting signs of distress, expelling blood from her mouth. The ambulance arrived at the air ambulance landing site approximately eleven minutes after the helicopter had landed. Kristin was later pronounced dead.

While paramedics were still at the house, Sergeant Michael Knobbe arrived and began the process of securing the crime scene. As part of that process, two Sheriff's deputies took several family members from the house and left them inside the family motor home which was parked in the driveway. Another family member was told to wait in the driveway, but outside the motor home, where he heard a deputy say "Nobody is leaving. This is a crime scene." This statement, and a statement subsequently made by during a deposition that Sergeant Knobbe was "so concerned with the crime scene [he] didn't want to let the ambulance leave," was offered by the family to support their claim that the deputies caused a delay in medical treatment.

The Court denied qualified immunity to the deputies on the following grounds:

First, the Court found the deputies affirmatively increased the danger to Kristin by preventing her ambulance from leaving. The Court found that "[it] was obvious that delaying a bleeding gun shot victim's ambulance increased the risk of death." In her dissent, Judge Ikuta found "no evidence that the Sheriff's deputies were aware of the urgency of Kristin's situation when they allegedly delayed the ambulance. Kristin was shot, she was conscious, communicating effectively, and her vital signs were normal. The County Medical Examiner testified that Kristin's injury was survivable. The deputies knew that the paramedics who were tending to her decided to wait the 25 minutes it would take for an air ambulance to arrive. Based on multiple contemporaneous assessments of Kristin's condition in the aftermath of the shooting, the Sheriff's deputies, according to the dissent, could reasonably conclude that her condition was stable and that a delay of a few minutes would not put her in peril." Judge Ikuta also found that any delay caused by the deputies could not have lasted longer than seven minutes. "[E]ven if the (at most) seven-minute delay before the ambulance left the property could have placed Kristin in danger, there is no evidence that the deputies actually recognized that risk."

Second, the Court found the over-five hour detention of the witnesses for investigative purposes was unreasonable. In her dissent, Judge Ikuta found that "both Supreme Court and Ninth Circuit cases support the deputies' decision to detain the Maxwells while seeking a search warrant based on probable cause to believe that a violent crime had just occurred inside the Maxwells' house. The Supreme Court has made clear that a search warrant is not always necessary to justify detention of the occupants of a targeted home."

Third, the Court found the supervising captain and lieutenant, who did not directly participate in any of the allegedly unlawful acts, "tacitly endorsed the other Sheriff's officers' actions by failing to intervene." In her dissent, Judge Ikuta found that "it is impossible to conclude that Captain Gregory Reynolds and Lieutenant Anthony Salazar could be held liable merely because they were standing behind yellow crime tape at the scene." "Nor can we infer, solely based on geographic proximity, that Reynolds and Salazar knew or reasonably should have known that the other Sheriff's deputies had forcibly detained the Maxwells and prevented them from seeing their daughter and each other, and that there were no exigent circumstances to justify the detention."

As noted by Judge Ikuta in the dissent, "[I]t is a truism that "tragic facts make bad law." "Nevertheless, we may not furnish a cause of action where the law does not supply one." "The deputies arriving at the Maxwells' residence faced a chaotic scene: a woman had been shot in the jaw; the perpetrator was still in the house; multiple ambulances and paramedics were responding to the scene; and frantic relatives were milling about. From the perspective of the deputies, it was more than merely reasonable to take steps to secure the crime scene and separate the witnesses--it was their duty. The majority has not pointed to a single case that clearly establishes that the deputies' actions here violated the Maxwells' constitutional rights. Under existing case law, the deputies are entitled to qualified immunity for their actions."

PRACTICE POINTER

While this is a unique, fact-specific case, in the aftermath of a critical incident, officers should be aware that perceived interference with medical assistance being provided to a suspect or victim could result in liability. Likewise, using constitutional methods for the handling of witnesses after a critical incident is essential, and voluntary cooperation should be sought.

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Defenses

Colorado Supreme Court Abolishes Sudden Emergency Doctrine Defense

On January 22, 2013, the Colorado Supreme Court reversed an appellate decision affirming the trial court's instruction to the jury on the sudden emergency doctrine, finding that competent evidence did not support giving the instruction. The Court then abolished the 60-year-old doctrine altogether, reasoning that its potential to mislead the jury greatly outweighs its minimal utility.

In *Bedor v. Johnson*, 10SC65 (Colo. 2013), it was undisputed that the defendant lost control of his car when he hit an icy patch on the road. As such, the trial court instructed the jury as follows: "A person who, through no fault of his or her own, is placed in a sudden emergency is not chargeable with negligence if the person exercises that degree of care that a reasonably careful person would have exercised under the same or similar circumstances."

The evidence presented at trial established that the defendant (1) was not specifically aware of the icy patch and that the road leading up to the ice was dry and (2) attempted to correct his course after losing control of his vehicle. However, a majority of the Supreme Court was persuaded by defendant's testimony that he generally anticipated that the roads were likely to be icy the morning of the accident and, therefore, he was not confronted with a "sudden or unexpected occurrence." Further, the majority ignored testimony regarding defendant's attempt to correct his course and opined that simply losing control did not constitute a deliberate response to a sudden emergency necessary to warrant the instruction. Moreover, the Court noted that conflicting evidence indicated that the defendant may have been speeding and/or intoxicated when he lost control of his vehicle. Because the defendant may have contributed to or caused the claimed "sudden emergency" that led to the accident, the Court concluded that the totality of the evidence did not reasonably support the trial court's decision to tender the sudden emergency instruction.

Abolishment of the Doctrine

In abolishing the sudden emergency doctrine in all negligence cases, the Court reasoned that the doctrine was of minimal utility because it was established to overcome the harsh effect of the former contributory negligence defense. While the doctrine does not conflict with Colorado's modern comparative negligence scheme, the Court opined that the instruction unnecessarily repeats the "reasonable care under the circumstances" standard articulated in other pattern negligence instructions. The Court then assessed the instruction's potential to mislead a jury and concluded that serious risks exist because, among other things, the instruction implies that sudden emergency situations require a reduced standard of care and improperly focuses the jury's attention on events that transpired during and after the emergency rather than on the totality of the circumstances.

The Court's abolishment of the sudden emergency instruction is curious because only recently it had determined that the doctrine was helpful to the jury and, as noted in the dissenting opinions, nothing has changed since its earlier pronouncements in this regard. Notably, however, under the Court's reasoning the decision should not drastically affect the defense of cases involving sudden emergencies because the standard of care in those instances remains the same. While the instruction was important to highlight the exigent circumstances and explain *how* the jury should apply the standard of care in emergency situations, it remains the defendant's duty to exercise reasonable care under those circumstances.

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Employment Discrimination

Cross-Border Anti-Harassment Initiatives

US multinationals proactively ban illegal harassment across their operations worldwide. But the radically different harassment landscape outside the US seriously complicates global anti-harassment rules and training.

Harassment law in the US: Over the past few decades, American workplace harassment law has evolved into the most intricate body of harassment jurisprudence in the world. US federal and state court decisions in harassment cases now construe concepts as esoteric as a "tangible employment action requirement for vicarious liability" in *quid pro quo* harassment, an "affirmative defense of unreasonable failure to take advantage of preventive or corrective opportunities," a "severe and pervasive requirement for hostile environment harassment" and claims of "implicit *quid pro quo* third-party harassment."

These esoteric harassment law doctrines evolved in US court decisions even though the texts of American statutes tend not even to prohibit workplace harassment. US federal harassment prohibitions are judge-made extensions of statutes that nominally prohibit only *discrimination*. Even the US EEOC defines "harassment" as "a form of employment discrimination." *See* "Harassment" page at www.eeoc.gov./laws. Therefore, harassing behavior in the American workplace tends to be actionable only to the extent it is a form of discrimination. *Non-discriminatory* harassment—sometimes referred to as bullying, pestering, abusive work environment or equal opportunity harassment—tends to be perfectly legal stateside. A Washington State Department of Labor & Industries publication issued to combat abusive workplace behavior actually concedes that "[b]ullying in general is NOT illegal in the US unless it involves harassment based on" protected status. "Workplace Bullying and Disruptive Behavior: What Everyone Needs to Know," WSDLI rept. #87-2-2011, Apr. 2011 (emphasis in original).

Harassment law abroad: In contrast to the tough, well-evolved but narrow American stance against workplace harassment, the harassment-law landscape overseas differs greatly. Singapore imposes no specific laws banning workplace harassment. Countries such as China and Russia may ban harassment on paper, but they tend not to offer workplace harassment victims many tough precedents or readily enforceable remedies. (Although there are some: In February 2013, Chinese "[m]ilitary prosecutors indicted a one-star general on charges of sexually harassing a military officer." Jo Yeh, "One-Star General Indicted for Sexual Harassment," chinapost.com, Feb. 26, 2013). In 1997 India's Supreme Court banned workplace sex harassment *(Vishakha v. State of Rajasthan)*, but women's rights advocates say India has a long way to go in enforcement. More enlightened countries such as the Netherlands and Luxembourg impose tough bans against workplace harassment, but confounding case law in these jurisdictions actually supports proven sex harassers—labor judges in these countries can be quick to hold dismissal too severe a punishment for a proven sex harasser, particularly a long-serving executive with a relatively clean prior discipline record. *E.g.* Luxembourg C.S.J. no. 34066 (Nov. 12, 2009).

Meanwhile, common-law countries impose tough anti-harassment rules broadly consistent with the US model. All European Union states now impose laws that prohibit certain harassment, and awareness is spreading. A January 2013 article in the German press is called "Wake Up Germany, You've Got a Serious Sex Harassment Problem." A. Borchardt & T. Rest in *Suddeutshe Zeitung* (English translation by WorldCrunch). Countries such as France and Egypt have criminalized certain types of harassment—France reenacted its sex harassment criminal law in 2012 (law no. 2012-954 of August 7, 2012). Under a 2006 Algerian law (art. 341bis), anyone who "exert[s] pressure to obtain sexual favors" in Algeria faces two to twelve months in prison plus a fine of up to 200,000 dinars (US$2,540). These days even Shari-ah law gets interpreted to criminalize workplace sex harassment—in October 2010, a judge in Arar, Saudi Arabia sentenced a sex harasser to *death*. The Saudi harasser had tried to blackmail a government employee at her workplace with revealing photographs, but she denounced him to the Saudi Virtue Police. *See* Deccan Herald, India, deccanherald.com, Oct. 23, 2010.

As countries overseas get serious about stopping workplace harassment, their harassment laws mutate into new forms, some even broader (if less nuanced) than counterpart US doctrines. Unfortunately, these growing differences leave our state-of-the-art American tools and training for weeding out the US variety of workplace harassment increasingly less helpful overseas. So any multinational trying to foster a harassment-free workplace *internationally* these days needs subtlety, nuance, strategy and finesse. Reflexively extending the rigid American "zero tolerance" approach around the world does not work.

Toward a global approach to eradicating workplace harassment: Multinationals pursuing a global approach to eliminating harassment from their worldwide workforces need to account for the international context by factoring in seven issues: alignment; protected status; affirmative mandates; policy drafting; launch logistics; communications/training; and investigations. We address each.

- **Alignment.** A multinational must align any global approach to eradicating workplace harassment with its own approach to preventing *workplace discrimination* and promoting equal *employment opportunity*. Be sure a global harassment policy and international harassment training, as well as a cross-border anti-harassment enforcement initiative, dovetail with the multinational's global initiatives as to discrimination and diversity. Tackle these three related issues together, not in isolation.
- **Protected status.** Because American-style prohibitions against workplace harassment grow out of US statutes that prohibit workplace discrimination, American employers' harassment policies and training tend to ban only *status-based* harassment linked to a victim's membership in a protected group—sex harassment, race harassment, disability harassment, age harassment, religious harassment, even theoretically veteran status harassment and genetic harassment. To date, not too many US domestic employers have taken the bold step of imposing tough, enforceable workplace rules that ban *status-blind* harassment—bullying, pestering, equal opportunity harassment. A trend may be emerging at the US state government level to outlaw so-called "abusive work environments," but state proposals here so far have little traction. (Remember even Washington State's campaign against abusive work environments concedes "[b]ullying in general is NOT illegal in the US.")

By contrast, many other countries already prohibit infinitely broader *status-blind* harassment (abroad called workplace "bullying," "mobbing" "psycho-social harassment," or "moral harassment"), without regard to protected group status. A Belgian law of June 2002 prohibits workplace "pestering." A French law of June 2010 criminalized "psychological violence." A Luxembourg law of June 2009 prohibits "bullying and violence at work." Venezuela's 2005 "Organic Law on... Work Environment" prohibits "offensive, malicious and intimidating" conduct in the workplace, including "psychological violence" and "isolation." And mushrooming case law in Brazil imposes damages for workplace "moral harassment"—Brazilian moral harassment law in recent years has become a common claim in all sorts of workplace disputes. In Brazil these days, even employers that legally assign and legally pay overtime have faced "moral harassment" litigation from overworked employees arguing the extra hours amount to a form of bullying.

In theory, foreign status-*blind* harassment laws are infinitely broader than American-style status-*based* harassment prohibitions: A doctrine that bans abusive behavior for whatever reason is infinitely broader than a targeted American-style rule that prohibits only harassment motivated by a dozen or so protected traits. For a multinational, the challenge here is how to factor these broad foreign status-blind harassment laws into a workable global workplace anti-harassment policy and training module. Expanding a US-style harassment policy, and training, to account for foreign status-blind harassment prohibitions requires exponentially increasing its scope, and this expansion makes US employers uncomfortable, especially if the broadened policy and training will reach into US workplaces. Too many US multinationals downplay this conflict and simply issue overly narrow international policies that merely ban status-based harassment. But this approach blows a huge hole in the multinational's international harassment compliance initiative, because the employer's internal harassment prohibition bans much less than all illegal harassing behavior.

- **Affirmative mandates.** Every law against workplace harassment imposes a negative *prohibition* against employers (and often co-workers) who commit illegal harassment. In addition, some jurisdictions' laws go farther and impose affirmative employer *duties* or *mandates* as to harassment compliance. Multijurisdictional harassment initiatives (policies, training, enforcement) need to account for these. A global policy that merely bans illegal harassment does not go far enough in a jurisdiction where employers have to take affirmative harassment compliance steps.

For example, like California, South Korea requires employers to offer periodic training on sex harassment. Chile, Costa Rica, India, Japan and other countries affirmatively require employers to issue written sex harassment policies. The Austrian Supreme Court requires employers affirmatively to investigate complaints of sex harassment (Austria Supreme Court decision *9 ObA 131/11x*, Nov. 26, 2012), as do statutes in countries including Chile, Costa Rica, India, Japan, South Africa and Venezuela. Costa Rica requires employers to institute sex harassment claim procedures and to report each sex harassment claim to the Ministry of Labor Inspection Department. A 2006 Japanese regulation (MHCW notification No. 415) imposes similar affirmative mandates. (In addition, some jurisdictions' harassment laws, such as China's Special Provisions on Occupational Protections for Female Employees of April 2012, affirmatively require that employers provide a "harassment-free workplace." But in practice, mandates of harassment-free workplaces differ little from simple negative prohibitions against harassment.)

- **Policy drafting.** In drafting a multinational's cross-border anti-harassment policy (or code of conduct provision), be sure the policy mandates actually work overseas. Reject American- style prohibitions that are unworkable abroad. To do this, define key terms cross-culturally and ensure the policy's explicit prohibitions are enforceable in each affected jurisdiction:
    - ***Define key terms cross-culturally.*** Workplace harassment policies implicate concepts that are stubbornly susceptible to being misconstrued abroad. Be sure to be clear. For example, the common harassment policy terms "inappropriate" behavior and "improper" touching get interpreted very differently depending on cultural context—some behavior obviously "inappropriate" or "improper" in Atlanta, Roanoke and Milwaukee may not seem so out of line in Athens, Riyadh or Mexico City. "Kissing," prohibited by many US harassment policies and training modules, usually implies romantic mouth-kissing without distinguishing the cheek-kissing common among co-workers in many countries. Even the term "harassment" itself takes on very different meanings abroad. In Brazil, "harassment" (*assédio*, in Portuguese) is understood to mean overt and abusive acts like bullying and *quid pro quo* harassment and therefore does not reach "hostile environment" harassment. For that matter, employees abroad are not likely to understand even basic US harassment terms of art like "hostile environment" and *"quid pro quo"* harassment.

  - ***Ensure the policy's explicit prohibitions are enforceable in each affected jurisdiction.*** A harassment policy's specific restrictions may raise legal issues abroad. Be sure policy prohibitions are enforceable overseas. For example, again we have the "kissing" problem: The common US harassment policy provision prohibiting on-job "kissing" is unworkable in places like France where men and women co-workers kiss one another every morning as a greeting. Also, restrictions against co-worker dating raise serious privacy law issues and spark human resources challenges overseas, especially in countries such as Germany and Switzerland where birth rates are low and a third to half of married couples are believed to have met in the workplace. Society in these countries actually sees workplace romance as vital to sustaining the local population base, and so local employees and even courts push back hard against American-style co-worker dating restrictions (or at least passive-aggressively ignore them). In these jurisdictions, even a workplace rule that merely requires dating co-workers to disclose their relationships almost always offends. In one extreme case, a Russian judge confirmed a worker's sex harassment allegation as true but nevertheless denied her claim, reasoning that *"if we had no sexual harassment, we would have no children." See* E. McKenzie, "Sex Harassment Good for Procreation: Russian Judge," *Law360*, Aug. 8, 2008.

- **Launch logistics.** Be sure to launch a cross-border harassment policy so that it complies with overseas procedures for implementing new work rules. Every harassment policy imposes a discipline or termination sanction, but as we have seen, many jurisdictions get surprisingly lenient when an employer invokes an anti-harassment policy to fire a harasser for good cause—so the policy needs to stick. Harassment policies are work rules that can be subject to mandatory "information and consultation" with works councils and health-and-safety committees or mandatory bargaining with unions. Launching a new harassment policy may also require tweaking lists of local work rules, such as the rules required in France, Japan and Korea. And any harassment policy that imposes a mandatory disclosure rule—such as a rule requiring dating co-workers to disclose their relationships—can trigger employment and data privacy law challenges. *See* our *Global HR Hot Topic* for Feb. 2012.
- **Communications/training.** A multinational implementing a global harassment policy should communicate its policy to employees abroad and then train on how it works. But never directly export US online or live harassment training modules around the world. Training about sex harassment, in particular, raises unique cultural challenges in places where harassment remains poorly understood. Foreign workers, male and female alike, used to mock US-generated sex harassment and gender-sensitivity training. In recent years, overseas workers may have become superficially more accepting of these training sessions, but many overseas employees forced to sit through harassment modules may still see this as a puritanical American exercise irrelevant to their local environment. Indeed, in some pockets of the Arab world, Africa, Asia, Latin America and Eastern Europe, a workforce may openly scoff at training seen as too awkward, too "politically correct" and too insensitive to the local environment. For example, at a February 2013 sex harassment training session at Chinese manufacturing giant Foxconn, one "18-year-old female worker" was "often"—*during the sex harassment training session itself*—"subjected to obscene gestures and sexual harassment from three male colleagues." Ma Yujia, "Foxconn Employees Suffer Sexual Harassment," China.org.cn, Feb. 22, 2013. So tailor anti-harassment communications and training for local audiences. Tone down messages likely to ruffle local feathers. Make the case for why harassment is a local problem. Show how harassment rules can work locally to improve local conditions.
- **Investigations.** US employers understand the importance of thoroughly investigating credible harassment complaints, allegations and denunciations received both informally and through reporting channels like hotlines. Indeed, as already mentioned, law in Austria, Chile, Costa Rica, India, Japan, South Africa, Venezuela and elsewhere affirmatively requires employers to investigate allegations of sex harassment. But even in these countries, an aggressive American-style workplace harassment investigation can trigger push-back and unexpected legal issues. So adapt overseas harassment investigations (and discipline for proven harassers) to comply with host-country rules and culture. *See* our *Global HR Hot Topic* for Apr. 2013.

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Employment Discrimination

UK Must Change Law On Political Beliefs

In *Redfearn v the United Kingdom* [2012], the European Court of Human Rights held that the UK has breached Article 11 of the European Convention of Human Rights (ECHR) by failing to protect employees who are dismissed because of their political opinions or affiliations.

Facts

Mr.Redfearn worked as a bus driver for Serco Ltd, transporting children and adults with disabilities. Approximately 75% of Serco's passengers and 35% of its workforce in the relevant area were Asian in origin. Mr. Redfearn had a clean employment record and had even been nominated for the award of 'first-class employee' by his Asian supervisor.

Following a newspaper article identifying Mr.Redfearn as a candidate for the British National Party (BNP) in local elections, Serco received complaints from the UNISON and GMB trade unions about Mr.Redfearn's continued employment. A few weeks later, Mr.Redfearn was elected as a local councillor for the BNP. Due to Serco's concerns that his continued employment would carry health and safety risks and about the reactions of its customers, the company summarily dismissed Mr.Redfearn.

Mr.Redfearn did not have sufficient qualifying service to bring an unfair dismissal claim (at that time, one year's continuous employment). Instead, he brought a claim in the employment tribunal alleging that Serco had unlawfully discriminated against him on the grounds of race under the Race Relations Act 1976 (a cause of action now covered by the Equality Act 2010 and which does not require a qualifying length of service to pursue).

The Court of Appeal found that Mr.Redfearn was not discriminated against on the grounds of his race but because he was a member of the BNP. It found that membership of a political party or the holding a particular political belief was not a 'racial ground' and considerations such as membership of a political party were not 'protected categories'.

Judgment

Mr.Redfearn, having been refused leave to appeal to the House of Lords, chose to pursue his case before the European Court of Human Rights (the court). He asserted that in choosing to become a BNP member, he was exercising his right to freedom of assembly and association as protected by Article 11 of the ECHR. Mr.Redfearn went on to argue that for his Article 11 rights to be effectively protected within the UK, the qualifying period for bringing an unfair dismissal claim should not apply.

The court acknowledged that membership of a political party is a central tenet of democracy and should be protected by member states even if the views expressed by that party offend, shock or disturb. It held that contracting states (which are different from EU member states) have a wide discretion in their implementation of the ECHR in cases where there are sensitive social and political issues. Nevertheless, any measures taken which restrict an individual's human rights must be proportionate and necessary.

In the court's view, the one-year qualifying period then applying in the UK to unfair dismissal claims pursued the legitimate aim of increasing employment. However, it deprived Mr.Redfearn of his only right of recourse under UK legislation against interference with his human rights.

The court therefore stated that the UK must take further steps to protect individuals' rights under Article 11. It suggested that this could be done by adding in a new head of claim under unfair dismissal law which did not require one or two years of qualifying service (as is the case for health and safety or whistleblowing claims at present). Alternatively, it said that the UK could introduce a free-standing claim for unlawful discrimination on the grounds of political opinion.

Possible Routes To Compliance

Unless the government decides to appeal the decision to the Grand Chamber of the European Court of Human Rights, it will need to consider steps to comply with the ruling.

Even without any change to UK law, the judgment will directly affect public sector employers as a result of s6(1) of the Human Rights Act 1998. This provides that public employers must act in a way which is compatible with the ECHR. Public sector employees could therefore rely on this judgment to claim that they were unfairly dismissed because of their membership of a political party, even if they do not have the requisite service to bring an unfair dismissal claim (now two years). Private employers will not be directly affected unless and until the law has been amended.

It has been suggested that the government could consider extending the definition of ‘religion or belief’ (a protected category) in the Equality Act 2010 so that it expressly includes political beliefs. Arguably, however, it may not need to; when Mr.Redfearn was dismissed, the Employment Equality (Religion or Belief) Regulations 2003 were expressed to cover ‘religious belief[s] or similar philosophical belief[s]’. In *Finnon v Asda Stores Ltd* [2005], which was decided under those Regulations, a tribunal held that membership of the BNP did not amount to a philosophical belief because British nationalism did not have a clear belief system nor was it a profound belief affecting the person’s way of life or view of the world. The tribunal reached a similar verdict in Baggs v Fudge [2005] (also decided under the 2003 Regulations) on the basis that BNP members were not required to hold particular religious or philosophical beliefs.

In 2007, however, the definition of ‘belief’ was amended to include ‘any religious or philosophical belief’ and the same definition is now contained in the Equality Act 2010. The new definition therefore omits the word ‘similar’. Baroness Scotland is recorded as stating that ‘similar’ was deleted because it added nothing and because the definition of belief could not include support for a political party. However, the subsequent interpretation of the legislation does seem to take a wide view of the definition of ‘belief’. For example, recent case law has found that both a belief in climate change and a belief that fox-hunting is wrong fall within this definition. On this basis, if Mr.Redfearn brought the case today, he might seek to argue that he has been discriminated against on the basis that his membership of the BNP falls within the definition of ‘philosophical belief’. Moreover, Baggs and Finnon were both decided before Redfearn. Under the Human Rights Act, British courts are obliged to interpret any UK legislation in accordance with the ECHR so far as is possible to do so. To achieve this, the courts and tribunals may now be more willing to interpret philosophical belief as including political opinion.

A Conundrum

Whether or not the definition of philosophical belief is expressly extended or the courts interpret philosophical belief as including political opinion, a considerable problem remains for the UK if political affiliation becomes a ground of discrimination. In virtually all areas of discrimination law, an employer cannot justify direct discrimination (less favourable treatment ‘because of’ a protected characteristic). Thus, if political affiliation was a protected characteristic and Mr.Redfearn’s dismissal was because of his philosophical belief or political affiliation, it would not be possible for Serco to argue that such a dismissal was justified. This is at odds with the court’s judgment, which proposed a more discretionary approach whereby discrimination can be justified so long as the measures taken pursue a legitimate aim and are proportionate. Making political affiliation a protected characteristic therefore arguably places a more onerous obligation on employers than is required by the decision in Redfearn. The UK is therefore left with a conundrum – should political opinion be treated in the same way as virtually all other protected characteristics in a direct discrimination situation (and thus not be justifiable) or should employers be able to justify discrimination on this ground? If it chooses the former option, employees discriminated against on the ground of political opinion would receive more protection than this judgment requires. However, if it chooses the latter option, it will create an inconsistent framework of discrimination legislation and run the risk that the right to hold a political opinion is worthy of less protection in the UK than other protected characteristics, such as race and gender.

The path ahead is therefore unclear. Given the political context and the coalition government’s intention to reduce red tape, it would be surprising if it chose to legislate beyond what the judgment requires. However, the UK is obliged to do something, whether one of the options highlighted above or something completely novel, to ensure that the right to hold a political opinion receives the protection required by the ECHR. However, we will need to wait for the government to announce how it proposes to deal with the case before its true impact will be revealed.

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Editors Note: The author notes since this article was published, the Government's response has been to put forward an amendment to the Enterprise and Regulatory Reform Bill to disapply the qualifying period for unfair dismissal "if the reason (or, if more than one, the principal reason) for the dismissal is, or relates to, the employee's political opinions or affiliation". Thus a dismissal on the basis of political opinion or affiliation would not be deemed automatically unfair, but rather such an unfair dismissal claim could be heard on the normal principles but without the need for the employee to have minimum qualifying service."

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Employment Discrimination

California Supreme Court's "Mixed-Motive" Decision Is A Mixed Bag For Employers

In a closely watched employment case, the California Supreme Court unanimously ruled that employees are not entitled to damages when discrimination factors into a termination if the termination would have occurred regardless of the discrimination.

Background

Plaintiff Wynona Harris was hired as a bus driver trainee in October 2004 by the City of Santa Monica. During her training and probationary period, she was involved in two accidents that the City deemed "preventable," and she incurred two "miss-outs" for failing to report for her scheduled shift.

In May 2005, Ms. Harris informed her supervisor that she was pregnant. Six days later, her employment was terminated. Ms. Harris sued, claiming that she was terminated because she was pregnant. The City asserted that it had a legitimate, non-discriminatory reason for the termination.

A jury found that Ms. Harris' pregnancy was a motivating reason for the City's employment decision, and awarded $177,905 in damages. The trial court awarded attorney's fees of $401,187.

On appeal, the City argued that the trial court's refusal to give its requested instruction regarding its "mixed-motive" defense was prejudicial error. The Court of Appeal agreed. Ms. Harris appealed to the California Supreme Court.

Holding

In a 6-0 decision, the Court held that when a plaintiff has shown that discrimination was a substantial motivating factor for the termination, the employer is then entitled to demonstrate that legitimate, nondiscriminatory reasons would have led to the same decision at that time. If the employer proves that it would have made the same decision for lawful reasons, then the plaintiff is not entitled to recover damages, backpay, or reinstatement. However, the plaintiff may be entitled to declaratory or injunctive relief, and may be eligible for attorney's fees and costs.

Analysis

The Fair Employment & Housing Act ("FEHA") prohibits discrimination in employment. Specifically, Government Code §12940(a) prohibits an employer from taking an adverse employment action "because of" a person's protected status.

CACI 2500 is the standard jury instruction that sets forth the essential factual elements a plaintiff must prove in an employment discrimination case. It states that the plaintiff must prove that discrimination was "a motivating reason" for the employment decision. However, until now, the degree of causation required by the "because of" language was unsettled.

After considering the legislative history and federal decisions, the Court held that a plaintiff must show, by a preponderance of the evidence, that "discrimination was a substantial motivating factor, rather that simply a motivating factor . . . ." (Emphasis in original.) The Court determined that the substantial motivating factor test satisfies the deterrent purpose of the FEHA, while also more effectively ensuring that liability will not be imposed based on evidence of mere thoughts or passing statements that are unrelated to the employment decision.

After the plaintiff satisfies this burden, the burden then shifts to the employer to show that it would have made the same decision regardless of any discrimination. However, the employer does not satisfy its burden simply by establishing a legitimate and sufficient reason for the decision. Instead, it must show that at the time it made the employment decision, it was motivated by legitimate reasons that would have resulted in the same employment decision, regardless of any discrimination.

The Court acknowledged that finding that a plaintiff has satisfied its "substantial motivating factor" burden may result in an "unjustified windfall" for plaintiffs if the employer proves that it would have made the same decision regardless of discrimination. In those cases, plaintiffs could recover backpay or an order of reinstatement, front pay, and future loss of income, in addition to non-economic damages. At the same time, employers' hands would be tied, as they would be forced to retain employees whose employment they would have terminated.

Therefore, the Court held that if a plaintiff establishes that discrimination was a "substantial motivating factor" in the employment decision, and the employer then establishes that it would have made the same decision regardless of any discrimination, the plaintiff is not entitled to backpay, an order of reinstatement, or damages, including non-economic damages. Instead, the employee may be entitled to a judicial declaration of the employer's wrongdoing. The trial court may also grant injunctive relief to stop discriminatory practices. Finally, the plaintiff may be eligible for a discretionary award of reasonable attorney's fees and costs, which would require the employer to absorb the litigation costs of its own wrongdoing but would avoid a windfall to plaintiffs.

Thus, the Court held that a jury in a "mixed-motive" case should be instructed that it must find that the employer's action was substantially motivated by discrimination before the burden shifts to the employer to make a same-decision showing. Juries should further be instructed that a same-decision showing precludes an award of reinstatement, backpay, or damages.

Significance

Until now, juries have been instructed according to CACI 2500, which states that an employment discrimination plaintiff must show that illegal discrimination was "a motivating factor" in the employment decision. The Harris decision raises the burden of proof for plaintiffs in employment discrimination cases. However, the ruling may not deter plaintiffs' attorneys from bringing discrimination lawsuits, as they are still able to recover attorney's fees if the plaintiff can establish that discrimination was a substantial motivating factor for the employment decision.

Furthermore, FEHA plaintiffs often assert tort claims for Wrongful Termination in Violation of Public Policy along with their FEHA-based claims. These tort claims are generally duplicative of FEHA-based claims, but may now take on added significance, as the Court did not address whether or not the substantial motivating factor standard also applies to those claims.

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Employment Discrimination

Blowing The Whistle On Direct Evidence

The Whistleblower Protection Act (WPA) was enacted to protect employees from adverse employment actions resulting from an employee engaging in a protected activity. A prima facie case under the WPA may be established by showing that a causal connection exists between the protected activity and an adverse employment action. The WPA comes under the burden-shifting framework set forth in the landmark case *McDonnell Douglas Corp v Green*, 411 US 792 (1973), which held that, absent direct evidence of retaliation, a plaintiff can rely on indirect evidence of an employer's unlawful motivation to show that a causal link exists between the whistleblowing act and the employer's adverse employment action. This establishes a rebuttable presumption that the employer's adverse action was "more likely than not based on the consideration of impermissible factors," such as an activity protected under the WPA.

Once a rebuttable presumption of retaliation is established, the employer has the opportunity to offer a legitimate reason for its action and may show that a reasonable fact-finder could still conclude that plaintiff 's protected activity was not a "motivating factor" for the adverse action. If an employer relies on the business-judgment rule as a defense to a claim under the WPA, the court must determine whether the decision to take adverse action against the employee was an "unwise" business decision, or whether the employer's stated justification was false or had no basis in fact. If plaintiff 's allegations are based on the latter, the business-judgment rule does not insulate the employer from liability under the WPA.

In *Debano-Griffin v Lake County*, et al, Plaintiff was employed as the director of the Lake County 911 Department. A millage had been passed for the purpose of operating the 911 Department, and Lake County contracted with Life EMS to provide ambulance services to the County. In 2002, Plaintiff discovered that Life EMS was using one of its ambulances to transport residents of other counties in nonemergency situations, and she informed the Lake County Board of Commissioners that Life EMS was in breach of its contract. Further, in 2004, Plaintiff publicly objected to the transfer of $50,000 (authorized by the Board), from the ambulance account to another account designated for a "mapping project". Plaintiff claimed that the transfer violated the millage proposal, and the Board later voted to return the funds to the ambulance account. The Board also voted to merge two county employment positions, resulting in the elimination of Plaintiff 's position and stated the rationale were "budget problems" and "cost cutting measures". Plaintiff filed a claim under the WPA, alleging that she was terminated as a result of her complaints regarding the transfer of funds and the breach of the Life EMS contract.

At the trial court level, Defendants' motion for summary disposition was denied, and the jury returned a verdict in Plaintiff 's favor. After a series of appeals and remands, the Court of Appeals held that Plaintiff failed to establish a genuine issue of material fact on the causation element of her claim and again reversed the trial court's denial of Defendants' motion for summary disposition. The Supreme Court then granted Plaintiff 's leave to appeal. Plaintiff presented evidence of a causal link that showed more than just a "coincidence in time" between the protected activity and the adverse action. During a twelve day period when Plaintiff engaged in the protected activity, making various complaints regarding the funds transfer and improper use of ambulance services, Plaintiff's position went from fully funded to non-existent. The Court held that: A reasonable juror could infer that the Board had already decided to fund Plaintiff 's position until she publicly voiced her complaints. It found further impermissible motivation because the same entity that made the decision to eliminate Plaintiff 's position (the Board) was also the recipient of Plaintiff 's complaints. The more an employer is affected by a plaintiff 's whistleblowing activity, the stronger the causal link becomes between the activity and the adverse action. It found that the Board was forced to do something that it would not have otherwise done (i.e., return the funds), and a reasonable inference may be drawn that the Board was motivated to eliminate Plaintiff 's position because of her complaints. It was also found that there was a reasonable inference that Plaintiff was the victim of unlawful retaliation, which established a prima facie case and gave rise to a rebuttable presumption that Defendants had unlawfully retaliated against Plaintiff by eliminating her position.

The Court then turned to the application of the business-judgment rule to the WPA.

Defendants argued that Plaintiff could not challenge the budgetary justification because this would impermissibly question their “business judgment,” or unconstitutionally require judicial review of a legislative body’s policy decision. As to the business-judgment argument, the Court found that Plaintiff provided evidence to show that Defendants’ budgetary justification was not the actual factor motivating the decision to eliminate her position. This “additional evidence” included testimony from a Lake County employee that Defendants had hired several full-time employees during 2005 and 2006, and that the budget worksheet for Lake County in 2005 indicated that many 911 dispatchers would receive pay increases. This evidence, coupled with the assertion that Plaintiff had not challenged whether the decision to eliminate her position was “sound” business judgment, but rather that the proffered justification had no basis in fact, led the Court to conclude that Plaintiff successfully rebutted Defendants’ budgetary justification for the adverse action. The Court held that reasonable minds could differ regarding the employer’s true motivation for eliminating Plaintiff ’s position, and that a genuine issue of material fact existed. Defendants were not entitled to summary disposition, and the Court reinstated the trial court’s judgment in favor of Plaintiff.

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Jurisdiction

In What Circumstances Can Foreign Nationals Be Held Liable for Violating The Foreign Corrupt Practices Act?

In the last two weeks, in two separate SEC enforcement actions, judges in the United States District Court for the Southern District of New York issued rulings addressing when the United States Securities and Exchange Commission ("SEC") can bring enforcement actions against foreign nationals in cases involving bribes paid in foreign countries. In one case, the Court held that the SEC could proceed; in the other, the Court dismissed the case. These cases are of great interest not only because they explain the limits of the SEC's jurisdiction, but they also set forth unexpected incidents of that jurisdiction, such as a potentially unlimited statute of limitations period for foreign nationals who never enter the United States.

Securities & Exchange Commission v. Straub[1]

On February 8, 2013, U.S. District Judge Richard Sullivan denied a motion to dismiss an SEC enforcement action for lack of jurisdiction. Judge Sullivan held that -- although the defendants, who are Hungarian nationals, were never physically present in the United States in connection with the alleged scheme to bribe government officials in Macedonia -- the SEC could proceed with a case against them for violating the FCPA.[2]

In its complaint -- filed in December 2011 -- the SEC alleged that, in 2005, the defendants, executives of a Hungarian telecommunications company, Magyar Telekom, Plc. ("Magyar"), bribed Macedonian government officials to mitigate the effects of a new law that increased fees, imposed regulatory burdens and allowed for the licensing of a mobile telephone operator which would compete directly with a Magyar subsidiary.[3]

At the time, Magyar's securities were publicly traded in the United States through American Depository Receipts ("ADRs") listed on the New York Stock Exchange ("NYSE"). Defendants made certifications to Magyar's auditors regarding the accuracy of the company's financial statements and its internal controls. One of the defendants signed management representation letters to Magyar's auditors and the other two defendants signed management sub-representation letters or "Sarbanes-Oxley certifications."[4]

The defendants argued that, as they are foreign nationals and the alleged bribery took place in Macedonia to further the interests of a Hungarian company, the Court lacked jurisdiction over them. In addressing this argument, the Court recited the standard rule that, in order to establish personal jurisdiction over the defendants, the SEC must show that each defendant "purposefully availed himself of the privilege of doing business in the forum state and that the defendant could foresee being haled into court there."[5] The Court noted that a defendant's physical absence from the forum is not, in and of itself, sufficient to defeat personal jurisdiction.[6] For foreign defendants, their activity in relation to the United States must be "sufficiently extensive and regular to make [the] possibility [of litigation in the United States] a foreseeable risk of the business."[7]

The Court held that the SEC's allegations satisfied the requisite "minimum contacts" standard. The Court reasoned that the defendants "allegedly engaged in a cover-up [of the bribe payments] through their statements to Magyar's auditors[,] knowing that the company traded ADRs on an American exchange, and that prospective purchasers [of the ADRs] would likely be influenced by any false financial statements and filings."[8] The Court noted "even if [d]efendants' alleged primary intent was not to cause a tangible injury in the United States, it was nonetheless their intent, which is sufficient to confer jurisdiction."[9]

This holding shows clearly that foreign nationals are at risk of a U.S. regulatory action, even under circumstances where foreign nationals might well assume that their actions are not directly connected to the United States.

Other Issues Decided by the Straub Court Impact Foreign Nationals

In addition to addressing the personal jurisdiction question, Judge Sullivan also ruled on two other aspects of the FCPA that have important implications for foreign nationals.

The Statute of Limitations Period Does not Begin to Run Until Foreign Nationals Are "Found Within the United States"

In their motion to dismiss, the defendants in Straub argued that the SEC action was barred by the statute of limitations because the alleged unlawful conduct took place in 2005 and the SEC did not file the action until 2011. The Court rejected this argument as well.[10]

The parties disputed the meaning of the statute of limitations period described in 28 U.S.C. § 2462[11] which states: "an action . . . shall not be entertained unless commenced within five years from the date when the claim first accrued if, within the same period, the offender or the property is found within the United States in order that proper service may be made thereon."

The Court agreed with the SEC's interpretation that "the statute applies only if, within the same period, the offender is found within the United States."[12] Thus, the SEC argued that because the defendants were not "found" in the United States from 2005 through the date the suit was filed, the five-year statute of limitations period had not yet started to run. The defendants argued that the statute of limitations begins to run when a defendant is either "found within the United States" or "subject to service of process elsewhere by some alternative means."[13] The defendants' position was that, since the law provides methods for the SEC to serve defendants with the complaint even if they are not in the United States, the statute of limitations started to run in 2005.

In ruling in favor of the SEC, the Court stressed that the plain meaning of the statute requires the defendant's physical presence in the United States in order for the statute to start running.[14] Under this ruling, foreign nationals can be sued in the United States many years -- or even decades -- after the allegedly unlawful conduct, so long as they remain outside the United States.

Emails Routed Through Servers Located in the United States Can Support a Substantive FCPA Violation

The SEC premised its substantive FCPA claim on, among other things, 15 U.S.C. § 78dd-1(a), which makes it illegal to "use . . . the mails or any means or instrumentality of interstate commerce corruptly in furtherance of an offer, payment, promise to pay, or authorization of the payment of any money" to "any foreign official." The complaint alleged defendants sent documents related to the alleged bribery scheme via email. Although the defendants were outside the United States when they sent the emails (which were addressed to recipients also outside the United States), the emails were routed or stored on network servers located in the United States.[15]

In an issue of first impression, the Court considered whether the SEC had to allege that the defendants intended to use servers based in the United States (i.e. instrumentalities of interstate commerce).[16] The Court held that the SEC did not have to do so. It is sufficient, Judge Sullivan held, for the SEC to allege that the servers in the United States were, in fact, used in transmission of the emails, whether or not the defendants knew or intended that those servers would be used.[17] This ruling, too, broadly expands the SEC's ability to sue foreign nationals for FCPA violations.

***Securities & Exchange Commission v. Sharef*[18]**

On February 19, 2013, less than two weeks after the denial of the defendants' motion to dismiss in SEC v. Straub, another judge on the U.S. District Court for the Southern District of New York, Judge Shira Scheindlin, granted Herbert Steffen's motion to dismiss an action brought by the SEC against him and six other former senior executives at Siemens Aktiengesellschaft ("Siemens") a multinational engineering and electronics company headquartered in Germany. Steffen, a 74-year old German citizen, was the former CEO of Siemens S.A. Argentina, a Siemens subsidiary from 1983 to 1989, and again in 1991. He served in other management roles with Siemens until he retired in 2003.[19]

The SEC's complaint, filed in December 2011, alleged defendants paid millions of dollars in bribes to government officials in Argentina in exchange for a billion dollar contract to create national identity cards. The contract was awarded to Siemens in 1998 and later suspended. Siemens allegedly then paid additional bribes to Argentine officials in order to get the contract reauthorized.[20] The complaint alleged, among other things, that the defendants "urged Siemens management to funnel more money to Argentine officials to ensure that earlier bribes were not disclosed."[21]

The complaint alleged that one of the defendants, the Chief Financial Officer of Siemens Business Services ("SBS"), "an operating group"[22] of Siemens, had "signed quarterly and annual certifications under the Sarbanes-Oxley Act [("SOX")] in which he represented that SBS' financial statements [which obviously did not report any bribe payments] were not false or misleading."[23] Defendant Steffen -- who was not alleged to have signed the SOX statements himself -- filed a motion to dismiss asserting that the Court lacked personal jurisdiction over him and that the complaint was untimely.[24]

As Judge Sullivan did in Straub, Judge Scheindlin analyzed the issue of personal jurisdiction. The Court cited a similar standard for the requisite "minimum contacts" as Judge Sullivan did in Straub.[25] However, Judge Scheindlin found that "Steffan's actions [were] far too attenuated from the resulting harm to establish minimum contacts."[26] The Court scrutinized Steffan's role in the scheme and noted that while he may have "pressured" others to make certain bribes, he ultimately did not authorize the bribes, nor did he sign and falsify any of the SEC filings to conceal the bribes.[27]

Judge Scheindlin expressed concern that “under the SEC’s theory, every participant in illegal action taken by a foreign company subject to U.S. securities laws would be subject to the jurisdiction of U.S. courts no matter how attenuated their connection with the falsified financial statements.”[28] Judge Scheindlin noted that when a defendant is not in the United States “great care” should be taken in exercising jurisdiction.[29] “Steffen’s lack of geographic ties to the United States, his age, his poor proficiency in English” and the fact that Germany already resolved an action against him, all weighed heavily against establishing personal jurisdiction.[30] Judge Scheindlin dismissed the action on jurisdictional grounds and therefore found it unnecessary to address the statute of limitations issue.[31]

Conclusion

These two recent District Court decisions make clear that -- although there are limitations -- foreign nationals face a real risk that conduct that occurs outside the United States could give rise to an SEC enforcement action for violation of the FCPA. While these decisions reached different results, the analysis of whether a foreign national has the requisite “minimum contacts” is a fact-specific inquiry. Certainly, signing financial statements or certifications that ultimately will be filed in the United States, or form the basis of such filings, can be a sufficient basis for jurisdiction, but it is not a requirement for an assertion of personal jurisdiction and even actions less directly connected to the United States may be enough.

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1 No. 11 Civ. 9645, 2013 Dist. LEXIS 22447 (S.D.N.Y. Feb. 8, 2013).
2 Id. at *2.
3 Id. at *3.
4 Id. at *7-8.
5 Id. at *17 (quoting Kernan v. Kurz-Hastings, Inc., 175 F.3d 236, 242-43 (2d Cir. 1999)).
6 Id. at *18.
7 Id. at *20-21 (alteration in original) (quoting Leasco Data Processing Equip. Corp. v. Maxwell, 468 F.2d 1326, 1341 n.11 (2d Cir. 1972)).
8 Id. at *24-25.
9 Id. at *25.
10 Id. at *2.
11 Id. at *36.
12 Id. (internal quotation mark and citation omitted).
13 Id. at *39.
14 Id. at *38.
15 Id. at *43.
16 Id. at *44.
17 Id. at *46-51.
18No. 11 Civ. 9073, 2013 U.S. Dist. LEXIS 22392 (S.D.N.Y. Feb. 19, 2013).
19 Id. at *1-2.
20 Id. at *3.
21 Id. at *4.
22 Id. at *3.
23 Id. at *5.
24 Id. at *2.
25 Id. at *12.
26 Id. at *16.
27 Id. at *17.
28 Id. at *21 (emphasis in original).
29 Id. at *24.
30 Id.
31 Id. at *2 n.2.

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Jurisdiction

Illinois Supreme Court Rules Against The Plaintiffs' Bar And Finds That Asbestos Lawsuit Should Not Be Heard In Illinois

In a closely watched case, the Illinois Supreme Court on December 28, 2012, issued its decision in *Fennell v. Illinois Central R.R. Co.*, No. 113812, ruling that the Circuit Court of St. Clair County abused its discretion in denying defendant's motion to dismiss on the basis of interstate forum non conveniens because there was no nexus to Illinois, let alone to St. Clair County, for plaintiff's asbestos lawsuit. Justice Freeman delivered the opinion, joined in by Justices Garman, Karmeier, Burke and Theis. Justice Kilbride dissented; Justice Thomas took no part in the case.

The importance of the Supreme Court's decision is evident. A decision to dismiss on the basis of forum non conveniens is committed to a trial court's discretion. Overturning a decision committed to a trial court's discretion in Illinois is virtually impossible. The Supreme Court's decision in Fennell, however, sends a message, not only to trial courts but the plaintiffs' bar, that the Supreme Court no longer will tolerate actions that have no place in Illinois.

Factual Background

In 2002, Fennell, with over 80 additional named plaintiffs, brought an action against defendant in the Circuit Court of Jefferson County, Mississippi, seeking recovery for injuries sustained as the result of exposure to asbestos and asbestos containing products while employed by defendant. Fennell resided in Hazelhurst, Mississippi and worked for defendant in Jefferson County, Mississippi. In 2006, Fennell's action was dismissed without prejudice.

In 2009, Fennell filed a complaint in the Circuit Court of St. Clair County, Illinois against defendant, claiming he developed respiratory problems as a result of being exposed to asbestos and other toxic substances while working for defendant. Defendant moved to dismiss based upon interstate forum non conveniens, contending that Mississippi and not Illinois was the most convenient forum to try the case. The Circuit Court of St. Clair County denied defendant's motion to dismiss, ruling that St. Clair County was a convenient forum based upon several findings: (1) substantial documentary evidence critical to plaintiff's case was located a short distance from the St. Clair County courthouse; (2) in-court testimony of two important witnesses for plaintiff would be available if the case were tried in Illinois but unavailable if the case were tried in Mississippi; (3) St. Clair County is closer than Mississippi for plaintiff's expert witness from Chicago; (4) the citizens of St. Clair County had an interest in the litigation; and (5) the St. Clair County circuit dockets were no longer congested.

The Appellate Court, in a split 2-1 decision, affirmed and the Illinois Supreme Court granted leave to appeal.

The Supreme Court's Decision: All Public And Private Factors Must Be Evaluated And Not Weighed Against Each Other And A Foreign Plaintiff's Choice Of Illinois Is Entitled To Less Deference

The Supreme Court found several flaws in the trial court's decision, leading the Supreme Court to hold that the trial court abused its discretion when it denied defendant's motion to dismiss the Illinois action in favor of an action in Mississippi. It first found that the trial court failed to consider all the relevant private and public interest factors in its analysis. According to the Court, a trial court should not weigh private interest factors against public interest factors but rather evaluate the total circumstances of the case in light of all the factors to determine whether the balance of factors strongly favors dismissal. Additionally, the Supreme Court held that although a plaintiff's right to select the forum is substantial, when the plaintiff is foreign to the chosen forum and when the action giving rise to the litigation did not occur in the chosen forum, the plaintiff's choice of forum is accorded less deference.

In looking at the private factors, the Court found that they weighed heavily in favor of the convenience of a Mississippi forum over an Illinois forum because the alleged exposure occurred in Mississippi and Louisiana; the vast majority of the identified witnesses, including the treating physicians, are located in Mississippi and are not subject to Illinois subpoenas; and a jury view of the premises would occur outside of Illinois.

As to the public interest factors, the Supreme Court found that Illinois simply had no relevant or practical connection with the litigation. The only connections Illinois had with this case were the offices of the parties' counsel, accessible and transportable documents in the possession of defendant's counsel; and a compensated expert witness for plaintiff. The Court found that these "connections" did not provide "a significant factual connection with the instant case that justify imposition of the burdens of a litigation upon the citizens and the court system of St. Clair County and Illinois."

In summary, the Court found that the weight of the private and public interest factors greatly favored Mississippi. Further, the deference to plaintiff's choice of an Illinois forum was significantly lessened because: (1) Illinois was plaintiff's second choice of forum; and (2) plaintiff did not reside in Illinois and the action did not arise in Illinois. Mississippi and not Illinois therefore should hear this case.

Learning Point

This case shows how arguments can be fashioned in order to overturn a trial court's discretionary ruling regarding forum non conveniens motions. The Supreme Court recognized that a trial court's ruling on a forum non conveniens motion cannot be overturned in the absence of an abuse of discretion. In order to overturn such a decision, a reviewing court must conclude that no reasonable person would take the view of the trial court. The Supreme Court held that the Fennell defendant met that test in this case. The Supreme Court's decision provides a "roadmap" for future cases challenging the discretionary rulings of trial courts in deciding such forum non conveniens motions.

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Jurisdiction

PA Federal Court Denies Use of State Law Remedy in Employee Discrimination Claim

Employee discrimination suits routinely allege claims under the federal anti-discrimination statutes as well as state statutes or common law. While the standard of proof for a violation under these statues may be identical, the damages available may differ vastly. Compensatory and punitive damages are capped under the federal anti-discrimination laws depending on the number of those working for the employer.[1] However, these caps may not exist under state statutes or common law, providing plaintiffs with the possibility of a more lucrative recovery by alleging the purported discrimination also violated state law. As a result, many have tried to take advantage of employers who have operations in more than one state -- asserting claims under statutes enacted by states in which they have never worked, but where the employer may have their corporate/ home offices or where the employee's supervisor may be located.

Recently, a Pennsylvania federal court addressed this area of the law by holding that individuals employed by companies doing business in the state, but who neither live nor work in the Commonwealth, lack standing to assert discrimination claims under the Pennsylvania Human Relations Act (PHRA). In Blackman v. Lincoln National Corporation, et al., U.S. District Court for the Eastern District of Pennsylvania, Civil Action No. 10-6946 (December 10, 2012), the plaintiff asserted sex and age discrimination claims against her former employers, alleging violations of Title VII, the Age Discrimination in Employment Act and the PHRA. The defendant, Lincoln National Corporation (Lincoln), is an Indiana-founded company with its principle place of business in Radnor, Penn., and the plaintiff is an Illinois resident who worked for Lincoln in their Illinois office. Lincoln argued that the state law claims should be dismissed because the PHRA does not apply to individuals that neither reside nor work in Pennsylvania.

The federal district court judge agreed and dismissed the PHRA claims, concluding that the purpose and intent of the PHRA is to protect "people of the Commonwealth of Pennsylvania". The court found that the relevant location for determining the application of the PHRA is where the employee works, not the employer's location or the location where the decision to take discriminatory action took place. Even the plaintiff's attendance at quarterly meetings and daily interactions with employees located in Pennsylvania were insufficient to justify extending the reach of the PHRA to a non-resident employee not working in Pennsylvania.

The court left open the question of whether the protections afforded by the PHRA extend to a broader class of individuals, such as those who work but do not reside in Pennsylvania. The court observed, however, that limiting the scope of the PHRA to protect only Pennsylvania "residents" would create a problem with the protection afforded by New Jersey's counterpart to the PHRA, the New Jersey Law Against Discrimination, N.J. Stat. §§10:5-1, et seq., which has been limited to only those who work in New Jersey.

In this global economy, it is routine to have employees located in states outside that where a company's main offices are located. In fact, it is becoming commonplace to have supervisors or managers located in a state different from the one where employees may be located. Limiting an employee's legal remedies to those statutes effective in the state in which he/she resides and works brings a level of predictability and common sense to this area of the law.

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1 Federal law caps punitive and compensatory damages (excluding back pay and front pay awards) to $50,000 for employers with 15 to 100 employees; $100,000 for employers with 101 to 200 employees; $200,000 for employers with 201 to 500 employees; and $300,000 for employers who employ more than 500 employees.

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Jurisdiction

U.S. Supreme Court Narrows Federal Jurisdiction For Malpractice Actions Arising out of Federal Patent Issues

Brief Summary

In a 9-0 decision, the U.S. Supreme Court held that state courts have jurisdiction to resolve state legal malpractice actions even if the determination of the malpractice claim requires resolution of a disputed federal patent question. This decision effectively overrules the Federal Circuit's prior case law in *Air Measurement Technologies, Inc. v. Akin Gump Strauss Hauer & Feld, LLP*, 504 F. 3d 1262 (2007) and *Immunocept, LLC v. Fulbright & Jaworski, LLP*, 504 F. 3d 1281 (2007). Although the Supreme Court did not expressly rule out the possibility of federal jurisdiction in these cases, it did suggest that all but the rarest patent malpractice cases belong in state court.

Complete Summary

Gunn previously represented Vernon Minton in prior patent infringement litigation. In that underlying litigation, however, the district court declared Minton's patent invalid because he had placed it "on sale" more than one year prior to filing his application. Minton later determined that he may have prevailed under the "experimental use" exception to the on-sale bar, but that Gunn was allegedly negligent in failing to advise him of that available argument. Minton then sued Gunn for legal malpractice in Texas state court. After losing in state court, however, Minton requested that the case be sent to federal court based upon 28 U. S. C. § 1338(a)'s provision for exclusive federal jurisdiction over any case "arising under any Act of Congress relating to patents." The Texas Supreme Court agreed with Minton and found that because Section 1338(a) provided exclusive jurisdiction for claims relating to patents, the state court lacked jurisdiction over the state law legal malpractice action against Gunn. Gunn then petitioned the U.S. Supreme Court to address the scope of federal "arising under" jurisdiction.

The question, as the Supreme Court saw it, was whether a state law malpractice claim could be said to "arise under" federal patent law simply because the court hearing it would address patent law issues in deciding whether the lawyer defendant had erred and whether that error had cost his client. The "arising under" language used in Section 1338(a) has its foundation in the U.S. Constitution. Section 1338(a) is particularly focused on "any civil action arising under any Act of Congress relating to patents." Section 1338(a) is particularly noteworthy because, unlike most causes of action, it provides for exclusive federal jurisdiction if the "arising under" requirement is met. In most patent cases, the "arising under" analysis is quite easy because the complaint asserts a claim that is clearly based on federal patent law, such as a patent infringement claim or a complaint seeking a declaration of invalidity. The U.S. Supreme Court has also held, however, that "arising under" jurisdiction may exist in cases where the cause of action is not based upon federal law, but where there is an underlying federal issue arising from the well-pled cause of action. See, e.g., *Grable & Sons Metal Products, Inc. v. Darue Engineering & Mfg*., 545 U. S. 308 (2005). In Grable, the U.S. Supreme Court noted that this other form of "arising under" jurisdiction will only exist when the cause of action alleged in the complaint: (1) necessarily raises a stated federal issue; (2) that is actually disputed; (3) substantial, and (4) capable of resolution in federal court without disrupting the federal-state balance approved by Congress.

A legal malpractice action is generally a state law claim. Applying the foregoing factors, the Supreme Court ruled that Minton's malpractice claim did not arise under patent law. The Court went further, however, and observed that: "state legal malpractice claims based on underlying patent matters will rarely, if ever, arise under federal patent law for purposes of §1338(a)." The Court acknowledged that the federal patent question at issue here, i.e., the viability of the experimental use exception, was necessary and actually disputed in Minton's legal malpractice claim. The Court determined, however, that that federal question was not "substantial." The resolution lacked significance to the federal system because the patent law issue would only be resolved in a hypothetical sense in the context of the malpractice litigation. Regardless of whether the state court determined that the experimental use exception applied, Minton's patent would remain invalid. State court adjudication of these matters in similar cases will not undermine the development of federal patent law. The Court also found the fourth requirement of Grable unsatisfied, stating: "We have no reason to suppose that Congress—in establishing exclusive federal jurisdiction over patent cases—meant to bar from state courts state legal malpractice claims simply because they require resolution of a hypothetical patent issue."

In addition, although not explicitly holding such, the Supreme Court suggested that state court decisions involving patent issues such as invalidity or obviousness should not have preclusive effect on other courts. For example, a state court decision involving a patent dispute that results in a state court finding that a particular patent is invalid should have no preclusive effect on either the U.S. Patent and Trademark Office or federal courts. Rather, "the result would be limited to the parties and patents that had been before the state court."

Significance of Opinion

This opinion presents issues of considerable significance. It will have a huge impact because it appears that legal malpractice actions involving underlying patent issues that are currently being litigated in federal court will most likely be dismissed for lack of subject matter jurisdiction, absent diversity or other special conditions. Although the Supreme Court did not hold that a patent malpractice case could never arise under federal patent law, it made clear its view that such cases will “rarely, if ever” exist. It appears that virtually all legal malpractice actions arising out of underlying patent issues will be litigated in state courts, again absent diversity or other special conditions. This case also raises a number of other issues, such as its effect on cases where judgments have already been entered. Because subject matter jurisdiction may be raised in federal courts at any time so long at the case remains live, including on appeal, any federal patent malpractice case in which a judgment has not yet become final would be subject to dismissal, either on motion of a party (even a plaintiff like Minton seeking a “do-over”) or by the court where the case is pending. The application of statutes of limitations to cases dismissed in this way that are refiled in state court also presents an important issue.

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Evidence and Procedure

U.S. Supreme Court Rules That the Government Does Not Have an Unlimited Amount of Time in Which to Bring Civil Penalty Actions

In a unanimous decision written by Chief Justice John G. Roberts, Jr., the United States Supreme Court has ruled that the Government does not have an unlimited amount of time to bring civil penalty actions based on fraud. In *Gabelli v. Securities* and *Exchange Commission*, 11-1274 (U.S. Feb. 27, 2013), the Supreme Court ruled that 28 U.S.C. § 2462, the five-year statute of limitations applicable to civil penalty actions brought by the Government, starts running on the date the allegedly fraudulent conduct occurred and is not subject to a discovery rule in cases based on fraud. Section 2462 states that "[e]xcept as otherwise provided by Act of Congress," an action for a civil penalty "shall not be entertained unless commenced within five years from the date when the claim first accrued." The Securities and Exchange Commission (the "SEC") had argued that a civil penalty claim sounding in fraud accrues when the Government discovers or reasonably should have discovered the violation. But the Court squarely rejected the SEC's argument, noting the "lack of textual, historical, or equitable reasons to graft a discovery rule onto the statute of limitations of § 2462."[1]

The SEC originally brought claims against Marc Gabelli, a former portfolio manager of Gabelli Global Growth Fund (the "GGGF"), and Bruce Alpert, the Chief Operating Officer of Gabelli Funds, LLC, alleging, among other things, that Gabelli and Alpert had aided and abetted a violation by Gabelli Funds of Section 206 of the Investment Advisers Act of 1940, 15 U.S.C. §§ 80b-6(1)-(2). According to the SEC, Gabelli Funds had violated Section 206 by allowing one investor to engage in frequent trading of mutual fund shares in exchange for a small investment in a Gabelli hedge fund without disclosing the trading or investment to the GGGF board of directors. Although Gabelli Funds had caused the trading at issue to end in August 2002, the SEC did not file its complaint until April 2008. The SEC sought to avoid the bar of Section 2462's five-year statute of limitations by arguing that it had not discovered the alleged fraud until late 2003, after then-New York Attorney General Eliot Spitzer announced his investigation of market timing in mutual funds.

At the motion to dismiss stage of the case, the United States District Court for the Southern District of New York dismissed as time-barred the SEC's civil penalty claim for aiding and abetting a violation of Section 206.[2] But, on appeal by the SEC, the United States Court of Appeals for the Second Circuit reversed the District Court and held that, for purposes of Section 2462's statute of limitations, a claim sounding in fraud does not accrue until the SEC discovers it or reasonably should have discovered it.[3]

The Supreme Court granted certiorari on September 25, 2012, and oral argument was held on January 8, 2013. In its 9-0 decision, the Court explained that "the most natural reading" of Section 2462 is that "a claim based on fraud accrues—and the five-year clock begins to tick—when a defendant's allegedly fraudulent conduct occurs."[4] The Court noted that since the 1800s, it has been the "standard rule" that an action accrues "when the plaintiff has a complete and present cause of action."[5] Moreover, the Court said, statutes of limitation are vital to the welfare of society and advance the basic policies of repose and elimination of stale claims.[6] That is particularly so in cases involving the pursuit of penalties, since they are not intended to compensate but are instead intended to punish and label wrongdoers.[7]

According to the Court, the discovery rule is an exception to the general rule of accrual, and can suspend the running of a limitations period where a plaintiff has been injured by fraud and remains ignorant of it, without any fault or want of diligence or care on his or her part.[8] But, the Court explained, the discovery rule has not been and should not be applied in a case like this one, where the plaintiff is not a victim seeking recompense for a latent injury, but is instead the Government bringing an enforcement action.[9] Unlike the situation of an individual victim who may not know he or she has been wronged until an injury becomes apparent, the Government is charged with rooting out potential claims. That is particularly so here, where the SEC has as its mission to investigate potential violations of the federal securities laws and has "many legal tools at hand to aid in that pursuit."[10]

The Court further explained that the discovery rule proposed by the SEC would present particular challenges for the courts, because it would require courts to determine exactly when the Government knew or should have known of a fraud.[11] This would be a very challenging inquiry to force upon courts given that many individuals and agencies might have knowledge of potential wrongdoing, issues concerning agency priorities and resource constraints play a role in the government's determinations about whether to bring enforcement actions, and governmental privileges might come into play if discovery were sought on the issues of when the Government knew or should have known about wrongdoing.[12] Given the challenges associated with applying the discovery rule to Government penalty actions, the Court held that Congress is better suited than courts are to determine whether such a rule should apply.[13]

The Supreme Court's decision is a blow to the enforcement powers of all Government agencies. The Government can no longer pursue expired civil penalty claims sounding in fraud simply by pleading reliance on the discovery rule. And companies and individuals can take some comfort in the fact that conduct that occurred more than five years ago cannot form the basis of a penalty claim, unless the Government can establish fraudulent concealment, equitable estoppel or equitable tolling.[14]

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1 *Gabelli v. SEC*, No. 11-274, slip op. at 11 (U.S. eb. 27, 2013).
2 *SEC v. Gabelli*, No. 08-CV-3868, 2010 WL 1253603 (S.D.N.Y. Mar. 17, 2010).
3 *SEC v. Gabelli*, 653 F.3d 49, 59-61 (2d Cir. 2011). Note that this decision was based solely on the pleadings and was not a decision on the merits of the dispute.
4 *Gabelli v. SEC*, No. 11-274, at 4.
5 Id. at 5 (internal quotation marks and citation omitted).
6 Id.
7 Id. at 8-9.
8 Id. at 6.
9 Id. at 6-8.
10 Id. at 8.
11 Id. at 9-11.
12 Id.
13 Id. at 11.
14 Note that defendants deny any wrongdoing and the case is yet to be tried. After the case is remanded, defendants will have the opportunity to refute the SEC's claims.

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Evidence and Procedure

U.S. Court of Appeals for the Second Circuit Court Affirms Dismissal of Anti-Terrorism Act Claims Against UBS

A federal appellate court in New York has held that under the Anti-Terrorism Act (ATA), a bank cannot be held liable for the acts of terrorist organizations, such as Hamas and Hezbollah, solely because the bank provided financial services or otherwise dealt with a state sponsor of terrorism, such as Iran. The court further held that the ATA does not allow claims for aiding and abetting.

The decision comes in *Rothstein v. UBS AG*, where the US Court of Appeals for the Second Circuit affirmed the dismissal of plaintiffs' ATA claims for failure to state a claim. According to the court, the plaintiffs failed to plausibly allege that customary banking services provided to Iran were the proximate cause of injuries suffered due to terrorist attacks by Hamas and Hezbollah.

Rothstein is significant because it is the first appellate decision to reasonably constrain the ATA on third-party liability by imposing a meaningful proximate causation requirement. The Second Circuit's rationale, moreover, may prove helpful to financial institutions in other cases in which plaintiffs attempt to hold banks liable for routine banking transactions based on allegations that such transactions bestowed some type of downstream benefit on those who injured the plaintiffs. *Rothstein's* holding on aiding and liability is not only important in the ATA context, it also may prove helpful in defending against attempts by plaintiffs to read secondary liability into other statutes that do not expressly provide for it.

The plaintiffs in *Rothstein* brought claims against UBS pursuant to the ATA, a statute that provides a private cause of action for "[a]ny national of the United States injured in his or her person, property, or business by reason of an act of international terrorism." UBS moved to dismiss plaintiffs' claims in the district court, arguing that plaintiffs lacked standing because UBS's alleged conduct was not "fairly traceable" to plaintiffs' injuries. UBS also argued that plaintiffs failed to state a claim because they had not adequately alleged that UBS's conduct was a proximate cause of their injuries. The district court agreed, and dismissed plaintiffs' claims for lack of standing and failure to state a claim. The district court further held that UBS could not be held liable on an aiding and abetting theory because the ATA does not allow civil aiding and abetting claims.

On appeal, the Second Circuit reversed the district court's decision on standing, but affirmed the plaintiffs' failure to state a claim due to lack of proximate causation. The Second Circuit explained that "the requirement that a complaint allege an injury that is fairly traceable defendants' conduct for purposes of constitutional standing is a lesser burden than the requirement that it show proximate cause."

To satisfy the "fairly traceable" requirement necessary to establish standing to sue under the Constitution, a plaintiff need allege only that defendants' conduct was "a small incremental step" toward plaintiffs' injury. The court found that this minimal standard was satisfied by plaintiffs' allegations that UBS provided banknotes to Iran, and that Iran, in turn, funded terrorist groups that attacked the plaintiffs.

The Second Circuit's discussion about standing set the stage for the its decision against plaintiffs on proximate causation, which the appellate court unequivocally held imposed a higher burden on the plaintiffs than the "fairly traceable" standing requirement. At the outset, the court rejected plaintiffs' attempt to read the proximate causation requirement out of the ATA by arguing that causation should be presumed.

Specifically, plaintiffs argued that the common law permits a court to presume causation where a defendant is alleged to have engaged in a violation of law, and that, accordingly, causation could be presumed in Rothstein based upon plaintiffs' allegations that UBS violated US laws prohibiting US persons from dealing with Iran. The Second Circuit rejected this argument, holding that the "by reason of" language in the ATA imposes a proximate causation requirement, as courts have held with regard to the identical language that appears in the RICO and Clayton Antitrust Acts. The Second Circuit explained that plaintiffs' interpretation of the ATA "would mean that any provider of U.S. currency to a state sponsor of terrorism would be strictly liable for injuries subsequently caused by a terrorist organization associated with that state." But, "[i]f Congress had intended to impose strict liability, we have no doubt that it would have found words more susceptible to that interpretation, rather than repeating the language it had used in other statutes to require a showing of proximate cause."

Having concluded that plaintiffs were required to show nothing less than proximate causation, the Second Circuit then explained why plaintiffs' allegations fell short of doing so:

The Complaint does not allege that UBS was a participant in the terrorist attacks that injured plaintiffs. It does not allege that UBS provided money to Hizbollah or Hamas. It does not allege that U.S. currency UBS transferred to Iran was given to Hizbollah or Hamas. And it does not allege that if UBS had not transferred U.S. currency to Iran, Iran, with its billions of dollars in reserve, would not have funded the attacks in which plaintiffs were injured …. Iran is a government, and as such it has many legitimate agencies, operations, and programs to fund. We see no nonconclusory allegation in the Complaint that plausibly shows that the moneys UBS transferred to Iran were in fact sent to Hizbollah or Hamas or that Iran would have been unable to fund the attacks by Hizbollah and Hamas without the cash provided by UBS.

In addition, the Second Circuit held that the district court's holding that the ATA does not permit aiding and abetting claims. Following the Supreme Court's decision in Central Bank of Denver v. First Interstate Bank of Denver—which held that an implicit congressional intent to impose aiding and abetting liability could not plausibly be inferred from statutory silence—the Second Circuit concluded that because the ATA does not expressly provide for civil aiding and abetting liability, the ATA cannot be interpreted to allow civil claims for aiding and abetting liability. In so holding, the Second Circuit contrasted certain of the ATA's criminal provision, which do expressly provide for aiding and abetting liability.

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Evidence and Procedure

Valid Appellate Issues Ignored If Lower Court's Decision Not Challenged

In *Joseph E. Brown v. McCue Mortgage Co.,* No. AC34022, 2012 Conn. App. LEXIS 601 (Conn. App. Dec. 18, 2012), the Connecticut Appellate Court was presented with an appeal from the Superior Court which granted pre-answer motions to dismiss of a Complaint seeking declaratory relief, injunctive relief and an accounting as to a piece of real property owned by plaintiff Joseph E. Brown ("Plaintiff") located at 108 South Main Street in Brooklyn, Connecticut (the "Property"). Defendants, McCue Mortgage Company ("McCue") and Connecticut Housing Finance Authority (the "Authority)(collectively "Defendants"), held the first and second mortgages, respectively, on the Property. On appeal, Plaintiff raised a number of claims. However, Plaintiff failed to raise or to brief the issue on which the case was dismissed by the trial court, and therefore the Appellate Court declined to review the issues raised in Plaintiff's appeal such that the appeal was dismissed.

In November, 1996, Plaintiff contracted for the sale of the Property and entered into a mortgage agreement with McCue. In April, 2007, Plaintiff completed a loan modification with the Authority. Although McCue and the Authority worked with Plaintiff on a temporary loss mitigation plan and Plaintiff paid $5,115 to McCue in August, 2009, neither McCue or the Authority received any funds from Plaintiff thereafter. The Authority commenced a foreclosure action against Plaintiff on April 30, 2010 (the "Foreclosure Action"). Summary judgment as to liability was granted in favor of the Authority on August 3, 2010, and after foreclosure mediation was terminated on March 24, 2011, the Authority filed a motion for strict foreclosure. Plaintiff did not interpose any defense to the amount owed, and on July 21, 2011, the Superior Court rendered a judgment of foreclosure by sale.

On August 8, 2011, Plaintiff filed the Complaint underlying this action. On August 23, 2011, McCue and the Authority filed a motion to dismiss the Complaint, arguing that because of the Foreclosure action, this action could not proceed under the "prior pending action doctrine." Notwithstanding Plaintiff's objections, the Superior Court granted Defendants' motion to dismiss on October 24, 2011. In turn, Plaintiff filed a motion asking the Superior Court to articulate the basis of its dismissal of his action, and the Superior Court granted the motion, citing the "prior pending action doctrine" as its ground for dismissal. Plaintiff then appealed.

Before the Appellate Court Plaintiff presented many claims. In response, Defendants argued that Plaintiff failed to raise or brief the grounds of the Superior Court's dismissal. The Appellate Court found that because Plaintiff failed to challenge the basis of the Superior Court's dismissal, it declined to reach the issues he did brief.

The Appellate Court held that "[Appellate] practice requires an appellant to raise claims of error in his original brief, so that the issue as framed by him can be fully responded to by the appellee in its brief, and so that [the Court] can have the full benefit of that written argument." (Internal quotation marks omitted.) *Grimm v. Grimm*, 276 Conn. 377, 394 n.19, 886 A.2d 391 (2005), *cert. denied*, 547 U.S. 1148, 126 S. Ct. 2296, 164 L. Ed. 2d 815 (2006). Further, it held that for "this court judiciously and efficiently to consider claims of error raised on appeal . . . the parties must clearly and fully set forth their arguments in their briefs. We do not reverse the judgment of a trial court on the basis of challenges to its rulings that have not been adequately briefed." (Internal quotations marks omitted.) *Paoletta v. Anchor Reef Club at Branford, LLC,* 123 Conn. App. 402, 406, 1 A.3d 1238, cert. denied, 298 Conn. 931, 5 A.3d 491 (2010).

Plaintiff failed to challenge the basis of the Superior Court's dismissal of his action under the "prior pending action doctrine." Thus, the Appellate Court held that "where alternative grounds found by the reviewing court and unchallenged on appeal would support the trial court's judgment, independent of some challenged ground, the challenged ground that forms the basis of the appeal is moot because the court on appeal could grant no practical relief to the [appellant]." *Green v. Yankee Gas Corp.,* 120 Conn. App. 804, 805, 993 A.2d 982 (2010). "[I]t is not the province of an appellate court to decide moot issues disconnected from the granting of actual relief." Id., 806; see also *Lyon v. Jones*, 291 Conn. 384, 394-95, 968 A.2d 416 (2009) (holding that Appellate Court improperly considered merits of claims brought where there was independent basis for upholding summary judgment rendering claims raised by appellant moot).

Since the Appellate Court held that there were unchallenged grounds to support the Superior Court's dismissal, the Appellate Court could grant no practical relief to Plaintiff on the claims he actually did raise in his brief.

Learning Point

Under Connecticut Appellate Practice, if a party fails to challenge the basis of a lower court's dismissal, the Appellate Court will not reach any other valid issues he actually did brief. Further, under the "prior pending action doctrine," a foreclosed Connecticut homeowner cannot file a new lawsuit against its mortgagees seeking declaratory relief, injunctive relief and an accounting after judgment of foreclosure enters.

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Evidence and Procedure

Kentucky Supreme Court Removes the Physical Impact Requirement

In a reversal of long-standing law, the Kentucky Supreme Court recently removed the requirement that a plaintiff suffer a physical impact or touching to recover for negligence claims involving emotional distress, often described as the "impact rule." Now, a plaintiff must only show that the defendant was negligent and prove by expert testimony that the plaintiff suffered mental stress or an emotional injury that is greater than a reasonable person could be expected to endure given the circumstances.

In *Osborne v. Keeney*, No. 2010-SC-000430-DG, slip op. (Ky. Dec. 20, 2012), the plaintiff sued her former attorney, claiming he committed legal malpractice by failing to file a lawsuit within the applicable statute of limitations. By way of the "suit-within-a-suit" doctrine, which requires a legal malpractice plaintiff to establish that she would have recovered in the underlying lawsuit absent the malpractice, the plaintiff alleged that she lost the ability to recover from a pilot who crashed his airplane into the plaintiff's home. The plaintiff presented medical evidence that she was emotionally unstable as a result of the destruction of her home and personal belongings. However, no debris from the plane crash struck the plaintiff. Thus, the Court was left to determine whether the "impact rule" would have prevented the plaintiff's recovery for the purely emotional distress damages allegedly caused by the crash.

Noting that the rule existed in only a few remaining states, the Court abandoned the "impact rule" and held that a physical impact or touching was no longer required for recovery under a negligence theory. Further, the policy concerns which historically had supported the impact rule-e.g., damages being too remote, which may tend to promote fraud-were no longer sufficient to justify adherence to this rule. According to the Court, while the rule appeared on its face to be a bright line for determining when a plaintiff is entitled to recover for emotional injuries, in practice the rule had been stretched to the point of dilution. Therefore, the Court held that negligence cases should be analyzed under traditional principles of duty, breach, causation, and damages, the only caveat being that recovery should be provided for "severe" or "serious" emotional injury, which must be established by expert testimony.

At first blush, this holding appears to remove the very safeguards that prevented recovery for remote or dubious emotional injuries in Kentucky. A deeper look, however, dispels this notion. By holding that traditional principles of negligence apply when analyzing a claim for emotional injuries, the Court in effect put Kentucky in line with the majority of jurisdictions (including Ohio), which have adopted the "foreseeability test." This test requires that when analyzing any negligence claim in Kentucky, which now includes one for purely emotional damages, consideration must be given to whether the harm resulting from the negligence was foreseeable. See *T&M Jewelry, Inc. v. Hicks*, 189 S.W.3d 526, 531 (Ky. 2006).

Nevertheless, it remains to be seen whether this holding will create a flood of litigation, as a plaintiff alleging purely emotional injuries and armed with the assistance of a willing medical expert may now have enough to create an issue of fact for the jury.

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Product Liability

Massachusetts: No Liability for Somebody Else's Products

Massachusetts today joined other jurisdictions in holding that a defendant is not liable for the products of others – specifically, asbestos-containing gaskets, packing and insulation.

The decision affirmed summary judgments for two defendants that supplied equipment to the *Navy. Whiting v. CBS*, 2013 Mass. App. Unpub. LEXIS 183 (Mass. App. Ct. Feb. 14, 2013). Westinghouse "supplied its turbines uninsulated." There was evidence that Crane was one "of as many as seven different manufacturers" of valves aboard ship. "Although Crane sold products containing asbestos, such as gaskets, Crane never manufactured any materials or products containing asbestos." The Massachusetts Appeals Court found it significant that "any insulation originally installed on the turbines or valves would have been removed and replaced from unknown sources in two overhauls" before the decedent was aboard ship. "Accordingly, there is no evidence that Whiting's mesothelioma was caused by asbestos products manufactured by the defendants."

Whiting is therefore in line with similar decisions in asbestos cases in California (*O'Neil v. Crane Co., 53 Cal*. 4th 335, 342 (2012)); Washington (*Braaten v. Saberhagen Holdings*, 198 P.3d 493 (Wash. 2008) and *Simonetta v. Viad Corp.,* 197 P.3d 127 (Wash. 2008)); Maryland (*Ford Motor Co. v. Wood*, 703 A.2d 1315 (Md.Ct.Spec.App. 1998) abrogated on other grounds in *John Crane, Inc. v. Scribner*, 800 A.2d 727 (Md. 2002)); and the 6th Circuit (*Lindstrom v. A-C Product Liability Trust*, 424 F.3d 488, 495-497(6th Cir. 2005)).

The case also involves some questionable ID testimony – the only witness had not seen decedent "working on the turbines, but he opined that Whiting would have removed and replaced asbestos gaskets and packing in Crane and Chapman valves and other equipment" – but that was not the court's apparent focus so much as the "not the defendant's products" rationale.

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Product Liability

No Recovery for Emotional Distress If Claimant Had No Contemporaneous Awareness That Defective Product Was Cause of Injury

The California Court of Appeal has clarified that the rules for a bystander's recovery for the emotional distress of witnessing a loved one's injury or death requires a contemporaneous perception of what caused the injury. This can be particularly relevant in a product liability case where it is not always immediately apparent that a product failure is what caused the injury.

Background

In *Fortman v. Förvaltningsbolaget Insulan AB* (January 10, 2013), the California Court of Appeal for the Second Appellate District was asked to consider whether a claimant may recover for the emotional distress of witnessing an injury caused by a product defect where the claimant did not meaningfully comprehend that the defective product caused the injury. In that case, the plaintiff, Barbara Fortman, sought to recover as a bystander for the emotional distress she suffered when she witnessed the death of her brother Robert Myers while they were scuba diving off the coast of Catalina Island. While witnessing the accident, Fortman thought her brother had suffered a heart attack. She later learned that a plastic flow restriction insert manufactured by the defendant had become lodged in Myers's regulator, thereby preventing him from getting enough air to breathe while underwater.

Prior Law

In *Thing v. La Chusa* (1989) 48 Cal.3d 644, 667-668, the California Supreme Court established three mandatory requirements to state a claim for negligent infliction of emotional distress (NIED) under the bystander theory of recovery. "[A] plaintiff may recover damages for emotional distress caused by observing the negligently inflicted injury of a third person if, but only if, said plaintiff:

1. Is closely related to the injury victim,
2. *Is present at the scene of the injury-producing event at the time it occurs and is then aware that it is causing injury to the victim*, and
3. As a result suffers serious emotional distress – a reaction beyond that which would be anticipated in a disinterested witness and which is not an abnormal response to the circumstances." (Emphasis added.)

The court expressly emphasized the mandatory, exclusive nature of these requirements.

Arguments

Fortman cautioned the court against stringently applying the second *Thing* requirement when a close relative suffers a product-related injury where strict liability principles apply. The Appellate Court nevertheless pointed out that it was undisputed that Fortman did not have a contemporaneous understanding or awareness that the defective product was causing her brother's injury and, in fact, thought that her brother was drowning due to a heart attack. "Post- Thing, we are limited by a more stringent definition of the contemporaneous awareness requirement. Based upon the mandatory requirements set forth in *Thing*, we also reject Fortman's attempt to expand bystander recovery to hold a product manufacturer strictly liable for emotional distress when the plaintiff observes injuries sustained by a close relative arising from an unobservable product failure. To do so would eviscerate the second Thing requirement."

Although Fortman contended that applying the second Thing requirement precluded bystander recovery in all strict product liability cases, the Appellate Court disagreed. It noted that "we can envision a number of scenarios in which a bystander plaintiff might recover against a product manufacturer for NIED" such as "if he or she were present at a backyard barbecue and observed the defendant's propane tank connected to the barbecue explode and injure a close relative, or if the plaintiff observes a ladder collapse and injure a close relative." It reasoned that "[t]he plaintiff need not know the cause of the propane tank explosion or why the ladder collapsed," but "the plaintiff must have a contemporaneous awareness of the causal connection between the defendant's product as causing harm and the resulting injury to the close relative."

Ruling

The Appellate Court concluded by acknowledging that "[t]he Supreme Court in *Thing* admittedly created an arbitrary restriction on bystander recovery, stating 'drawing arbitrary lines is unavoidable if we are to limit liability and establish meaningful rules for application by litigants and lower courts.'" It explained that "[u]nless and until the Supreme Court revisits *Thing*, it is binding on this court."

The ruling in *Fortman* makes clear that the "contemporaneous sensory perception" requirement under *Thing* entails the mandatory requirement of a contemporaneous and meaningful awareness that a defendant's product caused the injury. Litigants may continue to debate what a "meaningful awareness" means in the context of differing fact patterns. This case is important in the defense of product liability cases where a plaintiff seeks recovery for emotional distress as a bystander, and it can be cited to limit such recovery in appropriate cases. If you have any questions regarding the impact of this case on the defense of a products or general liability matter, please contact us.

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Social Media

Socially Aware Looks Back: The Social Media Law Year In Review

2012 was a momentous year for social media law. We've combed through the court decisions, the legislative initiatives, the regulatory actions and the corporate trends to identify what we believe to be the ten most significant social media law developments of the past year–here they are, in no particular order:

***Bland v. Roberts* – A Facebook "like" is not constitutionally protected speech**

Former employees of the Hamptons Sheriff's Office in Virginia who were fired by Sheriff BJ Roberts, sued claiming they were fired for having supported an opposing candidate in a local election. Two of the plaintiffs had "liked" the opposing candidate's Facebook page, which they claimed was an act of constitutionally protected speech. A federal district court in Virginia, however, ruled that a Facebook "like" ". . . is insufficient speech to merit constitutional protection"; according to the court, "liking" involves no actual statement, and constitutionally protected speech could not be inferred from "one click of a button."

This case explored the increasingly- important intersection of free speech and social media with the court finding that a "like" was insufficient to warrant constitutional protection. The decision has provoked much criticism, and it will be interesting to see whether other courts will follow the Bland court's lead or take a different approach.

***New York v. Harris* – Twitter required to turn over user's information and tweets**

In early 2012, the New York City District Attorney's Office subpoenaed Twitter to produce information and tweets related to the account of Malcolm Harris, an Occupy Wall Street protester who was arrested while protesting on the Brooklyn Bridge. Harris first sought to quash the subpoena, but the court denied the motion, finding that Harris had no proprietary interest in the tweets and therefore did not have standing to quash the subpoena. Twitter then filed a motion to quash, but the court also denied its motion, finding that Harris had no reasonable expectation of privacy in his tweets, and that, for the majority of the information sought, no search warrant was required.

This case set an important precedent for production of information related to social media accounts in criminal suits. Under the *Harris* court's ruling, in certain circumstances, a criminal defendant has no ability to challenge a subpoena that seeks certain social media account information and posts.

The National Labor Relations Board (NLRB) issued its third guidance document on workplace social media policies

The NLRB issued guidance regarding its interpretation of the National Labor Relations Act (NLRA) and its application to employer social media policies. In its guidance document, the NLRB stated that certain types of provisions should not be included in social media policies, including: prohibitions on disclosure of confidential information where there are no carve-outs for discussion of an employer's labor policies and its treatment of employees; prohibitions on disclosures of an individual's personal information via social media where such prohibitions could be construed as limiting an employee's ability to discuss wages and working conditions; discouragements of "friending" and sending unsolicited messages to one's co-workers; and prohibitions on comments regarding pending legal matters to the degree such prohibitions might restrict employees from discussing potential claims against their employer.

The NLRB's third guidance document illustrates the growing importance of social media policies in the workplace. With social media becoming an ever-increasing means of expression, employers must take care to craft social media policies that do not hinder their employees' rights. If your company has not updated its social media policy in the past year, it is likely to be outdated.

***Fteja v. Facebook, Inc.* and *Twitter, Inc. v. Skootle Corp.* – Courts ruled that the forum selection clauses in Facebook's and Twitter's terms of service are enforceable**

In the Fteja case, a New York federal court held that a forum selection clause contained in Facebook's Statement of Rights and Responsibilities (its "Terms") was enforceable. Facebook sought to transfer a suit filed against it from a New York federal court to one in Northern California, citing the forum selection clause in the Terms. The court found that the plaintiff's clicking of the "I accept" button when registering for Facebook constituted his assent to the Terms even though he may not have actually reviewed the Terms, which were made available via hyperlink during registration.

In the *Skootle* case, Twitter brought suit in the Northern District of California against various defendants for their spamming activities on Twitter's service. One defendant, Garland Harris, who was a resident of Florida, brought a motion to dismiss, claiming lack of personal jurisdiction and improper venue. The court denied Harris's motion, finding that the forum selection clause in Twitter's terms of service applied. The court, however, specifically noted that it was not finding that forum selection clauses in "clickwrap" agreements are generally enforceable, but rather "only that on the allegations in this case, it is not unreasonable to enforce the clause here."

Fteja and *Skootle* highlight that potentially burdensome provisions in online agreements may be enforceable even as to consumers; in both cases, a consumer seeking to pursue or defend a claim against a social media platform provider was required to do so in the provider's forum. Both consumers and businesses need to be mindful of what they are agreeing to when signing up for online services.

Six states passed legislation regarding employers' access to employee/applicant social media accounts

California, Delaware, Illinois, Maryland, Michigan and New Jersey enacted legislation that prohibits an employer from requesting or requiring an employee or applicant to disclose a user name or password for his or her personal social media account.

Such legislation will likely become more prevalent in 2013; Texas has a similar proposed bill, and California has proposed a bill that would expand its current protections for private employees to also include public employees.

Facebook goes public

Facebook raised over $16 billion in its initial public offering, which was one of the most highly anticipated IPOs in recent history and the largest tech IPO in U.S. history. Facebook's peak share price during the first day of trading hit $45 per share, but with a rocky first few months fell to approximately $18— sparking shareholder lawsuits. By the end of 2012, however, Facebook had rebounded to over $26 per share.

Facebook's IPO was not only a big event for Facebook and its investors, but also for other social media services and technology startups generally. Many viewed, and continue to view, Facebook's success or failure as a bellwether for the viability of social media and technology startup valuations.

Employer-employee litigation over ownership of social media accounts

2012 saw the settlement of one case, and continued litigation in two other cases, all involving the ownership of business-related social media accounts maintained by current or former employees.

In the settled case of *PhoneDog LLC v. Noah Kravitz*, employer sued employee after the employee left the company but retained a Twitter account (and its 17,000 followers) that he had maintained while working for the employer. The terms of the settlement are confidential, but news reports indicated that the settlement allowed the employee to keep the account and its followers.

In two other pending cases, *Eagle v. Edcomm* and *Maremont v. Susan Fredman Design Group LTD*, social media accounts originally created by employees were later altered or used by the employer without the employees' consent.

These cases are reminders that, with the growing prevalence of business-related social media, employers need to create clear policies regarding the treatment of work-related social media accounts.

California's Attorney General went after companies whose mobile apps allegedly did not have adequate privacy policies

Starting in late October 2012, California's Attorney General gave notice to developers of approximately 100 mobile apps that they were in violation of California's Online Privacy Protection Act (OPPA), a law that, among other things, requires developers of mobile apps that collect personally identifiable information to "conspicuously post" a privacy policy. Then, in December 2012, California's Attorney General filed its first suit under OPPA against Delta, for failing to have a privacy policy that specifically mentioned one of its mobile apps and for failing to have a privacy policy that was sufficiently accessible to consumers of that app.

Privacy policies for mobile applications continue to become more important as the use of apps becomes more widespread. California's OPPA has led the charge, but other states and the federal government may follow. In September, for instance, Representative Ed Markey of Massachusetts introduced The Mobile Device Privacy Act in the U.S. House of Representatives, which in some ways would have similar notice requirements as California's OPPA.

Changes to Instagram's online terms of service and privacy policy created user backlash

In mid-December 2012, Instagram released an updated version of its online terms of service and privacy policy (collectively, "Terms"). The updated Terms would have allowed Instagram to use a user's likeness and photographs in advertisements without compensation. There was a strong backlash from users over the updated Terms, which ultimately led to Instagram apologizing to its users for the advertisement-related changes, and reverting to its previous language regarding advertisements.

Instagram's changes to its Terms, and subsequent reversal, are reminders of how monetizing social media services is often a difficult balancing act. Although social media services need to figure out how they can be profitable, they also need to pay attention to their users' concerns.

The defeat of the Stop Online Piracy Act (SOPA) and the PROTECT IP Act (PIPA)

Two bills, SOPA and PIPA—which were introduced in the U.S. House of Representatives and U.S. Senate, respectively, in late 2011—would have given additional tools to the U.S. Attorney General and intellectual property rights holders to combat online intellectual property infringement. A strong outcry, however, arose against the bills from various Internet, technology and social media companies. The opponents of the bills, who claimed the proposed legislation threatened free speech and innovation, engaged in various protests that included "blacking out" websites for a day. These protests ultimately resulted in the defeat of these bills in January 2012.

The opposition to and subsequent defeat of SOPA and PIPA demonstrated the power of Internet and social media services to shape the national debate and sway lawmakers. With prominent social media services such as Facebook, YouTube, Twitter, LinkedIn and Tumblr opposed to the bills, significant public and, ultimately, congressional opposition followed. Now that we've witnessed the power that these services wield when acting in unison, it will be interesting to see what issues unite them in the future.

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Labor Law §240

Labor Law §240

In prior issues of this publication, we have reported that the recent trend of the New York Court of Appeals, the State's highest Court, has been decidedly pro-plaintiff in cases involving the applicability of Labor Law §240(1). In this issue, we report on a case that departs from that trend and holds that a condominium corporation is not an "owner" within the meaning of the Labor Law §240(1). We also report on a decision from the Appellate Division, Second Department, which denies recovery under Labor Law §240(1) to a plaintiff who lost his balance and fell from a non-defective ladder. However, we also report on two pro-plaintiff Appellate Division decisions which some may view as disturbing. The first is a decision from the Appellate Division, First Department which imposes liability under the statute notwithstanding the fact that the two missing planks from the scaffold from which plaintiff fell may have been stolen. In the second, the Appellate Division, Third Department holds that the injured hydraulics specialist was not a "recalcitrant worker" within the meaning of Labor Law §240(1) notwithstanding the court's characterization of his actions as exhibiting "poor judgment."

CONDOMINIUM CORPORATION IS NOT A BUILDING "OWNER" SUBJECT TO LABOR LAW LIABILITY

Guryev v. Tomchinsky

Labor Law §240(1) generally imposes liability upon "owners, contractors and their agents." In *Guryev v. Tomchinsky*, 20 N.Y.3d 194, 957 N.Y.S.2d 677 (2012), the Court of Appeals held that a condominium corporation, unlike a cooperative corporation, is not an "owner" within the meaning of the Labor Law §240(1).

In *Guryev*, plaintiff was an employee of defendant YZ Remodeling, Inc. which was retained by defendant Tomchinsky to perform work in his condominium unit. Plaintiff allegedly was injured while using a nail gun when a nail ricocheted and struck him in the eye. He brought suit against Tomchinsky as well as the "condominium defendants," which included the condominium itself, its Board of Managers, and its Managing Agent. Plaintiff alleged a violation of New York Labor Law §241(6). [Like Labor Law §240(1), Labor Law §241(6) imposes a non-delegable duty on "owners and contractors," and the analysis of who is an "owner" under both statutes is the same.] The condominium defendants moved for summary judgment, which was denied by the trial court. The Appellate Division, Second Department reversed and granted summary judgment to the condominium defendants. The intermediate appellate court held that the condominium defendants did not have an interest in the property and did not assume the role of owner by contracting to have the work performed. Specifically, the court held that the condominium defendants "did not determine which contractors to hire, and were not in a position to control the renovation work or to insist that proper safety practices were followed."

The Court of Appeals granted plaintiff permission to appeal and, in a 4-2 decision, affirmed the grant of summary judgment to the condominium defendants. The Court noted plaintiff's argument that the condominium defendants are indeed owners within the meaning of the statute because the condominium owns the land beneath the building, and the board and managing agent are the condominium's agents. However, the Court stated that the plaintiff was injured in Tomchinsky's apartment, which was separate and apart from the real property beneath the building. As such, the Court held that Tomchinsky, and not the condominium, was the owner of the apartment and, therefore, the condominium defendants were not owners within the meaning of the Labor Law.

Likewise, the Court rejected plaintiff's alternative argument that the alteration agreement entered into by Tomchinsky and the Board established the Board's position as owner. While the agreement did give the Board an interest in making sure renovations were carried out with little or no inconvenience and/or damage to the building, other units or its common areas, it did not "vest the board with authority to determine which contractors to hire, control the renovation work or insist that proper safety practices be followed." The Court added that it has "insisted on some nexus between the non-contracting owner and the worker, whether by a lease agreement or grant of an easement, or other property interest . . . [and held that] ownership is a necessary condition although not a sufficient one for a non-contracting party's liability under section 241(6), and the condominium did not own the Tomchinsky's apartment."

Finally, the Court rejected plaintiff's argument - accepted by the dissent - that condominiums and cooperative corporations should be treated alike when it comes to the issue of ownership under the Labor Law. Here, the Court held that "whereas condominium apartments are owned by individual unit owners (here, the Tomchinskys), a cooperative corporation owns an entire building, including the apartments where individual tenant-shareholders reside."

The dissenting opinion, authored by Chief Judge Lippman, stated that the majority's conclusion "rips a gaping hole in the Labor Law's protective mantle."

FALL FROM NON-DEFECTIVE LADDER DOES NOT CREATE LABOR LAW LIABILITY UNDER ALL CIRCUMSTANCES

The general belief is that any fall from a ladder likely gives rise to potential liability under Labor Law §240(1). *Gaspar v. Pace University*, 101 A.D.3d 1073, 957 N.Y.S.2d 393 (2nd Dep't 2012) illustrates that such is not always the case.

In *Gaspar*, plaintiff was injured when he fell from a ladder on an asbestos abatement project. Prior to the accident, plaintiff's supervisor directed him to use a six-foot A-frame ladder to replace light bulbs in a decontamination area. Plaintiff inspected the ladder for stability prior to using it. While he worked, he wore a full face mask with a filter and respirator. As he was changing a light bulb, his face mask got caught on a cable hanging from the ceiling. In an attempt to dislodge the mask from the cable, plaintiff shook his head back and forth, during which time he lost his balance and fell from the ladder. Consequently, plaintiff commenced this action under Labor Law §240(1) and moved for summary judgment on liability. The defendants cross-moved to dismiss. The trial court denied plaintiff's motion and granted defendants' cross-motion.

The Appellate Division, Second Department affirmed. "Here, the defendants demonstrated that the ladder from which the injured plaintiff fell was not defective or inadequate and that the ladder did not otherwise fail to provide proper protection; rather, the injured plaintiff fell because he lost his balance."

The defendants' motion for summary judgment in the trial court was made by Ernesto O. Gimeno and Dawn C. DeSimone of McGaw, Alventosa & Zajac, AIG Staff Counsel in Jericho, New York. Plaintiff's appeal was successfully opposed by Ross P. Masler of the Appeals Unit at McGaw, Alventosa & Zajac.

The claims professional was James Joanos, Complex Director, AIG, PSU, New York, New York.

*** * ***

Liability under Labor Law §240(1) is absolute, and is imposed even if defendant exercises no control or supervision over a subcontractor performing a job on the property. New York Labor Law §240(1) is unique in the United States and there have been many calls for its repeal or modification. The following two decisions may be viewed by some as examples of cases which engender criticism of the statute and case law thereunder.

OWNER LIABLE FOR HIDDEN DEFECT IN SCAFFOLD CAUSED BY UNKNOWN PERSON

Susko v. 337 Greenwich LLC

In *Susko v. 337 Greenwich LLC*, 103 A.D.3d 434, ____ N.Y.S.2d ____ (1st Dep't 2013), plaintiff was injured when he fell from a scaffold. The device was constructed in such a manner that plywood sheeting was placed over planks on the scaffold. At the time of plaintiff's accident, there were two planks missing beneath the plywood.

In affirming summary judgment for plaintiff, the Appellate Division, First Department stated that defendant "had a nondelegable, statutory duty to ensure that the scaffold in use by plaintiff during the course of this construction project was an effective and stable safety device. Since preventing a worker from falling is a core objective of the statute, plaintiff established a violation of Section 240(1) as a matter of law."

The court rejected the defense that the planks were improperly removed, or possibly even stolen, by the employees of another contractor. The Appellate Division noted that defendant's principal testified that he was aware that other subcontractors on the site were moving and removing construction materials. Significantly, the court added that even if the removal of the planks were characterized as a "theft," this would "not convert this foreseeable event into a superseding intervening cause."

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