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MAY 2026

Business Litigation Report

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A TOOL-BASED FRAMEWORK:

How AI Platforms Fit Into Centuries Of Privilege Doctrine.

Artificial intelligence is rapidly reshaping the legal landscape, and the courts are taking notice. As one court recently observed, “[g]enerative artificial intelligence presents a new frontier in the ongoing dialogue between technology and the law.” *United States v. Heppner*, 2026 WL 436479, at *4 (S.D.N.Y. Feb. 17, 2026). That frontier, however, is not without boundaries. The growing integration of AI into litigation has forced “courts to confront difficult questions about how and to what extent longstanding protections apply when parties use AI to assist them in the litigation process.” *Morgan v. V2X, Inc.*, 2026 WL 864223, at *2 (D. Colo. Mar. 30, 2026). However, “AI’s novelty does not mean that its use is not subject to longstanding legal principles, such as those governing the attorney-client privilege and the work product doctrine.” *Heppner*, 2026 WL 436479, at *4.

The question, then, is not whether AI fits within existing privilege doctrine, but how. Some advocates argue that the doctrine should adapt to technology and that many practitioners treat AI tools as confidants, but as American University Professor Ira Robbins has noted, “ubiquity and intimacy are not the touchstones” of privilege. Ira P. Robbins, *Against an AI Privilege*, JOLT Dig., Harvard L. Sch. (Nov. 7, 2025). At least three courts confronting this new frontier in early 2026 have reached consistent conclusions about the governing standard: that the use of AI cannot extend privilege by casting AI as a lawyer *in its own right*, but AI use can be protected where attorneys and litigants wield it as a tool in service of otherwise privileged work. This piece examines the reasoning underlying the courts’ early guidance and explores the limitations on privilege set by this tool-based framework as AI becomes an increasingly common fixture in legal practice.

The Status Quo of Privilege Doctrine

Two foundational privileges govern the confidentiality of legal communications and litigation materials: the attorney-client privilege and the work product doctrine. Each operates under a distinct legal standard but they are related in purpose to protect distinct categories of information.

“The attorney-client privilege is the oldest of the privileges for confidential communications known to the common law.” *Upjohn Co. v. United States*, 449 U.S. 383, 389 (1981). “Its purpose is to encourage full and frank communication between attorneys and their clients” and “rests on the need for the advocate and counselor to know all that relates to the client’s reasons for seeking representation if the professional mission is to be carried out.” *Id.* To that end, the privilege attaches to, and protects from disclosure, “communications (1) between a client and his or her attorney (2) that are intended to be, and in fact were, kept confidential (3) for the purpose of obtaining or providing legal advice.” *Heppner*, 2026 WL 436479, at *2.

“Related to but distinct from the attorney-client privilege, the work product doctrine, [a]t its core[,] ... shelters the mental processes of the attorney, providing a privileged area within which he can analyze and prepare his client’s case.” *Id.* at *3 (internal citation omitted). Although the doctrine may in some circumstances apply to materials generated by non-lawyers, courts have stressed that its “availability in reference to materials in the possession of a client depends upon the existence of

FIRM HIGHLIGHTS

Quinn Emanuel Named Vault’s No. 1 Firm for General Commercial Litigation

When associates across the country were asked to name the strongest firm in General Commercial Litigation, they chose Quinn Emanuel. For the seventh year running, *Vault* has ranked us #1 in General Commercial Litigation in its Top Law Firms by Practice Area rankings.

New York Office Welcomes New Partner Minji Reem

Shareholder Activism and Private Funds litigator Minji Reem has joined Quinn Emanuel as a Partner based in the New York office. Minji focuses on shareholder activism, corporate governance, private funds, securities matters, and internal investigations. At her previous firm, McDermott Will & Schulte, Minji represented Politan Capital Management in litigation against Masimo Corporation and venBio Select Advisor in its successful board control campaign at Immunomedics. She regularly counsels investment managers through fund and partnership disputes, including a recent complete defense victory in an arbitration seeking over \$1 billion in claimed damages.

Partner Nicholas LoCastro Recognized as “Rising Star”

The Life Sciences Patent Network (LSPN) has awarded New York Partner Nicholas LoCastro Rising Star of the Year for 2026. Nick’s practice focuses on patent litigation involving a wide array of pharmaceutical technologies, including drug formulations and method of treatment claims.



a real, rather than speculative, concern that the thought processes of [the client's] counsel in relation to pending or anticipated litigation would be exposed." *Id.* (internal citation omitted). That distinction matters: the doctrine is not a general shield against disclosure of litigation-related documents, but a targeted protection for the strategic and analytical work by the attorney.

Together, these two doctrines form the core of the confidentiality framework into which AI has now arrived and into which courts are beginning to define its place.

United States v. Heppner (February 17, 2026)

The Southern District of New York confronted “a question of first impression nationwide: whether, when a user communicates with a publicly available AI platform in connection with a pending criminal investigation, are the AI user’s communications protected by attorney-client privilege or the work product doctrine.” *Heppner*, 2026 WL 436479, at *1. The court’s answer was an unambiguous no, and its reasoning made clear that the use of an AI tool standing alone does not qualify as attorney involvement sufficient to be protected.

In the case, defendant Bradley Heppner received a grand jury subpoena and learned he was a target of an investigation alleging that he defrauded investors. Thereafter, Heppner turned to the publicly available AI platform Claude, which he used, *without any direction from his attorneys*, to prepare “reports that outlined defense strategy” and “that outlined what he might argue with respect to the facts and the law.” *Id.* When FBI agents executed a search warrant at Heppner’s home, they seized those documents. Heppner’s counsel argued they were privileged because Heppner had input information learned from counsel, created the documents to prepare for conversations with counsel, and later shared them with counsel, even though counsel had never directed him to use the AI platform. The court disagreed.

The court held that all three elements of the attorney-client privilege were lacking. The first and most fundamental deficiency was the simplest: *Claude is not an attorney*. “[T]hat alone disposes of Heppner’s claim of privilege.” *Id.* at *2. This framing reflects the court’s core skepticism: the privilege exists to protect the attorney-client relationship, and there is no framing that can qualify an AI platform as the requisite attorney in that relationship.

The court's skepticism continued with the second element, confidentiality. The court emphasized not only that Heppner communicated with a third-party in his very use of the AI platform, but also that Claude's written privacy policy required users to consent to their inputs being collected to "train" Claude and that Claude has the right to disclose such data "to a host of third parties." *Id.* (internal citation omitted). On those facts, the court held, "Heppner could have had no reasonable expectation of confidentiality in his communications with Claude." *Id.* (internal citation omitted). According to the court, the voluntary disclosure of information to a platform operating under such a policy was fundamentally incompatible with the confidentiality that privilege requires.

Third, and most notable for attorneys and their clients moving forward, Heppner had not used Claude for the purpose of obtaining legal advice, nor had he been directed to do so by counsel. Although Heppner's attorneys argued that he had "communicated with Claude for the express purpose of talking to counsel," his counsel also "conceded, Heppner did not do so at the suggestion or direction of counsel." *Id.* at *3 (internal citations omitted). That concession was key to the court's ruling. The attorney-client privilege does not attach simply because a client later shares the documents with an attorney; the communication must be made for the purpose of obtaining legal advice, and the court held that purpose was absent here.

The court's work product protection analysis followed similar logic. The critical fact was that Heppner prepared the documents of his own volition, rather than by or at the direction of counsel. As a result, he "was not acting as his counsel's agent when he communicated with Claude." *Id.* Absent that direction forming an agency relationship, the documents could not reflect counsel's mental processes, which work product doctrine exists to protect. "Because the AI Documents were not prepared at the behest of counsel and did not disclose counsel's strategy, they do not merit protection as work product." *Id.* at *4.

As one of the first courts addressing this new frontier of privilege doctrine, the Southern District of New York in *Heppner* showed its obvious skepticism toward the broader proposition that AI-assisted communications might warrant privilege protection in their own right. Grounding its analysis firmly in existing privilege doctrine, the court was very clear: privilege belongs to the attorney-client relationship; the work product doctrine protects the attorney's mental process and strategy. Use of an AI tool, the court believes, does not insert a lawyer into the equation standing alone, and cannot therefore establish protection.

Warner v. Gilbarco (February 10, 2026)

Just one week before Heppner was decided, the Eastern District of Michigan reached a different result on very similar facts. *Warner v. Gilbarco*, 2026 WL 373043, at *4 (E.D. Mich. Feb. 10, 2026). Where as Heppner denied protection because no attorney was in the picture, Warner granted work product protection for precisely the opposite reason: the *pro se* litigant was the attorney.

This time in a civil case, *pro se* plaintiff Sohyon Warner had used ChatGPT in the course of litigation to prepare her work product.. Defendants moved to compel production of all documents related to her use of third-party AI tools in connection with the lawsuit, arguing that Warner had waived work product protection by using the platform to prepare. *Id.* at *4.



The court held that Warner’s AI-generated materials were protected by the work product doctrine, reasoning that ChatGPT was merely a tool in service of Warner’s own litigation preparation. Acting as her own attorney *pro se*, Warner’s use of the AI platform reflected her internal drafting and thought processes, which were prepared in anticipation of litigation and are squarely protected as attorney work product. Unlike in *Heppner*, the AI did not generate the strategy; it assisted the person who did.

The court further held that Warner had not waived work product protection by using ChatGPT. Anchoring its analysis in the core principle that work product waiver requires disclosure to an adversary, or disclosure in a manner likely to reach an adversary’s hands, the court found that Warner’s use of a third-party AI platform did not meet that standard. *Id.* The court was notably unimpressed by the defendants’ waiver theory, warning that accepting it “would nullify work-product protection in nearly every modern drafting environment.” *Id.*

That framing provided important insight into the court’s view of AI as functionally the same as the use of any other drafting aid: a tool. Where as *Heppner* used that characterization to deny protection, because the tool was operating in the absence of

any attorney, Warner used it to extend protection, because the tool was assisting the pro se litigant herself. The thrust of the two decisions is the same: the attorney-client privilege and the work product doctrine attach to the human legal mind at work, not to the platform facilitating that work.

Morgan v. V2X, Inc. (March 30, 2026)

The very next month, the District of Colorado picked up where the Eastern District of Michigan left off. Citing Warner with approval, the court in *Morgan v. V2X, Inc.* reaffirmed that a pro se civil litigant can assert work product protection in connection with AI use. 2026 WL 864223, at *4-5 (D. Colo. Mar. 30, 2026).

In *Morgan*, the defendants moved to compel pro se plaintiff Archie Morgan to disclose the specific AI platform he had been using in connection with the litigation, and simultaneously sought to amend the existing protective order to restrict how confidential information could be used with AI tools. *Id.* at *2. Morgan did not oppose amending the protective order in principle, but resisted disclosing his AI tool of choice, arguing that a litigant’s selection of litigation support tools falls squarely within the work product doctrine. *Id.*

The court agreed with *Warner* that work product protection applies to a pro se litigant's use of AI, rooting its analysis in Rule 26(b)(3), which protects "documents and tangible things that are prepared in anticipation of litigation or for trial by or for another party or its representative." *Id.* at *3 (citing Fed. R. Civ. Pro. 26(b)(3)(A)). The court observed that the Advisory Committee's 1970 Amendments to the Rule were specifically designed to extend that protection beyond attorneys' work product to materials prepared by or for a party and that courts have broadly interpreted the Rule to shield not just litigation preparation materials, but also the mental impressions, opinions, and theories of the parties themselves. *Id.* at *3.

The court held that the fact that "AI systems like ChatGPT, Claude, Gemini, and others widely available to the public, collect user data for training and other purposes" does not "eliminate all expectations of privacy or automatically waive protections." *Id.* at *4. Drawing on *Warner's* waiver reasoning, the court reiterated that even though AI use technically discloses information to a third party, it is highly unlikely that information would reach an adversary's hands absent legal process to compel it, and that AI interactions therefore do not automatically compromise work product protection. *Id.*

Notably, the court contextualized its analysis in the privacy expectations that Fourth Amendment doctrine has recognized in other third-party contexts, emphasizing that routing information through a third-party system does not forfeit all privacy. The court placed particular weight on the distinctive nature of modern AI platforms, which are "specifically designed and trained to engage," "invite candid and significant disclosure of information, including sensitive information," and "simulate empathy, foster trust, and interact in a way that feels genuine and intimate." *Id.* at *5. That intimacy, the court suggested, counsels against treating AI interactions as the kind of voluntary third-party disclosure that strips away legal protection.

Morgan represents the fullest judicial articulation to date of the tool-based framework. Across all elements of its analysis, the court's reasoning returned to the same premise: AI is a tool in service of the litigant's mind, and protection follows the mind, not the tool.

Tool or Privilege Holder?

Taken together, *Heppner*, *Warner*, and *Morgan* establish a coherent—though still developing—framework for analyzing privilege claims in the age of AI. At its core, the framework is simple: AI is a tool, not a lawyer, and protection follows the legal mind wielding it, not the platform through which it works.

Professor Ira Robbins has argued, "[t]he relevant duty-bearer is the lawyer—the human professional who owes fiduciary duties, is subject to discipline, and exercises legal judgment. AI systems cannot be admitted to the bar; they cannot form fiduciary relationships; and they cannot be sanctioned by courts or regulators the way human professionals can." Ira P. Robbins, *Against an AI Privilege*, JOLT Dig., Harvard L. Sch. (Nov. 7, 2025). And although this may be the case, AI systems can certainly aid the relevant duty-bearer.

The district court in *Warner* stated the premise clearly, explaining that "ChatGPT (and other generative AI programs) are tools, not persons, even if they may have administrators somewhere in the background." *Warner*, 2026 WL 373043, at *4. *Heppner* and *Morgan* affirmed that characterization. None of the three district courts to address this issue showed any interest in treating AI as establishing a privileged relationship in its own right. The question in each case was not what the AI was doing, but who was directing it, and whether that person stood in a legally cognizable relationship to an attorney.

In fact, even *Heppner*, which ultimately denied protection, reflected a similar line of thinking, theorizing that "[h]ad counsel directed Heppner to use Claude, Claude might arguably be said to have functioned in a manner akin to a highly trained professional who may act as a lawyer's agent within the protection of the attorney-client privilege." *Heppner*, 2026 WL 436479, at *3.

Confidentiality Concerns or Waiver of Privilege?

The tool-based framework resolves whether AI-assisted materials are privileged, but it does not resolve the concerns surrounding the confidential information fed into the tool to produce the privileged material. *Morgan* made clear that these are distinct questions, and that the answer to the first does not settle the second.

Even as the district court extended work product protection to *Morgan's* AI-generated litigation materials, it acknowledged that the risks of uploading confidential data to mainstream AI platforms could not be ignored. The defendant had raised legitimate concerns that its confidential information, including trade secrets and personnel files, was being entered into AI platforms, which collect and store user inputs and may disclose them to third parties. The court agreed that the defendant had a right to know where that data was going, and ordered *Morgan* to disclose the name of his AI tool so the defendant could assess whether confidential information had been compromised. *Morgan*, 2026 WL 864223, at *5.

To address the underlying risk going forward, the court crafted what appears to be the first AI-specific provision in a federal protective order of its kind—and perhaps a template for future litigation—prohibiting the submission of confidential information into any AI platform unless the provider is contractually barred from using inputs to train its model or disclosing them to third parties. *Id.* at *7. The court was candid that this requirement, as a practical matter, would bar the use of most mainstream AI tools with confidential discovery materials, and cautioned parties against over-designation of information as confidential in light of that burden.

Morgan confirms that work product protection and confidentiality protection are not the same shield. A litigant's mental impressions may be protected from compelled disclosure to an adversary, but that protection does not permit feeding sensitive information into a platform that may retain, analyze, or redistribute it.

Guidance Of These Early Cases

Ultimately, these three decisions reflect a confirmation of existing privilege doctrine in a new frontier. Courts have long extended attorney-client privilege and work product protection beyond the attorney alone, to clients acting on counsel's direction, to agents functioning as necessary extensions of the legal relationship, and to parties preparing their own litigation materials in anticipation of trial. AI, under the tool-based framework, fits comfortably within that doctrine as another instrument through which attorneys and litigants do the work that privilege has always protected.

The three decisions together offer attorneys and litigants reasonably clear guidance on how to preserve privilege and work product protection when using AI in litigation. Most importantly, attorneys should be prepared, if challenged, to demonstrate that AI was used as a tool in service of their legal work. Attorneys should direct, instruct, and supervise their clients' use of AI tools rather than leaving clients to use them independently. Attorneys should document the purpose of AI use, ensuring that the record reflects that AI-generated materials were prepared by themselves or their clients in anticipation of litigation and in furtherance of counsel's legal strategy, not merely as a personal exercise.

NOTED WITH INTEREST

The AI Arbitrator: How the AAA Is Reshaping Dispute Resolution



What Is the AI Arbitrator?

The American Arbitration Association (“AAA”) has recently introduced the “AI Arbitrator,” which it touts as a fast, cost-effective, and trusted dispute resolution tool. Using groundbreaking technology, the AI Arbitrator applies historical decision-making and a standardized rulebook to the facts of a new case, generating an outcome that a human arbitrator then reviews for reasoning and accuracy. Currently available for two-party, documents-only construction disputes, the tool is expected to expand to other case types later in 2026. As of March 2026, however, it had not yet issued its first award—in part because both parties must either agree in advance or mutually consent after a dispute arises to use it.

The AAA claims the tool delivers significant time and cost savings compared to traditional documents-only arbitration, with time savings starting at 20–25% and cost savings at 35–45%. Beyond efficiency, the AAA emphasizes the tool’s commitment to “the most important goal of arbitration, which is fairness and process.” American Arbitration Association, [The Human Element, AI Arbitrator Ep. 3](#), . By applying legal reasoning derived from past outcomes to new factual disputes, the AI Arbitrator takes an analytical, almost mathematical approach, which adds a degree of predictability and consistency to outcomes.

But is predictability worth the trade-off? Many in the field have expressed skepticism, arguing that arbitration involves more than mapping law to facts on paper. Weighing the relevance of evidence, judging witness credibility, and arriving at a truly



just outcome are tasks that require a uniquely human form of judgment that cannot easily be programmed. As the AAA looks to expand use of the AI Arbitrator beyond documents-only disputes, this tension will need to be carefully addressed.

What the AI Arbitrator Is Not

Importantly, the human element has not been removed from the process. The AI Arbitrator is designed as an efficiency tool, not a replacement for human judgment, and a human arbitrator remains in the loop at every key stage.

As the AAA acknowledges: “No one is going to trust an AI arbitrator where you put your inputs in, press a button, and two seconds later it gives you the answer.” American Arbitration Association, [The Human Element, AI Arbitrator Ep. 3](#), . Every AI Arbitrator case is assigned a human AAA arbitrator who validates the AI Arbitrator’s outputs and certifies the final result. The process is notably transparent, and perhaps even more transparent than typical AAA arbitration. After parties submit their materials, the AI Arbitrator generates a case summary, which the parties are then invited to review and provide

feedback on. The human arbitrator subsequently reviews both the AI-generated summaries and the parties’ feedback before confirming the structure of the award. This layered oversight ensures accuracy and fairness before any award becomes final.

What’s Next

The AAA has also introduced the Resolution Simulator, which is a companion tool that uses the same analytical reasoning to generate a non-binding, simulated outcome based on a single party’s submission. The AAA hopes that giving parties a low-stakes opportunity to see the tool in action will help ease skepticism before committing to it in a live dispute. Whether use of the AI Arbitrator takes off remains to be seen, as fundamental questions linger, including whether parties will begin building clauses into their contracts specifying that disputes must be decided by a human arbitrator or how the AI Arbitrator will be programmed to take factors like witness credibility into account. How the legal community navigates these issues will likely determine how broadly AI-assisted arbitration is embraced in the years ahead.



PRACTICE AREA UPDATES

Mergers & Acquisitions Update:

Delaware Supreme Court Applies Plain Language of Merger Agreement to Reverse \$300 Million Damages Award

Delaware is a frequent venue for mergers-and-acquisitions related litigation and has a “contractarian” reputation, meaning Delaware courts hold parties to the language of their agreements. This reputation was further cemented this January by the Delaware Supreme Court’s decision in *Johnson & Johnson v. Fortis Advisors LLC*, 2026 WL 89452 (Del. Jan. 12, 2026), which relied on the plain language of a merger agreement to reverse a lower court’s award of \$300 million in damages.

Background

Johnson & Johnson v. Fortis Advisors LLC arose out of an earnout dispute after Johnson & Johnson (“J&J”), a global healthcare company, acquired Auris, a startup medical robotics company.

J&J’s acquisition was prompted by the rise of robotic surgery, which posed an “existential threat” to J&J’s surgical instrument business. *Id.* at *2. To compete in the robotic surgery market, J&J acquired Auris, which had developed a versatile operating-room surgical robot called iPlatform. *Id.* at *2-3, 5. The resulting merger agreement included \$3.4 billion in upfront cash plus up to \$2.35 billion in earnout payments tied to post-closing milestones, many of which were triggered by regulatory approvals for Auris’s robotic platforms. *Id.* at *5.

The first and most valuable milestone (“Milestone 1”) promised \$400 million if iPlatform obtained “510(k)” clearance for specified surgical procedures by the end of 2021. *Id.* at *6. The 510(k) clearance pathway is an FDA regulatory mechanism under which a manufacturer seeks clearance by demonstrating substantial equivalence to a legally marketed predicate device. *Id.* at *3-4. It is historically the fastest and least burdensome path to market and significantly less burdensome than De



Novo classification, the other principal pathway to market. *Id.* To protect the earnouts, the Merger Agreement required J&J to use “commercially reasonable efforts” consistent with its usual practice for “priority medical device products,” and expressly prohibited J&J from taking any action with the intent to avoid earnout payments. *Id.* at *7.

After closing, J&J’s treatment of iPlatform quickly diverged from its contractual obligations. Rather than elevating iPlatform as a priority device, J&J pitted it against J&J’s own robotic surgery device program in an internal competition, merging the two programs in what the Court of Chancery called a “calamity of excess and redundancy.” *Id.* at *7-9. J&J also abandoned Auris’s milestone-oriented regulatory strategy, and restructured its employee incentive program so that it no longer rewarded achievement of the contractual milestones. *Id.* at *9-10. A further complication arose in August 2019, when the FDA informed J&J that first-generation robotic surgery devices like iPlatform would no longer be eligible for the 510(k) pathway and would instead require more burdensome De Novo clearance. *Id.* at *10. J&J used this shift to write down the value of all milestones to zero and it paid none of the \$2.35 billion in earnouts. *Id.*

Auris’s former stockholders sued, and the Delaware Court of Chancery found that J&J had breached its commercially reasonable efforts obligations and acted intentionally to avoid the earnouts. *Id.* at *12. As to Milestone 1 specifically, the court held that because the Merger Agreement was silent on what would happen if the 510(k) pathway became unavailable, the implied covenant required J&J to pursue De Novo clearance as the functional equivalent of the 510(k) clearance specified in the contract. *Id.* at *12-13. Because J&J did not do so, the court used a probability-weighted approach to award \$300 million for J&J’s failure to pay the portion of the earnout related to Milestone 1. *Id.* at *13.

The Delaware Supreme Court’s Reversal

On appeal, the Delaware Supreme Court reversed the Milestone 1 damages award, holding the Court of Chancery had erred as a matter of law in invoking the implied covenant. The court reaffirmed that the implied covenant functions as a limited “gap-filler” that applies only where there is genuine contractual silence about a truly unanticipated development, *Id.* at *14, and it may not be used as an “equitable remedy for rebalancing economic interests after events that could have been anticipated, but were not,” *Id.* at *21.

Applying these principles, the court concluded the Merger Agreement contained no genuine gap to fill. *Id.* at *18. It reasoned that the Merger Agreement did not speak in general terms about “regulatory approval”—instead, it conditioned each regulatory earnout, repeatedly and expressly, on achieving 510(k) clearance. *Id.* The parties had also anchored their milestones to this specific pathway exclusively, providing for neither alternative regulatory pathways nor adjustment if the FDA closed the 510(k) route. *Id.* at *19. Additionally, the court noted the FDA’s shift was not unforeseeable, pointing out that both J&J and Auris were sophisticated actors in a heavily regulated field, and that the FDA had specifically flagged before signing that the 510(k) pathway “might be unavailable” for iPlatform given its novelty and publicly announced in late 2018 that it was modernizing the 510(k) program. *Id.* at *19-20. As the court put it, a sophisticated acquiror and serial device innovator could “reasonably foresee that a first-generation RASD with new features may be steered away from 510(k), even if 510(k) remained the likeliest route at signing.” *Id.* at *19. Accordingly, the court held the implied covenant did not require J&J to pursue De Novo clearance in lieu of the 510(k) pathway specified in the Merger Agreement and reversed the \$300 million damages award relating to Milestone 1. *Id.*

Key Takeaway

For parties negotiating earnout provisions tied to regulatory milestones, *Johnson & Johnson v. Fortis Advisors* is a sharp reminder that Delaware courts will hold sophisticated parties to the precise language they negotiated and will not use the implied covenant to supply protections that could have been—but were not—included in the agreement.

Real Estate Update:



Commercial Real Estate Distress

Commercial real estate markets continue to experience significant distress as office building values remain depressed and lenders confront mounting defaults. With Commercial Mortgage Backed Securities (CMBS) office delinquency rates reaching 12.34% as of January 2026—surpassing 2008 financial crisis levels by 1.6%—and approximately \$875 billion in commercial real estate loans maturing in 2026, the industry faces a perfect storm requiring innovative legal solutions and careful navigation of evolving lender liability theories.

Market Fundamentals

The current crisis differs from prior downturns because it stems from structural rather than cyclical factors. Remote and hybrid work have permanently altered space utilization, driving the national office vacancy rate to 20.5% through Q4 2025, per Cushman & Wakefield. Office property sales totaled just \$45.4 billion in the first nine months of 2025—less than half the \$102.6 billion recorded in 2019. Total distressed CRE volume

reached \$126.6 billion in Q3 2025, up 18% year-over-year, with office properties accounting for the largest share, according to Morgan Stanley Capital International (MSCI).

Early stabilization signals are emerging. Sublease availability has declined roughly 20% from its Q1 2024 peak, and new construction starts have fallen to 25-year lows. Whether these trends signal a genuine inflection or a temporary pause remains a central factual dispute in workout negotiations, particularly given the uneven recovery across markets.

Evolving Workout Strategies

Traditional foreclosure activity, while rising—filings increased 14% in 2025—remains well below pre-pandemic levels, down 25% from 2019, as lenders continue to pivot toward negotiated workouts. The overall CMBS delinquency rate of 7.47% is nearly six times the bank loan distress rate of approximately 1.29%, reflecting that securitized debt is recognizing losses faster while traditional lenders continue extending and modifying loans.

Notably, only an estimated 50–55% of the \$957 billion in CRE loans that matured in 2025 were paid off; the remainder received extensions, swelling the 2026 maturity calendar and compounding future refinancing pressure.

Lenders are increasingly entering special servicing arrangements rather than pursuing immediate foreclosure. The office CMBS special servicing rate reached 17.11% in January 2026, up from approximately 2.85% in late 2020, according to Trepp. Creative right-sizing structures that tie debt service to cash flow are also emerging. However, lenders are now increasingly unwilling to grant further extensions without meaningful borrower concessions, signaling a practical end to the “extend and pretend” era for many assets.

Lender Liability and Guarantor Exposure

Lender liability theories continue to face judicial skepticism. Courts granted summary judgment for lenders in a string of implied covenant of good faith and fair dealing cases through 2023 and 2024, as noted in the *Chambers Real Estate Litigation 2025* guide. In *Beskroner v. KORE Capital Corp. (In re Moon Group, Inc.)*, 658 B.R. 92 (D. Del. 2024), the Delaware District Court affirmed dismissal of a lender liability action on the grounds that Maryland law provides no independent cause of action for breach of implied covenant separate from breach of contract.

As properties fall below loan balances, personal guarantors have become lenders’ primary recovery mechanism. Many commercial loans are held by special purpose entities with no assets beyond the mortgaged property, leaving guarantors exposed. Courts are also scrutinizing asset protection strategies, including challenges to foreign trust structures and corporate veil-piercing in connection with guarantor pursuit. Bad boy guaranty provisions—non-recourse carve-outs triggered by bankruptcy filings or lender misrepresentations—are generating significant litigation as guarantors face personal liability in a collapsed market.

Outlook and Strategic Considerations

The \$875 billion in 2026 maturities is projected to grow to a peak of approximately \$1.26 trillion in 2027, keeping refinancing pressure elevated well beyond the current cycle. Some analysts view 2026 as the likely peak of CMBS distress, with gradual normalization beginning in 2027, although significant unresolved maturities and ongoing maturity defaults could cause continued volatility. Private credit firms have stepped in where traditional lenders have pulled back, offering flexible capital for transitional assets and distressed repositionings, often with ownership-oriented structures.

For lenders, the calculus increasingly favors workout over foreclosure in markets with limited buyer interest, but only where borrowers can demonstrate a credible path to stabilization. For borrowers, the window for extension-only strategies has largely closed; new equity, loan restructuring, or a negotiated exit are the realistic options. For legal counsel, effective representation demands fluency across real estate law, bankruptcy, and commercial litigation, with particular focus on guaranty enforcement, special servicing dynamics, and the evolving contours of lender liability in a market where traditional assumptions no longer hold.

VICTORIES

Quinn Emanuel Secures Resounding Victory for Qualcomm as Consumers' Association Which? Withdraws £480 Million (\$650 Million) Class Action Post-Trial

Quinn Emanuel secured a decisive victory for long-time client Qualcomm after the Class Representative moved to withdraw in its entirety a £480 million (\$650 million) class action before the United Kingdom (“UK”) Competition Appeal Tribunal (the “Tribunal”) following trial. In accordance with the agreement for withdrawal concluded by the parties, Qualcomm will make no payment to the Class Representative or the proposed class, and approval of the withdrawal application will terminate the claim against Qualcomm.

On 25 February 2021, the UK Consumers' Association Which?, acting as the Class Representative for an estimated 29 million UK consumers who had purchased certain Apple and Samsung mobile phones supporting the Long-Term Evolution (“LTE”) 4G wireless standard, filed an opt-out collective action in the form of a standalone damages claim under section 47B of the UK Competition Act 1998.

The claim contained wide-ranging allegations that morphed several times during the proceedings—including during the trial—and targeted the very heart of Qualcomm's business, in particular its long-standing chipset supply and licensing practices, as well as the level of royalties paid by mobile phone makers for practising Qualcomm's cellular patents. In essence, Which? alleged that Qualcomm's chipset supply and licensing practices enabled Qualcomm to leverage a purported dominant position in the supply of certain types of baseband chipsets to extract supra-competitive royalties in relation to the sale of certain Apple and Samsung LTE-enabled mobile phones in the UK, which in turn were passed on to consumers, thereby infringing Section 18 of the UK Competition Act 1998 and, until 31 December 2020, Article 102 of the Treaty on the Functioning of the European Union.

Following a protracted battle spanning five years, including a gargantuan five-week trial in autumn 2025, on 17 February 2026, the Class Representative announced its decision to abandon the proceedings in their entirety, pending approval by the Tribunal. The Class Representative also issued a public statement asserting that, “based on the evidence and the arguments at trial, the Tribunal will find that: (a) Qualcomm did not coerce Apple, Apple's Chipset Manufacturers (“CMs”), or Samsung to sign any patent licences or chipset agreements; (b) Qualcomm did not leverage its position as a chipset supplier to coerce Apple, Apple's CMs, or Samsung to agree to any licensing terms; and (c) Qualcomm's licensing and chipset practices did not infringe competition laws, did not result in inflated royalties, and did not lead to an increase in prices consumers paid for their mobile phones.”

Quinn Emanuel has been advising Qualcomm since the inception of the case, guiding the strategy and shaping the substance of Qualcomm's defence throughout, including during the five-week trial.

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