

SUPREME COURT OF THE STATE OF NEW YORK  
COUNTY OF NEW YORK : IAS PART 56

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CONNECTU, INC., HOWARD WINKLEVOSS,  
CAMERON WINKLEVOSS, TYLER  
WINKLEVOSS, and DIVYA NARENDRA

*Petitioners,*

Index No: 602082/2008

-against-

**DECISION AND ORDER**

QUINN EMANUEL URQUHART OLIVER  
& HEDGES,

*Respondent.*

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**RICHARD B. LOWE III, J:**

In Motion Sequence numbers 002, 003, and 004, Petitioners Howard Winklevoss, Cameron Winklevoss, Tyler Winklevoss, and Divya Narendra (“Petitioners”) move pursuant to 9 USC § 7 and/or CPLR § 2308(b), to compel non-parties Facebook, Inc. (“Facebook”), Houlihan, Lokey, Howard & Zukin (“Houlihan”), and Microsoft Corporation (“Microsoft”) to comply with five separate subpoenas issued by an arbitration panel constituted to resolve Petitioners dispute with their former counsel, Quinn Emanuel Urquhart Oliver & Hedges, LLP (“Quinn Emanuel”). Quinn Emanuel previously represented Petitioners in a now settled action against Facebook. Petitioners also move, pursuant to CPLR § 1003, to remove ConnectU, Inc. (“ConnectU”) as a party to this proceeding.

**BACKGROUND**

On April 24, 2008, Quinn Emanuel initiated an arbitration against Petitioners for unpaid legal fees. On July 16, 2008, Petitioners and ConnectU commenced a special proceeding in this Court seeking a stay of the arbitration. On September 12, 2008, this Court denied the stay and

ordered the parties to commence arbitration proceedings consistent with the parties' engagement letter (*Connectu, Inc. v Quinn Emanuel Urquhart Oliver & Hedges, LLP*, 2008 NY Slip Op 52042U, at \* 2, 873 NYS2d 510 [Sup Ct, NY County Sept 12, 2008]). Petitioners have asserted malpractice counterclaims against Quinn Emanuel in the arbitration.

Petitioners are the former shareholders of ConnectU. In 2004, ConnectU initiated litigation in the District of Massachusetts against Facebook and its founders, including Facebook CEO Mark Zuckerberg ("Zuckerberg"), asserting copyright infringement, misappropriation of trade secrets, breach of contract, and fraud (the "Massachusetts litigation"). The well-publicized Massachusetts litigation claimed, *inter alia*, that Zuckerberg stole the idea for Facebook and its underlying intellectual property from Petitioners while they, along with Zuckerberg, were students at Harvard University.

On September 17, 2007, while the Massachusetts litigation was still in the discovery stage, Petitioners entered into an engagement letter with Quinn Emanuel. The engagement letter provided that Quinn Emanuel would represent Petitioners in the Massachusetts litigation against Facebook in exchange for 20 percent of the "value of any settlement or judgment in the Action" (Oct 1, 2009 Affirmation of Sean O'Shea ["10/01/09 O'Shea Aff"] Ex A, at 2). The engagement letter further provided that:

Any dispute regarding or arising out of our representation will be resolved by binding arbitration under the Commercial Rules of the American Arbitration Association ("AAA") before three arbitrators appointed from AAA's Large Complex Commercial Case Panel. The arbitrators will have the authority to determine whether the dispute is arbitrable. The arbitration will be governed by both the procedural and substantive provisions of the Federal Arbitration Act. The arbitration will be held in the County of New York.

(10/01/09 O'Shea Aff Ex A, at 6).

On February 22-23, 2008, Petitioners, represented by Quinn Emanuel, and Facebook engaged in mediation, during which a handwritten document titled “Term Sheet and Settlement Agreement” was signed. The Term Sheet contemplates that the parties would relinquish their claims against each other provided that Facebook transferred to Petitioners a certain amount of cash and a certain number of shares of Facebook common stock (the “Settlement”). Facebook is a privately held Delaware corporation and its stock is not publicly traded.

Petitioners explain that they signed the agreement under the mistaken belief that the value of Facebook’s common stock was approximately \$35.90 per share. “Petitioners’ belief was founded on widely circulated media reports rumoring that Microsoft had invested \$240 million in Facebook based on a \$15 billion valuation of Facebook” (10/01/09 O’Shea Aff Ex A, ¶ 12).

On March 26, 2008, while Petitioners and Facebook were finalizing documents related to the proposed settlement, Petitioners learned that a recent valuation of Facebook’s common stock was \$8.88 per share. Petitioners explain that Facebook performed this valuation in connection with its required filings under Internal Revenue Code provision 26 USC § 409A (“409A”). Subsequently, Petitioners learned that Facebook had filed documents with the State of California on February 25, 2008 averring that the value of its common stock was \$7.75 per share as of February 8, 2008 (*see* 10/01/09 O’Shea Aff Ex B).

Petitioners explain that after they brought the other, much lower Facebook stock valuations to Quinn Emanuel’s attention, Quinn Emanuel refused to support their efforts to challenge the Settlement. The relationship between Petitioners and Quinn Emanuel formally terminated on or about April 21, 2008. Thereafter, Petitioners obtained new counsel.

Based on the information concerning the lower Facebook stock valuations, Petitioners

maintain that the handwritten Term Sheet signed at the mediation was fraudulently induced, is unenforceable, and that they would not have signed such a document had they known the true value of Facebook's common stock at the time of the mediation (10/01/09 O'Shea Aff ¶ 15). After learning of Petitioners' position, Facebook filed a motion before the Northern District of California to enforce the Settlement against ConnectU and the Petitioners. Petitioners opposed the motion, moved for an evidentiary hearing and sought discovery from Facebook in anticipation of such a hearing.

Facebook explains that the discovery requests served on Facebook during the pendency of the motion to enforce the Settlement sought valuation information nearly identical to that sought by the subpoenas at issue here.<sup>1</sup> The Northern District of California denied the motion for an evidentiary hearing, noting that the requested valuation documents were not relevant to the dispute or the enforcement of the Settlement among Facebook and Petitioners. On June 25, 2008, the Northern District of California issued an order granting Facebook's motion to enforce the Settlement, holding that ConnectU and Petitioners failed to tender sufficient evidence of fraud (Bach Aff Ex B). The Northern District of California entered judgment enforcing the Settlement on July 2, 2008 (*see* Bach Aff Ex C at 1).

On April 24, 2008, Quinn Emanuel initiated the arbitration for unpaid legal fees against Petitioners. Quinn Emanuel seeks 20 percent of the a settlement, the value of which it bases on a \$35.90 per share value of Facebook stock as of February 22-23, 2008. Petitioners maintain that

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<sup>1</sup> Facebook explains that Petitioners petitioned the Northern District of California for "all documents concerning any valuation made or in effect after September 1, 2007, of Facebook or any shares of Facebook stock, including valuations implicating or concerning Internal Revenue Code § 409A" (October 16, 2009 Affidavit of Jonathan Bach ("Bach Aff") Ex A at 2).

the value of the settlement with Facebook was much lower than the value claimed by Quinn Emanuel, based on valuations of Facebook's common stock performed for Facebook in compliance with federal and state statutes.

In the arbitration, Petitioners asserted counterclaims against Quinn Emanuel including a claim for malpractice. Petitioners allege, *inter alia*, that Quinn Emanuel was negligent in its failure to obtain recent valuations of Facebook's common stock or to advise Petitioners that Quinn Emanuel had in its possession during the mediation at least three prior 409A valuations of Facebook's common stock, all of which established a value for Facebook stock well below the \$35.90 per share value claimed by Quinn Emanuel. Petitioners allege that Quinn Emanuel's negligence was a direct and proximate cause of tens of million of dollars in damages, plus additional amounts to be determined at the arbitration.

Petitioners argue that the true value of Facebook stock at the time of the mediation is a critical issue in the arbitration, both with respect to Quinn Emanuel's claim for attorneys' fees and with respect to Petitioners' counterclaim for damages. Petitioners argue that any fee to which Quinn Emanuel might be entitled will be far closer to the \$7.75 per share valuation than under a \$35.90 per share valuation.

Petitioners also argue that Quinn Emanuel's expert's report attacks the significance of the \$7.75 per share valuation verified by Facebook pursuant to 409A and CCC 2512(o). Quinn Emanuel's expert states: "In my experience, tax value – like balance sheet value – is often at odds with market value, even when the tax or balance sheet value purports to be at market" (10/01/09 O'Shea Aff Ex H, at 11). Petitioners' argue that this and similar statements by Quinn Emanuel's expert implies that Facebook "committed fraud, or at least Facebook's 409A

valuations are not true, objective valuations of its stock” contrary to 409A’s mandate that valuations must reflect the fair market value of a company’s stock (10/01/09 O’Shea Aff Ex ¶ 22). For these reasons, Petitioners seek to compel compliance with a number *subpoenas duces tecum* against Facebook, Houlihan and Microsoft seeking information concerning the valuation of Facebook equities and Facebook’s business plans.

#### *Facebook Valuation Subpoena*

On September 14, 2009, the arbitration panel issued a *subpoena duces tecum* directing Facebook to appear before the arbitration panel and to produce documents related to Facebook valuations from 2004 to the present (“Facebook Valuation Subpoena”). On September 18, 2009, the arbitration panel issued a second subpoena directing Facebook to appear and produce certain documents on a hard drive or, if Facebook does not have the documents, a copy of the hard-drive referred to as “Device 371-01” (“Facebook Device Subpoena”; *see* Discussion III(B), *infra*).

Specifically, the Facebook Valuation Subpoena commands Facebook to appear on September 22, 2009 and bring and produce the following:

- (1) All 409(A) valuations of Facebook.
- (2) Documents sufficient to show any and all valuations of Facebook from 2004 to present.

(10/01/09 O’Shea Aff Ex S at 4).

Petitioners explain that they are entitled to documents from Facebook that (1) show the results of any 409A or other valuations performed on its behalf from 2004 to present; (2) demonstrate any 409A or other valuations performed on its behalf were rigorous, objective, derived in good faith, and were not in any way skewed to gain undue tax advantages; and (3) demonstrate that any information by Facebook to firms performing valuations was accurate and

provided in good faith.

### *Houlihan Valuation Subpoena*

Houlihan is a provider of financial advisory services. Such services include fairness and solvency opinions, valuation opinions and financial consulting (Affidavit of Jennifer Muller [“Muller Aff”] ¶ 2). Houlihan has provided annual tax-related valuation services to Facebook since 2006 (*id.* ¶ 6).

On August 11, 2009, the arbitration panel issued a *subpoena duces tecum* commanding Houlihan to appear on September 11, 2009 and produce documents that:

- (1) show the terms and value of all offers, transfers, and sales of Facebook stock from 2004 to present.
- (2) show any and all valuations of Facebook stock, individually and/or collectively, of any class, series, or any classification, at any time.
- (3) show any and all valuations of any and all equity, debt or other assets owned by Facebook from 2004 to present.
- (4) all 409(A) valuations of Facebook.
- (5) show any and all valuations of Facebook from 2004 to present.
- (6) show any and all debt and/or equity investments in Facebook by various investors.
- (7) show debt and equity capitalization of Facebook from 2004 to present.
- (8) all financial statements for Facebook from 2004 to present.
- (9) all business plans for Facebook.

(September 21, 2009 Affirmation of Sean O’Shea [“9/21/09 O’Shea Aff”] Ex Q [“Houlihan Subpoena”] at 4).

### *Microsoft Valuation Subpoena*

Petitioners explain that Microsoft’s 2007 investment in Facebook was in exchange for preferred shares of stock, not common shares. Petitioners assert that the alleged \$15 billion valuation used by Microsoft and the \$35.90 per share that Microsoft reportedly paid for preferred stock in Facebook, are not valid data points for determining the value of the common stock at

issue in the ConnectU-Facebook settlement.

Petitioners also explain that the shares of stock received by Microsoft likely contained valuable liquidation preferences that Petitioners' common stock does not contain, and that in exchange for its investment in Facebook, Microsoft likely received additional consideration, such as an advertising partnership.

Quinn Emanuel suggests that it negotiated certain anti-dilution characteristics for Petitioners' stock similar to anti-dilution protections carried by Microsoft's Facebook stock, and that Petitioners' stock is a hybrid stock that carries a pricing premium. Petitioners valuation expert has opined that the value of such characteristics by no means bridges the differences between \$7.75 per share value filed pursuant to CCC 25102(o) and the \$35.90 per share value claimed by Quinn Emanuel and based on the purported value paid by Microsoft.

On August 11, 2009, the arbitration panel issued a *subpoena duces tecum* commanding Microsoft to appear on September 11, 2009 and produce documents that:

- (1) show all offers, transfers, purchases, and sales of Facebook stock from 2004 to present.
- (2) show any and all valuations of Facebook stock, individually and/or collectively, of any class, series, or any classification, from 2004 to present.
- (3) show any and all valuations of Facebook from 2004 to present.

(9/21/09 O'Shea Aff Ex R ["Microsoft Subpoena"] at 4).

Petitioners explain that they are entitled to documents from Microsoft that: (1) discuss the particular characteristics of the stock it received from Facebook in 2007; (2) demonstrate the valuation used in connection with the issuance of such stock and the accuracy of such a valuation; (3) and discuss the existence of any ancillary agreements or additional consideration

that may bear on the value of the Facebook equity received by Microsoft.

## DISCUSSION

### I. Removing ConnectU from this Proceeding

As a preliminary matter, Petitioners request that the Court remove ConnectU as a party to this proceeding pursuant to CPLR § 1003 because ConnectU is no longer a party to the arbitration. According to CPLR § 1003: “Parties may be dropped by the court, on motion of any party or on its own initiative, at any stage of the action and upon such terms as may be just.” There is no objection to Petitioners’ request. As ConnectU is no longer a party to the arbitration, it is just and appropriate to remove ConnectU from this proceeding.

### II. Arbitrator’s Authority to Subpoena Third-parties under the Federal Arbitration Act

It is well-established that New York courts favor and encourage “arbitration as a means of conserving the time and resources of the courts and the contracting parties” (*Smith Barney Shearson Inc. v Sacharow*, 91 NY2d 39, 49 [1997], quoting *Matter of Nationwide Gen. Ins. Co. v Investors Ins. Co.*, 37 NY2d 91, 95 [1975]). Arbitration does not generally involve the broad type of discovery favored in litigation,<sup>2</sup> and “court-ordered discovery is not available in arbitration proceedings ‘except under extraordinary circumstances’” (*Platzer v Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 2003 NY Misc. LEXIS 2001, at \* 7-8 [Sup Ct, NY County Oct 2, 2003], quoting *DeSapio v Kohlmeyer*, 35 NY2d 402, 406 [1974]).<sup>3</sup>

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<sup>2</sup> In *COMSAT Corp. v NSF*, the Fourth Circuit explained, “[a] hallmark of arbitration -- and a necessary precursor to its efficient operation -- is a limited discovery process” (190 F3d 269, 276 [4th Cir 1999]).

<sup>3</sup> As the Court of Appeals further explained in *De Sapio v Kohlmeyer* (35 NY2d 402, 406 [1974]):

Petitioners, ConnectU and Quinn Emanuel agreed to arbitrate their dispute under the Commercial Rules of the American Arbitration Association (“AAA”) before three arbitrators appointed from the AAA’s Large Complex Commercial Case Panel,<sup>4</sup> and that the arbitration is to be “governed by both the procedural and substantive provisions of the Federal Arbitration Act” (*Connectu*, 2008 NY Slip Op 52042U, at \* 2). Thus enforcement of the third-party subpoenas is governed by the provisions of the FAA (*Imclone Sys. v Waksal*, 22 AD3d 387, 388 [1st Dept 2005]; *see also Fletcher v Kidder, Peabody & Co.*, 81 NY2d 623, 631 [1993]).

Section 7 of the Federal Arbitration Act (“FAA”) provides that arbitrators “may summon in writing any person to attend before them . . . as a witness and in a proper case to bring with him or them any book, record, document, or paper which may be deemed material as evidence in the case” (9 USC § 7). According to the parties, the only New York State court decision interpreting section 7 of the FAA is the First Department opinion in *Imclone Sys. v Waksal* (22 AD3d 387, 388 [1st Dept 2005]). In that case, citing to the Fourth Circuit decision in *COMSAT Corp.* (190 F3d at 276-277), the Appellate Division held that “depositions of non-parties may be

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The availability of disclosure devices is a significant differentiating factor between judicial and arbitral proceedings. It is contemplated that disclosure devices will be sparingly used in arbitration proceedings. If the parties wish the procedures available for their protection in a court of law, they ought not to provide for the arbitration of the dispute. Under the CPLR, arbiters do not have the power to direct the parties to engage in disclosure proceedings. While a court may order disclosure “to aid in arbitration” pursuant to CPLR 3102, it is a measure of the different place occupied by discovery in arbitration that courts will not order disclosure “except under extraordinary circumstances.”

(*Id.* [quotations and citations omitted]).

<sup>4</sup> The AAA Commercial Rules do not provide guidance on how third-parties may move to quash subpoenas issued by AAA arbitrators, nor do the AAA Commercial Rules instruct parties on procedures for enforcement of non-party subpoenas.

directed in FAA arbitration where there is a showing of ‘special need or hardship,’ such as where the information sought is otherwise unavailable” (*id.* [citations omitted]).

Since the *Imclone* decision, the Second Circuit Court of Appeals issued a decision in *Life Receivables Trust v Syndicate 102 at Lloyd’s of London* (549 F3d 210, 212 [2d Cir 2008]) that leads to a contrary result. The Second Circuit held that “section 7 does not enable arbitrators to issue pre-hearing document subpoenas to entities not parties to the arbitration proceeding” (*id.*). Accepting the holding and reasoning put forward in the Third Circuit’s decision in *Hay Group, Inc. v E.B.S. Acquisition Corp.* (360 F3d 404, 411 [3d Cir 2004] [examining the “plain meaning” of section 7 of the FAA]), the Second Circuit held that section 7 of the FAA empowers arbitrators to subpoena non-parties to provide testimony at an arbitration hearing and “order ‘any person’ to produce documents so long as that person is called as a witness at a hearing” (*Life Receivables*, 549 F3d at 218; *see also Hay Group*, 360 F3d at 411 [“In sum, we hold that the FAA did not authorize the panel to issue a pre-hearing discovery subpoena to [non-parties]. We further reject any ‘special needs exception’ to this rule.”]). As the courts explain, the *Life Receivables* and *Hay Group* decisions are consistent with efficiency considerations generally associate with policies favoring arbitration (549 F3d at 216, n 9).<sup>5</sup>

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<sup>5</sup> As the Second Circuit noted, the Fourth and Eighth Circuits have reached different results. While noting that the FAA does not “explicitly authorize the arbitration panel to require the production of documents for inspection by a party” (*In Re Sec. Life Ins. Co. of Am.*, 228 F3d 865, 870-871 [8th Cir 2000]), the Eighth Circuit held that “implicit in an arbitration panel’s power to subpoena relevant documents for production at a hearing is the power to order the production of relevant documents for review by a party prior to the hearing” (*id.*). The court reasoned that “efficiency is furthered by permitting a party to review and digest relevant documentary evidence prior to the arbitration hearing” (*id.*).

The Fourth Circuit held that “a federal court may not compel a third party to comply with an arbitrator’s subpoena for pre-hearing discovery, absent a showing of special need

The *Life Receivables* decision, although not binding on this Court, changes the landscape from which the *Imclone* decision was made and from which to interpret it. In *Imclone*, the First Department looked to the Second Circuit for authority and specifically noted that the Second Circuit had not ruled on the question of “whether prehearing nonparty depositions are authorized under the FAA” (22 AD3d at 388, citing *Natl. Broadcasting Co., Inc. v Bear Stearns & Co., Inc.*, 165 F3d 184, 188 [2nd Cir 1999]). The First Department went on to explain that in the absence of “a decision of the United States Supreme Court or unanimity among the lower federal courts,” it was “not precluded from exercising [its] own judgment” (22 AD3d at 388, citing *Flanagan v Prudential-Bache Secs., Inc.*, 67 NY2d 500, 506 [1986]).

The impact of the *Life Receivables* decision is significant because the subpoenas at issue in the instant matter seek the type of discovery specifically prohibited by the Second Circuit’s decision -- that is, pre-hearing document production from a non-party. Although the subpoenas are worded to direct Microsoft, Houlihan, and Facebook to “appear,” the subpoenas do not designate or identify a witness from whom it seeks testimony. The title of “Subpoena Duces Tecum” further implies that the request is specifically for the production of documents and not

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or hardship” (*COMSAT Corp. v NSF*, 190 F.3d 269, 276-278 [4th Cir 1999]). The court also noted that the FAA does not explicitly grant “an arbitrator the authority to order non-parties to appear at depositions, or the authority to demand that non-parties provide the litigating parties with documents during pre-hearing discovery”(id.). Rather, according to the Fourth Circuit, “the FAA’s subpoena authority is defined as the power of the arbitration panel to compel non-parties to appear ‘before them;’ that is, to compel testimony by non-parties at the arbitration hearing” (id.). The court was persuaded by the argument the in complex cases “the much-lauded efficiency of arbitration will be degraded if the parties are unable to review and digest relevant evidence prior to the arbitration hearing”(id.). For that reason, *inter alia*, the Fourth Circuit determined that upon the “showing of special need or hardship,” a party may “petition a district court to compel pre-arbitration discovery” (id.). The court did not define “‘special need’ . . . except to observe that at a minimum, a party must demonstrate that the information it seeks is otherwise unavailable” (id.).

for testimony (*see* CPLR § 2301 [“A subpoena duces tecum requires production of books, papers and other things.”]). Additionally, the subpoenas seek production of documents on September 11, 2009 and September 22, 2009, well before the October 26, 2009 start date for the arbitration hearing.

The hardline rule of the Second Circuit permitting document discovery of non-parties only when it is part-and-parcel of the non-parties’ giving of testimony at an arbitration hearing is at odds with the First Department’s decision in *Imclone*. While the First Department recognizes the persuasiveness of Second Circuit decisions on this issue, its citation to the Fourth Circuit decision in *COMSAT Corp.* (190 F3d at 276-277) makes clear that the law in the First Department is that under the FAA a court may compel compliance with arbitrators subpoenas for pre-hearing depositions and document discovery if a “special need or hardship” exists (22 AD3d at 388).<sup>6</sup> This legal discrepancy between the First Department and Second Circuit, however, does not affect this Court’s ultimate decision on these motions. As explained below, even under the more liberal standards enunciated by the First Department, Petitioners have not met their burden of establishing special need or hardship necessary to justify granting Petitioners’ motions to compel (*Imclone*, 22 AD3d at 388).

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<sup>6</sup> The First Department decision in *Minerals & Chemicals Philipp Corp. v Panamerican Commodities* (15 AD2d 432, 433 [1st Dept 1962]) does not resolve the issue. As explained in *Minerals*, under the New York Civil Practice Act “arbitrators have the power to summon witnesses, and, in a ‘proper case’, to require production of books and records” (*id.*). Therefore, if this case were decided under the CPLR, this Court would still be required to determine whether this is a “proper case” and whether the documents sought are confidential or privileged (*id.* at 434).

### III. Special Need or Hardship

#### A) *Valuation Subpoenas*

The Microsoft and Houlihan subpoenas, along with the September 14, 2009 Facebook Subpoena, all seek information concerning the valuation of Facebook stock and all three respondents object to the production based on claims of confidentiality and privilege. Although the arbitration panel has made a decision to subpoena the requested information, the question of “whether particular documents called for may be of a confidential and privileged nature . . . is entitled to a judicial determination without advance disclosure to the arbitrators” (*Minerals & Chemicals Philipp Corp. v Panamerican Commodities*, 15 AD2d 432, 434 [1st Dept 1962]).

“[D]ue in part to the important public benefits in protecting trade secrets, the liberal discovery rules are modified when trade secrets are sought to be discovered” (*Curtis v Complete Foam Insulation Corp.*, 116 AD2d 907, 909 [3d Dept 1986], *citing Matter of New York Tel. Co. v Public Serv. Commn.*, 56 NY2d 213, 219 [1982]). “When a party attempts to avoid discovery by asserting that the information sought is privileged as a trade secret, a minimum showing is necessary to substantiate the assertion” (*Curtis*, 116 AD2d at 908, *citing Rooney v Hunter*, 26 AD2d 891 [1966]; *Interstate Cigar Co. v I.B.I. Sec. Serv.*, 105 Misc 2d 179, 183 [1980]).

The burden then shifts to the party seeking disclosure to show that “the information demanded appears to be indispensable to the ascertainment of truth and cannot be acquired in any other way” (*AIN Leasing Corp. v Peat, Marwick, Mitchell & Co.*, 166 Misc 2d 902, 904 [Sup Ct, NY County 1995], *citing Deas v Carson Prods.*, 172 AD2d 795, 796 [1991]; *see also Drake v Herrman*, 261 NY 414 [1933]). “Where disclosure is essential to ascertaining the truth the privilege must give way. . . . But, even then, appropriate procedures should be adopted to insure

that unessential information is not unnecessarily disclosed, to the possible advantage of competitors” (*Minerals & Chemicals Philipp Corp.*, 15 AD2d at 434, *citing Drake v Herrman*, 261 NY 414, 418 [1933]).

The standard is particularly high when, as here, the confidential information is sought from a non-party. As explained in *Frates v Pantry Pride, Inc.* (1985 US Dist LEXIS 15615 [SD NY Sept 25, 1985), “courts have repeatedly resisted efforts to utilize the liberal federal discovery rules for the purpose of gaining access to proprietary, confidential business information from third parties who have no interest in the litigation.” This is especially true where the disclosure of the subpoenaed information could place a non-party at a competitive disadvantage and damage the party’s business (*Cohen v City of New York*, 255 FRD 110, 119 [SD NY 2008], *citing Gonzales v Google, Inc.*, 234 FRD 674 [ND Cal 2006]).

The documents requested from Microsoft include offers, transfers, purchases, and sales of Facebook stock from 2004 to present; valuations of Facebook stock, individually and/or collectively, of any class, series, or any classification, from 2004 to present; and valuations of Facebook from 2004 to present. As argued by Microsoft, this includes sensitive competitive information. Microsoft substantiates its claims that it has not shared this information with anyone outside of Microsoft, even Facebook, and that details concerning its approach, strategies, market analyses and any analysis of value it may have conducted related to its deal with Facebook have remained confidential (Affidavit of Hayden Odell ¶ 7). Microsoft further claims that the methodology for assessing the value of companies are closely tied to how Microsoft formulates its strategy and approach to the market (*id.* ¶ 6). Microsoft explains that it implements procedures to maintain the confidentiality of this type of information and disclosure

would harm Microsoft with future business partners as well as Facebook (id. ¶ 4). Microsoft has met its burden of establishing that the information sought is privileged.

The documents requested from Houlihan includes any and all Facebook financial or investor information from 2004 to present. Houlihan alleges that the requested materials are confidential and proprietary, subject to nondisclosure and confidentiality restrictions aimed at protecting client information (Muller Aff ¶¶ 3-5). This includes annual tax-related valuation services, that result in valuations filed with the IRS and the California State Department of Corporations. Concerning the documents sought from Houlihan, Facebook argues that this information is extremely sensitive competitive information, not shared outside of Facebook, most of which is subject to Non-Disclosure Agreements, and includes valuations, including methodologies, deal comparisons, strategies, and market analyses that have remained confidential. Houlihan has met its burden of establishing that the information sought is privileged.

The documents requested from Facebook in the September 14th Subpoena include all 409A and other valuations of Facebook from 2004 to present. Facebook argues that this information is proprietary valuation and strategic information that, if disclosed, would harm Facebook with respect to future business partners. The information would reveal how Facebook values its own performance and could be used in numerous competitive environments against Facebook by competitors, which formerly included Petitioners themselves.

The Court finds that the recent Southern District decision in *Solow v Conseco, Inc.* (2008 US Dist LEXIS 4277 [SD NY 06-Civ-5988, Jan 18, 2008]) is instructive in this matter. In *Solow*, the plaintiff alleged that the defendants engaged in a sham auction to establish the price at

which a piece of real estate would be sold to the defendants' favored bidder. The plaintiff thereafter commenced an action for breach of duty and sought a declaratory judgment setting aside the sale of the property. Plaintiff issued a subpoena to the third-party bidder demanding "all documents and communications concerning any loan, debt or obligation" secured by the property. The third-party filed a motion to quash the subpoena. In granting the motion, the court noted:

In short, the documents sought in the subpoena have little or no relevance to the claims and defenses in this action, while having potential value to [the plaintiff] in his contemporary competitive relationship with [the third-party], a non-party to this litigation. Weighing this against [the third-party's] legitimate interest in maintaining the confidentiality of proprietary documents bearing on his assets and financial plans, the Court concludes that the motion to quash the subpoena should be granted.

(*Solow*, 2008 US Dist LEXIS 4277, at \* 15).

As in *Solow*, the information Petitioners seek through the non-party valuation subpoenas has "potential value" to competitors, including Petitioners. In fact, while it appears that Petitioners' litigation with Facebook is complete, Petitioners continue to argue, even before this Court, that the settlement of copyright infringement and misappropriation of trade secrets litigation is not enforceable and was fraudulently induced (10/04/09 O'Shea Aff ¶ 15). Thus the non-parties have significant and legitimate interests in continuing to protect the confidentiality of their financial and business records from the scrutiny of Petitioners.

Petitioners cannot establish a "special need or hardship" sufficient to require these non-parties to provide documents containing confidential financial and proprietary information. Petitioners do not argue that "the information demanded [is] . . . indispensable to the ascertainment of truth and cannot be acquired in any other way" (*AIN Leasing*, 166 Misc 2d at

904); rather, Petitioners simply argue that their expert can “render a stronger expert opinion” (10/05/09 Tr at 26) or “believes he can greatly amplify and greatly improve” (10/05/09 Tr at 11) the report with the confidential information sought (10/01/09 O’Shea Aff Ex E at ¶ 32).<sup>7</sup> In the current report, Petitioners’ expert explains the scope of publicly available information, including 409A Valuations, Sharepost.com listings, and analysts’ reports and estimates of value (*id.*). Because of such available information, according to their expert, the lack of the valuation information requested from Microsoft, Houlihan, and Facebook, does not preclude him from rendering an opinion as to the value of Facebook common stock in 2008 (*id.* at 33).

Private parties are free to value transactions based on the price of any entity, public or private, and the mere fact that the value of the entity is subject to a good faith dispute does not give such private parties the right to drag the non-party into disclosing confidential information.<sup>8</sup> However useful confidential proprietary business information would be to outside analysts would not give them the right to request such information from third-parties, even if they structured a deal around the pricing of this third-party’s equities. Quinn Emanuel’s purported reliance on the public announcement of the Microsoft deal does not justify Petitioners’ intrusive discovery into sensitive and confidential information. If either party submits the press release as evidence of value, then both parties should deal with the press release on its own terms. The information sought is privileged and confidential, of significant strategic value to the third-parties, and not

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<sup>7</sup> Petitioners have not argued that Quinn Emanuel has access to this information or that Quinn Emanuel has not provided them with all the information from which its expert derived his or her opinion.

<sup>8</sup> It is undisputed that not one of the non-parties subpoenaed have any claims or are implicated in any way in the transaction between Petitioners and their former counsel.

necessary for Petitioners' arbitration (*Fazio v Federal Express Corp.*, 272 AD2d 259, 260 [1st Dept 2000]). Petitioners have not established a special need or hardship sufficient to justify this Court to compel disclosure of the confidential valuation materials (*Imclone*, 22 AD3d at 388).

B) *Subpoena for Device 371-01*

On September 18, 2009, the arbitration panel issued a *subpoena duces tecum* commanding Facebook to appear on September 29, 2009 and produce:

- (1) All documents concerning or reflecting any use or plan to use any information or concept of any kind derived from or in conjunction with Cameron Winklevoss, Tyler Winklevoss, or Divya Narendra, or any actual or potential appropriation or theft of any such information or concept.

Limitations:

- This request is limited to messages to or from Mark Zuckerberg.
- This request is further limited to responsive documents concerning any actual or potential social networking website.
- This request is further limited in that the responsive documents sought were/are contained and/or located on the hard drive designated as device 371-01 in connection with the matter of *ConnectU, Inc v Facebook.*, 1:07-cv-10593(DPW) and 1:04-cv-11923(DPW)(D.Mass)

(November 4, 2009 Affirmation of Sean O'Shea ["11/04/09 O'Shea Aff"] Ex A

["September 18, 2009 Facebook Subpoenas"] at 4).

On October 8, 2009, the arbitration panel issued a Subpoena and Order commanding Facebook to appear on October 16, 2009 and produce:

- (1) Copies of the email from Jeff Parment to Neel Chatterjee attached as Exhibit C to Respondents-Counterclaimants' September 30, 2009.
- (2) In the event that Facebook (including but not limited to its attorneys, agents, affiliates, officers and/or directors (including but not limited to Mark Zuckerberg)) continues to claim that it does not have possession, custody, or control of a copy of the Documents [*sic*] specified above, Facebook shall appear before the Panel for a hearing and testimony in this

matter on October 16, 2009 and bring with it and produce to Respondents a mirror-image copy of the hard drive designated as device 371-01 in connection with the matter of *ConnectU v Facebook*, which copy shall contain the Documents that existed on the Drive at the time it was provided to Jeff Parmet for review in connection with the Massachusetts Litigation.

The Order further explains that the arbitration panel's intention in executing the subpoena was to secure production and testimony regarding the documents referenced in the unredacted version of the email from Jeff Parmet to Neel Chatterjee, attached as Ex C to Petitioners' September 30, 2009 letter (11/04/09 O'Shea Aff Ex B ["October 8, 2009 Facebook Order"] at 2-3).

The Facebook Device Subpoena and Order seek copies of certain documents found on device 371-01, which is the hard drive from Zuckerberg's personal computer while he was a student at Harvard University. These documents are inherently different than the valuation material discussed above. This evidence may have been at issue and/or produced during the Massachusetts litigation, but was not produced before Facebook and ConnectU reached a global settlement. Therefore, these requests seek to reopen discovery that was proceeding in the Massachusetts litigation. The Massachusetts Court entered a Stipulated Protective Order governing the use and disclosure of confidential materials, and Facebook presents a number of arguments concerning the Massachusetts Protective Order as to why this Court should not grant Petitioners' motion to compel compliance with these particular subpoenas.<sup>9</sup>

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<sup>9</sup> On November 13, 2009, Facebook served its opposition to Petitioners' November 4, 2009 motion to compel compliance with the two Device subpoenas. Facebook only served a redacted version of its memorandum in opposition on the Petitioners while submitting its unredacted memorandum to the Court. During a conference call, the Court suggested that a protective order governing the use of confidential materials filed with this Court would be appropriate. Despite numerous conferences, the parties were unable to agree on the scope of a protective order. Petitioners thereafter decided to submit its reply memorandum without the benefit of reviewing Facebook's unredacted opposition. While this issue would generally be of

The Court declines to grant the motion to compel compliance with the September 18, 2009 Facebook Subpoena and October 8, 2009 Facebook Order because it does not appear that Facebook is the proper party to be subpoenaed, and it does not appear that this Court has jurisdiction to compel the out-of-state non-parties, whether it be Facebook or Zuckerberg, to comply with the subpoenas.

First, Facebook claims that the device and its documents are the property of Zuckerberg, and that he may have independent privacy and privilege concerns. The District of Massachusetts protective order corroborates Facebook's statement and even Petitioners' concede that the device was Zuckerberg's personal property (Petitioners' Nov 25, 2009 Reply Memo at 4, n 3). Even though he is the CEO and a Founder of Facebook, Zuckerberg is entitled to maintain and protect separate property from the company. Petitioners' submissions' imply Facebook's receipt of these documents or a copy of Device 371-01 was subject to the protective order in the Massachusetts Litigation. The Court will not re-open discovery disputes that are properly before the Massachusetts court. Furthermore, Petitioners' arguments concerning Facebook's control over the documents or device are not persuasive. Contrary to Petitioners' position, the record does not demonstrate that the arbitration panel made any definitive ruling on this issue on whether Facebook properly protects Zuckerberg's property interests.

Second, there is a jurisdictional issue as to whether the Court has the power to compel a non-party located in California to testify at an arbitration in New York. Facebook explains that any witness called to testify and all the documents/devices sought would be in located in

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concern to the Court, none of the information redacted from Facebook's opposition is used or referenced in this decision and, thus, the issue is of no consequence.

California (Oct 9, 2009 Affidavit of Mark Howitson ¶ 19). This Court’s ability to compel a witness to testify is limited to witnesses located within New York State (*Matter of OxyContin II*, 2009 NY Slip Op 29062, 11 [Richmond Cty, Sup Ct Feb 10, 2009]). “In that event, a deposition may be conducted in the non-resident deponent’s home state on consent or by written questions under oath or with the assistance of the court by the issuance of a commission to conduct a deposition out of state or by letters rogatory, where this state court seeks the assistance of a sister state court to compel the out-of-state non-party to cooperate in taking a deposition” (*id.*, citing CPLR §3108; *see also New Bridgeland Warehouses, LLC v Home Depot U.S.A., Inc.*, 2009 NY Slip Op 51517U, 6 [NY Sup Ct 2009] [“To the extent that the production of any witnesses or documents located in New Jersey must be compelled, CPLR 3108 authorizes New York courts to issue a commission or letter rogatory to compel disclosure from out-of-state individuals.”]). Similarly, to the extent that the subpoenas are governed by the FAA, this Court’s power to compel does not reach the California parties (*Dynegy Midstream Servs. v Trammochem*, 451 F3d 89, 96 [2d Cir NY 2006]).

**CONCLUSION**

Accordingly, it is hereby:

ORDERED that petitioners' motion to remove ConnectU, Inc. as a party to this proceeding is granted; and it is further

ORDERED that a copy of this Order and Decision shall be served on Room 158 (Trial Support Office) in order to amend the caption to reflect the removal of ConnectU, Inc. as a petitioner in this matter; and it is further

ORDERED that petitioners' motion to compel Houlihan, Lokey, Howard & Zukin and Microsoft Corporation to comply with non-party subpoenas issued in the arbitration is denied; and it is further

ORDERED that petitioners' motions to compel Facebook, Inc. to comply with non-party subpoenas is denied.

This constitutes the decision and order of the Court.

**Dated: January 6, 2010**

**ENTER:**

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**J.S.C.**